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H.B. Chidlow  
F. Easton  
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I deem it a pleasure and an honor to be with you today and to have the opportunity to discuss with you some of the problems which we of the new Indonesia that is now emerging are facing that might be of interest to you, as well as the course of action we propose to pursue in our attempt to overcome these problems. I consider it especially an honor because I am aware of the substantial and longstanding interests some of you here have in various parts of the region in which Indonesia is situated, and even in my country itself.

I am sure that most of you are familiar with the dramatic events that have taken place in my country in the wake of the abortive coup d'etat now almost a year ago. These events have fundamentally changed the political climate and are bound eventually to lead to even more fundamental changes in the political conditions under which we will build and develop our country. They have also opened up an opportunity to come to grips, seriously and rationally, with the economic problems that beset us.

I am not giving you a piece of news when I say that the economy which we inherited was, and still is, in a deplorable state. This was accumulatively caused by the pursuit of incorrect policies based on an unrealistic order of priorities, an incredible degree of governmental mismanagement and unconcern for good government as well as by the fact that the Indonesian Communist Party over a prolonged period tried to use its stranglehold on the economy as a political lever in order to gain effective governmental power.

At this moment our economy shows the usual characteristics of a country with intensive inflation. Soaring prices to the degree of 10 to 20% a month, dwindling foreign exchange reserves, confused price structure affecting the export sector. What makes it even worse in our case is, that our import capacity has decreased to so low a level as to cause bottlenecks all over our productive capacity, resulting in production at a level of 30 to 40% only of capacity.

I intend to discuss some of these aspects in more detail in order to have a realistic base-line from which to start considering our plans for economic rehabilitation and stabilisation, and to enable you to orientate yourself realistically with regard to the possible implications and opportunities this may have for your interests in my country as well as in the general area in South East Asia. You are undoubtedly aware of the direct relationship that exist between the success of our endeavours to achieve economic stabilisation and rehabilitation, and the possibility of building a democratic Indonesia. Likewise of the relation-



ship between a democratic Indonesia and the general stability and security of South East Asian region.

It is on this common awareness as a basis that I am now asking your indulgence in having a closer look at some of our problems.

The present economic situation.

For the last seven years the economy of Indonesia has been steadily deteriorating at an increasingly rapid pace, bringing along abysmal discrepancies between the incomes of the different groups in our country. Figures will show you the increase of the price level, the decrease of exports, the decrease of Government revenues, the money circulation and so on, but the labourers, civil servants, members of the armed forces, in short all people with fixed incomes will tell you more lively - if you would be able to listen to them - the daily hardships, the impossibility to keep both ends meet, the lack of medicines and all those things which represent our minimum demands in life.

The decrease of the purchasing power of the rupiah, or, which is the same, the purchasing power of our people, is a direct consequence of the raging inflation. Certainly, we have experienced inflation since 1950, but the price increase during the years 1950 - 1958 are negligible, compared to the increases since 1959. Taking 100 as the cost of living index for 1957, this became 348 for 1960, but reached the figure of 36.000 in 1965 and 160.000 at the end of July 1966.

The main economic factors which caused this price increase are the flow of money and the flow of goods. Indonesia's economy has been characterized by an increase of the flow of money, totally unbalanced by a corresponding flow of goods, while the difference between both increases became greater and greater. While at the end of 1955 the money in circulation amounted to Rp. 12 billion and at the end of 1960 to Rp. 48 billion, this figure became Rp. 2.718 billion at the end of 1965. At the end of July 1966 there was Rp. 10.000 billion in circulation.

The continuous increase of the money in circulation, especially after 1960, has been mainly caused by the deficit on the Government's budget, which also increased at a fast rate. In 1961 the deficit amounted to Rp. 23 billion and increased to Rp. 1.500 billion in 1965.

Government's revenues and expenditures naturally went up simultaneously with the price increases, but the velocity of the increase of expenditures exceeded by far that of revenues. While in 1960 Government revenues amounted to 13.6% of the Gross National Product, this percentage decreased to 1.5% in 1965.

At the same time the pattern of expenditures also changed. More and more expenditures were directed towards projects, which did not immediately increase



the flow of goods or services in the society. This expenditure pattern was a direct consequence of the scale of national priorities, expressing the preferences of the national leadership at that time.

The lack of corresponding increase in Government revenue is a direct result of the incompleteness of our tax structure. Potential sources for tax assessments are not properly tapped, while the tax laws offer enough loopholes for tax evasion on a grand scale. Moreover the main source of Government revenue is the tax on foreign trade. As foreign trade decreased rapidly revenue based on foreign trade declined accordingly.

The previous policy of making "non-developmental oriented expenditures", and the neglect of the revenues, was based on the fallacy, that inflation caused by a budget deficit is not dangerous and that Government's deficit can be financed by printing money and bringing more of it in circulation. For this basic mistake the previous authorities and Indonesia are now paying a very heavy price.

While money in circulation increased, such was not the case with the flow of goods. The production of certain domestic goods increased steadily, especially in the agricultural sector. However, the production was not in balance with the flow of money which exceeded it by far. In the industrial sector however there was a sharp decline in the production of domestically made goods, as in almost all of these industries import of raw material is a necessary factor. The high velocity of the inflation resulted in a decline of the real exchange rate of the rupiah, which again resulted in a decrease of exports. The total amount of exports (oil excluded) once amounted to US \$ 900 million in 1951. It decreased until US \$ 775 million in 1955, decreased further until it reached the amount of US \$ 601 million in 1960, while in 1965 it only amounted to US \$ 424 million.

This decrease of exports was the result not only of lack of incentives for the exporters, but was also caused by physical and administrative impediments. Regulations on exports became more and more complicated and the breakdown of the transportation system hampered exports substantially.

As exports declined, foreign exchange earnings of the country decreased accordingly. Consequently the country's capacity to import goods decreased also. However, total import figures show that imports have not had a tendency to decline. While in 1955 imports amounted to US \$ 499 million (without oil), in 1966 it amounted to US \$ 664 million and in 1965 US \$ 550 million. This has only been made possible by foreign credits. Foreign loans increased continuously and at the end of 1965 amounted to round US \$ 2.4. billion.



In having our economic existence depend upon foreign loans the Indonesian authorities at that time obviously presumed that there would be no repayment problems. Exports for 1966 have been estimated to be round US \$ 360,- - 400 million, while payment of the installments of the foreign loans and interest would amount to US \$ 530 million (in this figure is included US \$ 157 for short term credits, while the rest consists of middle term and long term credits).

Moreover, these loans were not used to increase production within a short time, so that they did not assist in increasing the capacity for repayment.

One of the main reasons for the price increases has been that services have become more and more inadequate. The decline of the productivity of the means of transportation has been caused by the lack of spareparts and lubricants, while the usefulness of the transportation means has greatly suffered from the condition of the roads, which became worse and worse. Sea transportation and harbour facilities are far from efficient, while river transportation has still to be developed. Telecommunication, which is the main service in trade, cannot yet provide the services it is expected to supply. All these factors have contributed to the inflationary spiral and the rapid and continuous rise of the price level.

These are the several factors which have caused the immense deterioration of the Indonesian economy. I have tried to enumerate them briefly here and to show how closely interrelated they are. For most of you these are of course well known things. What I wanted to point out is however, that we can only overcome the present problems, if we consider them as one integrated whole.

There also exist a close relationship between economic and non-economic factors, and I mean especially the political and mental factors. I will deal with these later on.

The economic developments in 1966 too give rise to grave concern. In the first half of the year the cost of living increased with 400%. If this trend continues, it will mean that inflation will reach a height of 1000% at the end of this year. This will have of course serious consequences. It is bound to lead to further demoralisation of the bureaucratic apparatus of the government, to general despair and to even more wide-spread corruption, and might even endanger the degree of political stability that at present exists.

The prospects for the future would therefore be bleak indeed, but for the emergence of new political and psychological factors in the present situation.

THE NEW OUTLOOK.



### THE NEW OUTLOOK.

It would be quite difficult to overestimate the changes that have taken place in the political climate during the last half year. The yearning for more freedom, the demand for better government and for more rational leadership, long suppressed, has now finally broken its bounds. Responding to this new wave, vigorously carried through by a new generation, the *Madjelis Permusjawaratan Rakjat Sementara*, the ~~Rakyat~~ provisional Peoples Consultative Assembly, the highest legislative body in our political system, vested with the sovereignty of the people, set itself during its recent session two months ago, to issue directives for the restoration of democratic rights; the re-establishment of the rule of law, among others by re-establishing the independence of the ~~judiciary~~ judiciary from executive power ; by annulling the constitutional deviations in violation of the Constitution of 1945, and by ordering a review of all the Presidential decrees. It also ordered a reassessment of our international position with a view to break out from our isolation, and instructed the government to rejoin the U.N.

It set a new order of national priorities in which the rehabilitation and stabilisation of the economy figures high on the scale. In its "Decision on the Renovation of Economic, Financial and Developmental Policies" the People's Assembly stipulated that the economic democracy which should be striven for should be based on the "strength, initiative and creative capacity of every citizen", which should therefore be developed to its fullest extent. The role of the government is one of a supplier of ideas and guidelines, as well as of facilities to enable the people to develop their own initiative and to give guidance to these activities, so that they will be beneficial to the common welfare.

Changed is also the outlook with regard to foreign capital. While in the past foreign capital was regarded as an evil, the People's Assembly has stated explicitly the need for foreign capital, considering the limited supply of capital within our country.

The successful passage by the MPRS of these directives has given rise to a new hope and to new creative impulses. In consonance with these directives the present government - itself the product of a People's Assembly's directive - has put a speedy end to our confrontation policy with regard to Malaysia. We have rejoined the IMF, we have resumed our seats in the various specialized agencies of the U.N. And before long, we will have resumed our active membership in the U.N.

It is in this changed political climate, with its new hopes and energies, that it has become possible to think of a new and vigorous attack on the economic



problems that have beset us for so long, and to map out in a systematic fashion, the various steps that will have to be taken. And of these I want to speak to you now.

In the first place we will have to mount what might be called a rescue operation for the remaining part of this year, with a view substantially to reduce the sharply downwardmoving trend and to mitigate its social and political repercussions. This will also give us a chance to prepare the ground for the actual stabilisation and rehabilitation program that will have to be initiated in the beginning of next year. In this connection most needed will be the immediate supply of food and spare parts for transportation through stopgap credits. These credits will have to be realized - in order to be effective - before the end of this year. With the beginning of the next year the government hopes to be in a position to operate on the basis of its economic rehabilitation and stabilisation program, and to have secured parliamentary acceptance of its new bill on foreign investment.

I should like now to present to you the main features of this rehabilitation and stabilisation program.

#### BASIC CONCEPTS AND TARGETS OF THE SHORT TERM REHABILITATION AND STABILISATION PROGRAM.

The program is aiming at the following targets:

- a) to control inflation;
- b) to satisfy the need for food;
- c) to rehabilitate the economic services ;
- d) to increase export activities ;
- e) to satisfy the needs for clothing.

The order given here is also the order of priorities; the program also provides an opportunity to come to grips with various institutional problems, like the State Enterprises, with the problems of salaries, wages and fares. We are quite aware that the program we have worked out is neither perfect nor complete. Many data are lacking. However, while implementing the program we will improve it by bringing data in accordance with factual situations. The main importance of the program is, that it will serve as a guideline for action.



The short program comprises of (I) the economic rehabilitation program having as special targets:

- a) rehabilitation and increase of the productive capacity in the field of food-stuff, export and clothing ;
- b) rehabilitation and improvement of the economic services, which support the economic activities mentioned above.

And (II) the economic stabilisation program, having as special targets:

- a) to insure rupijah and foreign exchange financing to implement the rehabilitation program ;
- b) to control the inflation leading to price level and a price equilibrium which is relatively stable and in accordance with the purchasing power of our people.

In rehabilitating the economy we will consecutively endeavour to restore the capacities in the fields of food production, exports, clothing and services. The main impediments in our efforts to increase these capacities are the lack of raw material, spare parts and capital goods, which in fact means lack of foreign exchange and rupijahs.

However, in our effort to provide for foreign exchange we have to take into consideration our country's capacity and the necessity not to disturb the stabilisation program by the rehabilitation program. Therefore, in our attempts to attain these two targets, rehabilitation and stabilisation, we should be constantly aware of their close interrelationship and that any solution regarding one target cannot be its maximum solution, but will always <sup>be</sup> conditioned by the other.

Any economic measure has its effect on the political stability, which therefore also conditions those measures. In the implementation of the program we therefore have to act pragmatically and with great wisdom, without however abandoning the targets we have set.

As foreign exchange is the main limiting factor in the implementation of the program, we have put great stress on the increase of all activities leading to the increase of foreign exchange (exports) and to the savings of foreign exchange (by import substitution). We have - as I stated before - ~~gave~~ great confidence in the activity and initiative of our own people, if they are not hampered by Government regulations. Debureaucratization therefore will characterize the implementation of this program.

However, though we stress our people's auto-activity, we are quite aware that without foreign credits or other forms of assistance it will require more hardships from the people to get the program off the ground.



In drawing up the program we have also included as our aim the increase of our country's capacity for repayment of its debts, by giving the highest priority to the rehabilitation and expansion of the export sector.

Let me now say a few words about the program in the several fields of economic activity :

#### FINANCE:

As I said before, in the scale of priorities, control of the inflation is the main target. The starting point of the monetary program is to increase Government revenues up to 10% of the national income.

Governments expenditures have to be in accordance with the Government's capacity to collect its revenues, so that we have to break with our customary inclination to live beyond our means.

Basic in our program therefore is the increase of revenues and the limitation of expenditures and this basic concept expresses our determination to put our house in order.

The incredible amount of foreign debts forces us into austerity not only with regard to rupijah financing but the more so with regard to the use of foreign exchange. Every expenditure in foreign exchange has to be in accordance with the import planning, which forms the link between the monetary and the physical plan. By implementing the program in this way we ~~can~~ hope within a period of two years to be able to control the inflation. In this connection I want however to stress that we are not hoping for "economic miracles".

#### Food and Clothing production.

The population increase and the increased shift to rice in the diet of our people has caused the demand of rice to exceed production. All efforts will therefore be directed to the increase of rice production by using better seed, better planting methods and better agricultural extension methods.

The experience of the last eight years has shown that, without interference of the Government, rice production could increase to a great extent. We are therefore convinced that by the process of de-bureaucratizing, limiting the Government's role to the supply of seed, fertilizers, insecticides, agricultural implements and the dissemination of better agricultural methods, our farmers will be able to increase their rice production, so that there will be a substantial marketable surplus in the years to come.

With regard to clothing the program is aiming in the first place at the restoration of the productive capacity of the textile industry. Working at full



capacity however the industry will not be able fully to meet the people's needs. Textiles then will still be imported, but taking into account the depletion of foreign exchange reserves, the program does not envisage that the demand of our people will be fully met during these Program years.

#### ECONOMIC SERVICES.

Economic services are, as I said before in an intolerably bad shape. Trucks, buses and trains are only running at a small percentage of their capacity, because of lack of spare parts and lubricants. Many roads do not deserve that name or are even non-existent, terminals are broken down, the telecommunication system is far from adequate, the greater part of the merchant fleet cannot sail, again because of lack of spare parts and the lack of repair facilities.

The program aims at an adequate supply of spare parts and lubricants, so that all transportation means can be employed at full capacity, repair and restoration of the main roads and the railway tracks, terminals and harbours. Spare parts have also to be imported to restore the productive capacity of ~~the~~ the dredge fleet, so that rivers and irrigation canals can be deepened and sandbanks at the mouth of the several rivers, now hampering the export of valuable exportable products, can be dredged. The program further aims at a rapid restoration of the telecommunication system, which in its present state hampers the speed of transactions.

#### EXPORTS, IMPORTS AND FOREIGN EXCHANGE CONTROL.

The sharp decline of exports during the last years was caused by physical difficulties, the break down of the services but also by the multitude of regulations on foreign exchange control. Therefore the whole system of foreign exchange control will have to be overhauled, so as to make it easier to handle, both for the exporter as well as for the officials in charge of foreign exchange control.

As far as imports are concerned, the whole import program has to be geared towards the import of those goods necessary for the implementation of the rehabilitation and stabilisation program.

#### FOREIGN CAPITAL.

As I said before, foreign capital is no longer considered an evil, but welcomed as a necessary factor in the development of our country. We hope to attract as much foreign capital as possible.



I cannot give you the contents of the new investment bill, as this has not yet been submitted to Parliament, but I can spell out to you some of the underlying thoughts, on which there is a consensus in the Cabinet.

We are aware that we ~~kn~~ will have to compete with other developing countries. We are also well aware that the capital which is willing to invest in these countries is risk capital and that we have to reduce the risk burden. The Government hopes to create the conditions that will make it possible for foreign capital to have the confidence that it can work undisturbed in our country.

Besides the security of capital, there is full understanding within the Cabinet for the problems as seen from the foreign investor's standpoint, like transfer of profits, management, facilities, tax abatement and tax relief.

On the other hand, we from our side expect from the foreign investor that he will not confine his efforts to profit making for his own enterprise, but that he will constantly keep in mind the general development and welfare of our country, so that the enterprise he is working for will not be an isolated island of economic and technical progress within an ocean of backwardness and poverty.

In this connection an extremely useful contribution could for instance be made in the training of technical and managerial personell, so much needed for the growth of our economy.

4 in attracting foreign capital.

#### REGIONAL COOPERATION.

While fifteen, even ten years ago economic cooperation between the countries of the South East Asian Region was an academic problem, at present it represents an opportunity for these countries to speed up their development. We believe that a close cooperation between the countries of this region can assist us in the implementation of our short term and at a later stage with our long term program. Our neighbouring countries have much in common with our country, we are at about the same stage of economic development (except Japan), so that we can learn from their experiences, their monetary, agricultural, industrial problems, their problems with regard to their population increase, their problems with regard to foreign capital. We are restoring trade relations with Singapore and Malaysia, we have just recently concluded most fruitful talks with the Philippines on trade. We have always had substantial trade relations with Japan and Hongkong. We will continue and intensify all these relations and expand them to all countries in the region for our common welfare. In this connection I am fully aware of the interests many of you already have in several of the South East Asian countries. Regional cooperation, I venture to suggest, might therefore open up a new avenue for your participation in Indonesia's economic development.



POLITICAL STABILITY.

It is of course impossible to overlook the close interrelationship that exists between economic and political stability. In an unstable political situation economic stability can not be achieved, and vice versa. Fortunately however, the converse is also true : Every step toward political stability also means a step toward economic stability and vice versa. And this conviction is helping us in taking the first difficult steps. We have no illusions about the magnitude of the challenge we face. Essentially the question is : "Are the democratic forces in Indonesia at this stage strong enough to put Indonesia's house in order, to give new impulses to an economy that has ground to a standstill, and to create the conditions in which gradually democratic life will be possible?" The consequences of our success or failure will be great, not only to ourselves but also for the security and progress of the South East Asian area. We have no doubts about its final outcome. Our course is set, and though the difficulties will be tremendous, there is no turning back. And with hard work and perseverance, common sense, a clear vision of our goals, and with God's blessing, the short term objectives that I have outlined here, are not beyond our reach.

I have dealt here frankly and, I hope not too lengthily, with our problems and the ways we see to overcome them. I have done so, as you will be undoubtedly aware, in order to solicit your interest in what might in various ways be a ~~xxx~~ rewarding enterprise, but beyond this, also in the opportunity ~~to~~ participate in the great endeavour of the building of a new democracy.

September 1966.