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Economic Rehabilitation and Development

by Dr Azhari Zahri, Singapore

The Five Year Development Plan of the Suharto Cabinet was drafted in November, 1968, and was presented to Parliament for approval in January 1969. This is the fourth Indonesian development plan formulated since independence.

Indonesia started an Urgency Programme in 1950 which was succeeded in 1956 by a Five Year Plan and in 1961 by an Eight Year Plan. The Urgency Economic Programme, which puts the main emphasis on industrial development, failed to achieve its goals. The Five Year Plan of the National Planning Bureau was presented to Parliament for approval in May, 1956, but it did not receive formal approval until 1959. The Eight Year Plan which was drafted by the National Planning Council in 1961 met the same fate as the previous plan. The factors responsible for the failures in planning are, perhaps, common to less developed countries. Lack of capital, foreign exchange, technical skill, and managerial ability are among the barriers considered critical. However, political and social conflicts, corruption, and such economic disturbances as inflation resulting from chronic deficits in the government budget were equally responsible for the failures.

The Present Development Plan

The Suharto Cabinet claims that by 1969 its rehabilitation programme would have been concluded and hence the government must start its development programme this year. The assumption that the rehabilitation of Indonesian productive units and infrastructure has been completed seems to be a most naive and misleading contention.

It is true that efforts have been made by the present government to improve roads, harbours and irrigation especially on Java, but it is hard to believe that by 1969 the infrastructure and productive units which were neglected during the Sukarno regime have been rehabilitated.

The Five Year Plan of the Suharto Cabinet covers the period between 1969 and 1974 and will invest the amount of Rp 1,420 billion (about US \$ 3,500

million) of which almost 75 p.c. will come from the government¹.

Unlike the previous plans, the present development plan gives the highest priority to agriculture with the aim of increasing the nation's food production. The second highest priority is given to infrastructure, which accounts for about 30 p.c. of the total investment budget of the plan. The industrial and mining sector receives only 12 p.c. of total planned expenditures. While 9 p.c. of total budget of the plan will be spent on education, the defence sector receives less than 5 p.c. The plan reflects indeed the government's commitment to the nation's economic development.

Rehabilitation of Infrastructure

Investment capital is to be allocated for the development of infrastructure, i.e. electric power, irrigation, transport and communication projects.

The Sukarno administration had also aimed at laying the basis for a large-scale industrial development in Indonesia. Among ambitious targets formulated by Sukarno were the construction of 2,585 kilometers of new roads in addition to the 1,100 kilometer Sumatran Highway, an increase in electric output from 260 mw to 600 mw, the manufacture of trucks at a rate of 4,000 per year and an annual production of steel of 100,000 tons in 1968.

Other social overheads such as schools, hospitals, national theatres, museums, art galleries and various other cultural projects were also included in Sukarno's Eight Year Plan and took almost 10 p.c. of the total planned development budget. However, the implementation of the Plan was completely inconsistent. The government was more committed to the execution of President Sukarno's "prestige projects" such as national monuments, Ganefo Stadium, Konefo (new emerging forces), Political Venue project, and various military installations. These projects alone took

¹ Cf. Bappenas (National Planning Agency), Repelita (Five Year Development). The Plan consists of three volumes which are known as Appendix I, II and III of the Presidential Decree No. 319 of 1968.

no less than half a billion US dollars and were not a part of the Eight Year Development Plan.

Roads and Railways

The total length of roads in Indonesia is about 80,000 km, of which about 15,000 km are asphalted. By early 1966 it was estimated that no less than 75 p.c. of the total roads were in bad condition. The poor condition of the road system caused together with the lack of land transport facilities a rise in prices of export as well as consumer goods.

The railways have also been in poor condition. The only significant railway project carried out during the Sukarno administration was the 167 km track between the coal mine at Tanjung Enim and Kertapati in Palembang. This was completed at the end of 1963 with US financial and technical assistance.

Rolling stock was badly maintained and mechanical faults often caused a series of crashes and derailments. Between 1963 and 1964 no less than 2,000 units of rolling stock and vans were purchased. However, two-thirds of the total number of locomotives, vans and carriages have been operating for more than 40 years.

The improvement of the railways system has been handicapped by various factors. Apart from insufficient funds allocated by the government to this transportation system, an unrealistic fares policy, the permanent use of the railways system by the Public Work Department and Military Transport Service, and illegal passengers have been the major obstacles.

Sea Transportation

Sea transportation has also faced serious problems. Forced withdrawal of the Dutch fleet and personnel in 1958 confronted Indonesia with overwhelming problems. By charter and credit purchase the fleet problems were partly solved.

In 1961 the Indonesian merchant fleet had a total tonnage of 210,000 tons. By the end of 1965 Indonesia had more than 535 vessels of almost 500,000 tons. However, lack of trained mechanics and technicians to repair and maintain the ships and equipment, and lack of spare parts caused about half of the inter-island steamer fleet to be laid up. Poor condition of harbours and inefficient port procedures for loading and unloading cargo were also frequent causes for inefficiency in sea transport.

Against this gloomy background, any attempt to improve the present state of infrastructure by even only one-third would require a lion's share in the government investment budget.

In 1968 only Rp 8.6 billion or about 6 p.c. of the total budget were provided for the rehabilitation

of transport infrastructure; Rp 3 billion or a little more than 2 p.c. were allocated to the irrigation sector; and only Rp 5.1 billion or about 3 p.c. of the total budget were spent on the rehabilitation of power and other social overheads.

The new Five Year Development Plan makes, however, provision for the rehabilitation of infrastructure in the order of more than 20 p.c. of the total expenditure planned. The reconstruction of 11,000 kilometers and the up-grading of 6,000 km of road throughout the country, as drafted in the plan, are considered urgent, since the transportation of the export produce from rural areas to the ports has been impeded by the bad condition of roads.

Food Production

Between 1960 and 1967 the total production of rice increased by roughly 14 p.c. Since the population had increased by about 15 p.c. during that period, per capita production declined by 1 p.c. As a result of a drastic cut in rice imports—due to an overestimate of domestic rice production by the government in 1967—the per capita consumption declined to 91 kilograms in 1967, a level which is substantially below the one achieved in 1960². The failure of achieving the planned rice crop production and a reduction in rice imports raised the price of rice from Rp 7.92 per kg in January to Rp 26.40 in December, 1967, and hence stimulated the existing inflationary pressures. The failures of Sukarno's Eight Year overall Development Plan show quite clearly in this sector.

The Suharto Cabinet's Five Year Development Plan sets a target of raising the production of rice from an estimated level of 10.2 mn tons in 1968 to 15.4 mn tons in 1974. This is indeed a very modest target. However, in view of the present low level of rice price which is kept by the government at Rp 31.5 per kilogram, there is reason to believe that the production of rice will decline at least in 1969³. This contention is supported by the fact that in the past the rapid increase in rice output had a connection with a downward movement of the price of Indonesia's export products in the international market⁴. The connection between the rate of rubber output and rice production, for example, is primarily due to the fact that most smallholders who produce no less than 60 p.c. of the total rubber production in Indonesia do not devote all of their labour to rubber. They grow other crops,

² The per capita consumption of rice amounted to 100 kilograms in 1960.

³ Since to produce one kilogram of rice requires the cost of production of Rp 30, the profit left to the farmers is too small to provide incentive. For the estimates of cost of production of rice see Dr D. Kusnadi: "1969 Produksi Padi Akan Menurun", Indonesia Raya, Jakarta, December 26, 1968.

⁴ Azhari Zahri, Public Control and Economic Planning in Indonesia, Ph. D. Dissertation, mimeographed, Indiana University, Bloomington, 1964, p. 209.

primarily dry rice, at the same time. If the present upward trend in prices of export crops such as rubber, coffee, and pepper continues, there will be enough reason to believe that such a shift of productive resources would take place in the next future at the expense of rice production.

Agricultural Export Crops

Production of rubber, from which Indonesia earns almost one half of its export revenues, continued to suffer from insufficient replanting. It is true that the production of rubber had maintained its pre-guided economy level, but, in effect, more than half of all the country's rubber trees were over the normal age for cutting down⁵. In the long run, a constant neglect in replanting of rubber estates could easily lead to a decline in rubber production and export proceeds.

Production of sugar, too, suffered a setback. In 1966 production of sugar accounted for about 600,000 tons compared with 776,000 tons in 1965. In 1968 the production of sugar is estimated at around 700,000 tons, about one half of the pre-war level of production. There are various factors which caused a reduction in output, but the most important seem to be the condition of sugar factories and the government price policy.

Estate production of coffee and tea experienced no increase, while the smallholders' coffee and tea production increased rapidly. The upward movement of export prices of these crops seems to have made it possible for smallholder producers, especially those outside Java, to concentrate on the production of these crops in the past.

Like the past Eight Year Plan, the present Five Year Development Plan leaves the promotion of agricultural export production to individual exporters and export crop producers.

From the regional point of view an expansion of agricultural export production, especially by smallholders, could raise the standard of living of the people in the exporting islands. The continuous neglect in development of the smallholders export sector together with low export prices resulting from the government's unrealistic foreign exchange policy were responsible for a declining standard of living of smallholders in the leading export-producer islands during the Sukarno regime.

Strategy for Industrial Production

The ambitious industrial programme of Sukarno's Eight Year Development Plan failed to achieve its aims. Neglects in the agricultural export sector and existing mining industries caused con-

siderable difficulties in the balance of payments and handicapped industrial development. The lesson derived from the past experience forced the present government to change the strategy of its development plan. The strategy which gives a highest priority to the agricultural and mining sectors is not new, because it is precisely such a strategy which had been suggested by the former Minister of Finance and Governor of the Bank of Indonesia, Dr Sjafruddin Prawiranegara, almost 17 years ago⁶.

In 1967 the domestic output of textiles accounted for only 225 mn meters or about 2 meters per capita, and the government was forced to import about 525 mn meters to maintain the per capita consumption of textiles of 7 meters. The textile output increased from this level to about 325 mn meters in 1968, or by 40 p.c. Provision of priority to the textile industry in the present Five Year Plan is based upon the target that Indonesia must achieve an annual domestic production of 900 mn meters or the per capita production of 7 meters by the end of the plan period.

The success of the present development plan to achieve its target of textile production depends on two important factors. First, the rehabilitation of textile industries depends on the availability of sufficient foreign exchanges to import raw materials and spare parts for the industries. Secondly, it is determined by the government import (protection) policy and the willingness and the ability of the domestic textile producers to raise both the quality and quantity of their production. The failure of the domestic textile producers to respond to the government protection is likely to result in an increase of textile prices in Indonesia.

The declining export earnings during the last eight years restricted the imports including industrial raw materials, engineering supplies and spare parts. Since most industries are dependent on such import supplies, they were producing at less than full capacity.

Despite the fact that manufacturing industries were facing these difficulties, the government policy did not concentrate on the rehabilitation of the existing industries, but continued instead to establish new ones. Eighteen government industrial projects were being developed in 1964; shortly after the abortive coup d'état, though, the construction of these projects was suspended.

New Trade Policy

The adoption of the government's new trade policy early in 1967 eased the imports of industrial consumer goods. This tended to stabilise the prices of manufactured goods, including tex-

⁵ The production of rubber accounted for 738,000 tons in 1965; 718,000 tons in 1966; 585,000 tons in 1967; and 595,000 tons in 1968. See Antara Financial & Economic News, No. 300, January 2, 1969.

⁶ This can be consulted in his article "Herorientatie Dikembangkan Pembangunan Ekonomi" (Reorientation in Economic Development), Abadi, Jakarta, March 6-8, 1952.

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tiles. But as a result of the new trade policy domestic industries faced a problem of increasing cost of production because raw materials and spare parts were to be imported by using B.E. certificates and had to pay high import duties. By October, 1967, roughly 60 p.c. of textile industries in the country had stopped operation because imported products retailed cheaper. No less than 50 out of 88 pharmaceutical producers closed down and many companies were operating at about 25 p.c. of capacity. The government's monetary and fiscal measures were considered additional factors causing a decline of economic activity in Indonesia during 1967.

Declining Mineral Production

The loss of technical and managerial skills resulting from the forced exodus of the Dutch after 1957, shortages of equipment and spare parts, and corruption and inefficiency in state-owned mineral industries, are the main basic causes of stagnation and decline in mineral production.

While the production of oil, bauxite, and natural gas increased markedly between 1958 and 1968, the output of tin, coal and manganese had dropped rapidly. Tin, the third major source of foreign exchange, suffered a drastic decline in ten years. During this period tin production accounted for only about 50 p.c. of its output in 1956. Indonesia failed to reap the benefits of the high export quotas granted under the International Tin Agreement.

From 1960 to 1966 alone coal production declined by more than 50 p.c. The highest level of coal production during independence was achieved in 1952 with 959,000 metric tons, but was still only about one half of the pre-war level. In 1966 the production accounted for only one-third of the 1952 level or about 15 p.c. of the 1939 level.

The production of manganese also declined substantially. This mineral production could play an important role in export trade if provided with sufficient reinvestment capital. It reached a production level of 82,000 tons in 1956 and dropped to 10,900 in 1960, and to 7,200 tons in 1965. This resource has been totally neglected since independence.

Increasing Petroleum Exports

A steady increase in the production and export of oil helped to offset the foreign exchange losses resulting from declining production of coal and tin. Petroleum accounted for about 25 p.c. of the export total. Oil production amounted to 20.8 mn tons in 1960. The production of oil was not affected by the exodus of the Dutch in 1958 since the oil wells were not in the hands of Dutch entrepreneurs. The undertaking of production sharing in the oil sector after 1959 has

also been responsible for a rapid increase in oil output.

More than 70 p.c. of total oil production was exported since 1965. Oil production was 23.4 mn tons in 1966. In March, 1965, the government started supervision of operations of foreign oil companies. This was followed by the statement that the government would take over local sales of the foreign oil companies in Indonesia. As a result of these measures, the oil sector failed to meet the ambitious target of foreign exchange earnings as formulated in the Eight Year Plan. After Sukarno's dismissal, the confidence of foreign oil companies in this country was restored and was followed by a marked increase in oil output in the years after.

Some Prerequisites for Future Development

The success of the Suharto Cabinet's Five Year Plan to achieve its goals depends on the ability of the present government in removing the obstacles to economic planning. Political and social conflicts, corruption, and inflation remain the most dangerous bottlenecks for development in this country. To a certain degree President Suharto has successfully maintained political stability in Indonesia. The Indonesian army has, indeed, successfully crushed the rebellions and the communist abortive coup and its underground movement. It has played an important role in imposing the internal security of the country. However, the continuous domination of the army and vested groups in the government, and the ignoring of the public demand for more political freedom will invite new social conflict.

Indeed, a functioning democratic political atmosphere is important if the inflow of foreign capital especially from the Western countries is to be encouraged. The present Five Year Development Plan is relying heavily on foreign aid, although the government does not seem to admit it. Evidently, more than 60 p.c. of the plan's total expenditure of US \$3,500 mn must come from foreign sources. Government saving is expected to provide only US \$565 mn. Foreign credits and grants are estimated at US \$2,000 mn. Efforts will be made, according to President Suharto, to request assistance from foreign countries, especially the United States and Japan, amounting to US \$500 mn per year for the next four years.

From this it becomes obvious that not only a favourable political atmosphere is required, but the needs for improving the inefficient government administration and eliminating corruption are equally urgent. The slow economic progress made during the last three years has already proved that the suppression of the communist movement and the establishment of political stability are not sufficient requisites for economic stability and development.