1 Indonesia

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1.1 Introduction

The Republic of Indonesia is located on a crossroad between two oceans, the Pacific and the Indian, and bridges two continents, Asia and Australia. Indonesia is the largest archipelago in the world. It consists of five major islands and about 30 smaller groups. The figure of the total number of islands is 13,670. This strategic position has always influenced the cultural, social, political, and economic life of the country. The territory of Indonesia stretches from 6°08' north latitude to 11°15' south latitude, and from 94°45' to 141°05' east longitude. The Indonesian sea area is four times greater than its land area, which is about 1.9 million square kilometers. The sea area is about 7.9 million square kilometers (including exclusive economic zone) and constitutes about 81% of the total area of the country. The climate and weather of Indonesia is characterized by two tropical seasons. The climate changes every six months. The dry season (June to September) is influenced by the Australian continental air masses, while the rainy season (December to March) is the results of the Asian and Pacific Ocean air masses. The air contains vapor, which precipitates and produces rain in the country. Tropical areas have rains almost the whole year through. Due to the large number of islands and mountains in the country, average temperatures maybe classified as coastal plains 28°C, in land and mountains areas 26°C, and higher mountain areas 23°C varying with the altitude. Being in tropical zone, Indonesia has an average relative humidity between 70% and 90%, with a minimum of 73% and a maximum of 87%. The country consists of 26 provinces with about 500 tribes.

Indonesia is governed by a constitution drawn up in 1945 and based on the five principles of monotheism, humanitarianism, Indonesian unity, representative democracy by consensus and social justice. These principles are embodied in the state ideology, Pancasila. The constitution also contains provisions for six principal organs of state: the People's Consultative Assembly; the presidency and vice-presidency; the House of People's Representatives; the Supreme Advisory Council; the State Audit Board; and the Supreme Court.

Indonesia is the fourth most populous country in the world. The intercensal population survey, held in 1995, put the total population at 194.65 millions. The population was officially estimated to have passed the 200 millions mark in February 1997. Population growth, however, has been slowing. In the 1960s and 1970s growth averaged 2.3% per year. By the mid-1990s it was estimated to have fallen to about 1.6% – 1.7%.

Table 1.1 Population*

	1994	1995	1996	1997	1998
Total (millions)	192.22	195.28	198.34	201.39	204.42
% Change, year on year	1.6	1.6	1.6	1.5	1.5

* Mid-year estimates.
Source: IMF, International Financial Statistic

Indonesia has a reasonably well-balanced economy in which all major sectors play important roles. Agriculture has been historically the dominant activity, in terms of both employment and output. There is a vast range of mineral resources, the extraction and exploitation of which have proceeded rapidly in the past three decades, enabling the mining sector to make an important contribution to the balance of payments. The manufacturing sector also expanded dramatically since the mid-1980s. The services sectors jointly accounted for approximately 42% of GDP in 1998, when 30% of the working population was engaged in these sectors. Exports have traditionally constituted the primary engine of growth. Before the mid-1970s exports consisted mainly of a small number of primary commodities, including natural rubber, coconut oil and copra, tin and crude oil.

After the Indonesian economy rehabilitated in the 1960s, a reappraisal of economic objectives took place; they were henceforth defined as stability, growth and equity, collectively described as the "Trilogy of Development". The means of attaining these objectives have been a series of Five-year Development Plans, designed to establish development priorities and set specific growth targets.

The Sixth Five-year Development Plan (April 1994 – March 1999) was intended to achieve an economic growth rate of 7.1% a year to provide adequate employment opportunities for a projected increase in the labor force of 12.6 millions. The government was on target to surpass the intended growth rate until the disastrous year of 1998, during which the economy contracted by 13.2%, bringing average growth for 1994-1998 down to a mere 3%.

1.2 Overview of Macroeconomic Activity and Fiscal Position

Stabilization of the Indonesian economy went quite well during 1999, following the onset of a severe economic crisis in the middle of 1997. More stable monetary conditions, favorable domestic socio-political developments, and improved international economic conditions have fostered a return to rupiah exchange rate and price stability and stronger national economic activity. The Indonesian government pursued the banking restructuring, corporate debt restructuring, international and domestic trade reform, and increasing transparency in government operations as an effort to restore market confidence.

Macroeconomic stability has been maintained by upholding prudent and consistent principles of monetary policy of 1999 relatively tight. This stance took into consideration the threat to rupiah exchange rate stability. In the 2000 fiscal year the rupiah exchange rate is estimated to be 7.000 rupiah per US$ 1. Gross Domestic Product (GDP) rose by 0.2 percent in 1999 compared to the previous year -13.2 percent (as shown in Table 1.2 below). This increase has primarily been driven by increased household consumption. In 1999 the low trend rate of inflation was maintained by only 2 percent compared with the previous year was 77 percent. This was being driven by a continued decline in food prices, while clothing, housing and health services posted a slight increase.

The fiscal year 2000 budget has been prepared in consultation with the IMF and the World Bank and was approved by Parliament on March 2000. The fiscal year 2000 budget deficit remains unchanged but with higher expenditures and revenue. The budget deficit is now expected to be 5% of GDP, compared with 1999 budget deficit of 6.8% of GDP, thanks to higher than expected revenues largely due to higher oil prices and unexpectedly high tax receipts for interest income.

Table 1.2 Selected Macroeconomic Indicators

Items	1995	1996	1997	1998	1999
1. Gross domestic product at constant 1993 prices (In billions of rupiah)	383,792	413,797	433,246	376,051	376,902
2. Gross national product at constant 1993 prices (In billions of rupiah)	371,868	401,311	417,783	348,086	354,768
3. Per capita GNP (In thousands of rupiah)	2,277	2,633	3,049	4,675	4,994
4. GDP growth rate (%)	8.2	7.8	4.7	-13.2	0.2
5. GDP deflator (%)	9.9	8.7	12.0	83.3	--
6. Inflation rate (CPI, % change)	8.6	6.4	11.0	77.7	2.0
7. Unemployment rate (%)	4.8	4.9	4.7	5.5	6.3
8. Current account deficit/GDP (%)	--	-3.5	-2.3	4.3	4.0
9. Debt service ratio (%)	--	14.6	44.6	58.7	51.9

Source: Bank Indonesia & International Monetary Fund.

1.2.1 Macroeconomic Activity

A. International Environment

A.1 Trade Balance

Indonesia has a relatively open economy, although the import of certain goods is prohibited or limited by quota restrictions, while other goods may be imported only by approved importers. Tariffs and surcharges are also imposed to regulate the flow of imports.

Indonesia's balance of payment in 1999 experienced a surplus of $3.4 billion (Table 1.3). Gross official foreign exchange reserves rose by 13.9% to $27.1 billion, which was equivalent to 10.9 months of non-oil/gas imports.

Exports were expected to be the main force for economic revival. However, a highly competitive exchange rate and lower interest rate failed to bolster the nation's non-oil/gas exports. This was due to internal problems mainly had to do with the capital structure of domestic industries, which were heavily dependent upon external debts. The crisis created heavy burden for the repayment of the principal and interest on those debts. As for external problems, there were several obstructions to non-oil/gas exports. These included: severe global competition; limited trade financing facilities; the difficulties in obtaining working capital; and unstable social and political conditions.

In order to address these problems, during 1999 the government took several measures. On July 2, 1999, export taxes on oil palm, oil palm kernel, and crude palm oil (CPO) were cut from 30% to 10%. In addition, export taxes on refined bleached deodorized palm oil and palm olein were reduced from 22% to 6%; the export tax on crude olein was cut to 8%. Furthermore, to overcome the shortage of trade financing, the government in May 1999 established an export-financing institution called PT Bank Ekspor Indonesia.

During 1999, the Law Number 24 year 1999 on Capital Account and Foreign Exchange System was endorsed. Besides re-affirming the open capital account regime, the law also requires financial institutions to report in detail all foreign exchange transactions above $10.000 to Bank Indonesia.

Table 1.3 Indonesia's Balance of Payment

Items	1997	1998	1999*
	In billions of dollars		
A. Current account	**-5.0**	**4.1**	**5.2**
1. Goods	10.1	18.3	20.1
a. Exports f.o.b.	56.3	50.3	51.4
i. Non-oil/gas	44.6	42.9	41.4
ii. Oil/gas	11.7	7.4	10.0
b. Imports f.o.b.	-46.2	-32.0	-31.3
i. Non-oil/gas	-41.4	-29.1	-27.4
ii. Oil/gas	-4.8	-2.9	-3.9
2. Services	-15.1	-14.2	-14.9
a. Non-oil/gas	-10.5	-11.4	-11.9
b. Oil/gas	-4.6	-2.8	-3.0
B. Capital account	**2.6**	**-3.9**	**-3.2**
1. Net official capital inflows	2.9	10.0	6.5
a. Official inflows	7.6	13.7	10.6
b. Debt repayment	-4.7	-3.7	-4.1
2. Net private capital inflows	-0.3	-13.9	-9.7
a. Foreign direct investment	4.7	-0.4	-2.3
b. Others	-5.0	-13.5	-7.4
C. Total (A + B)	**-2.4**	**0.2**	**2.0**
D. Net errors and omissions	**-1.7**	**2.1**	**1.4**
E. Monetary movement	**4.1**	**-2.3**	**-3.4**
Note:			
1. Gross foreign assets (GFA)	21.4	23.8	27.1
2. Equivalent to non-oil/gas imports (months)	4.5	8.9	10.9
3. Net international reserves (NIR)	17.6	14.1	16.4
4. Current account deficit/GDP (%)	-2.3	4.3	4.0

* Provisional figures.

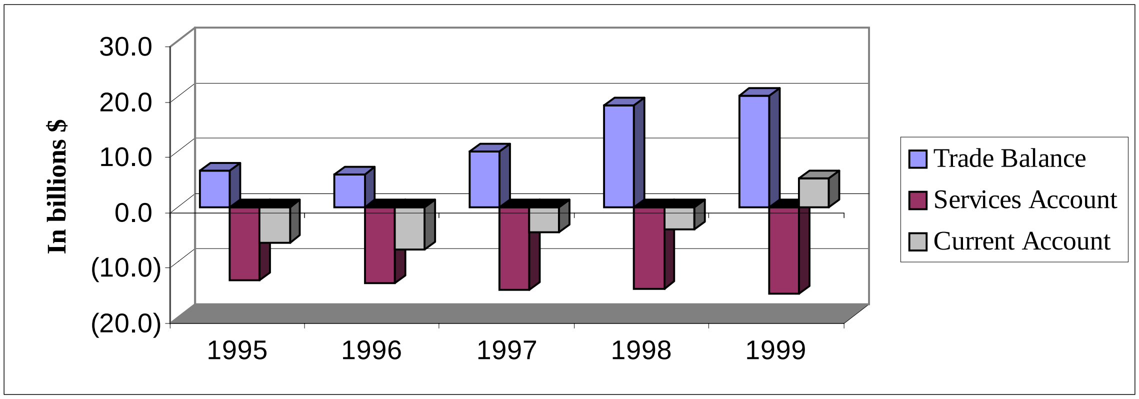
Source: Bank Indonesia, Annual Report 1999.

The Indonesian government on February 1999 received financial assistance from the Japanese government in the framework of the New Miyazawa Initiative amounting to $2.4 billion. The assistance was to bolster international trade activities, also used to finance the social safety net program, development of small and medium scale businesses, and the promotion of activities that boost the real economy and the banking system. The government of Indonesia also received financial assistance from Consultative Group on Indonesia (CGI) amounting to $5.9 billion.

A.2 Current Account Balance

Until recently the current account had consistently been in deficit, with surpluses only in the three oil-boom years of 1974 and 1979 – 1980. The current account in 1999 is estimated to have registered a surplus of $5.2 billion (4.0% of GDP), up from the surplus of $4.1 billion (4.3% of GDP) in 1998. The $20.1 billion trade surplus accounted for the current account surplus; the service account, as in previous years, remained in deficit. During 1999, the deficit on services amounted to $14.9 billion, widening a little from $14.1 billion in the previous year. This wide deficit was due to both oil/gas and non-oil/gas sectors.

Figure 1.1 Current Account, Trade Balance, and Services Account



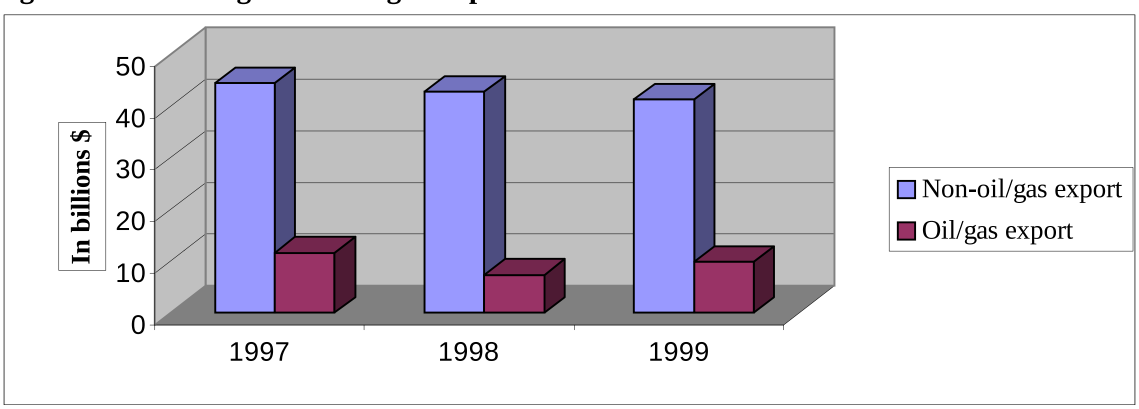
Source: Central Bureau of Statistics, Indikator Ekonomi; Buletin Ringkas.

A.2.1 Exports

After the oil price increases of 1973 – 1974, Indonesia's external trade was dominated by oil and gas exports, which consistently enabled it to register a surplus on its merchandise account, even though the non-oil/gas account remained in deficit. After the slump in global oil markets in the middle 1980s, a major effort was launched to reduce the non-oil/gas deficit, mainly by promoting non-oil/gas exports. In 1993 and 1994 the non-oil/gas account recorded surpluses of $920 million and $740 million respectively, for the first time in more than two decades, which put the overall trade balance into substantial surplus. In 1997 despite a mediocre performance by non-oil/gas exports, the balance went into surplus as non-oil/gas imports fell, a trend, which intensified sharply in 1998 as a result of the economic crisis.

During 1999, total exports rose by 2.2% to $51.4 billion. The growth was led by an increase in oil/gas exports, while non-oil/gas exports slipped further. Oil/gas exports amounted to $10.0 billion, or up 35.1% compared with the previous year. As for the breakdown, oil exports rose 39.0% whereas gas gained 30.3%. The increase in oil/gas exports was due to an improvement in international oil and gas prices. In 1999, the average price for oil exports rose sharply to $16.8 per barrel from $12.3 per barrel in 1998.

Figure 1.2 Non-oil/gas and Oil/gas Export Value



Source: Central Bureau of Statistics, Indikator Ekonomi; Buletin Ringkas.

Non-oil/gas exports in 1999 stood at $41.4 billion, or down 3.5% from the value in previous year. Declines took place in all major sectors. Agricultural exports witnessed the sharpest drop of 11.0% followed by industrial and mining sectors, which fell by 3.0% and 0.4% respectively.

As in previous year, Indonesia's non-oil/gas exports were dominated by the industrial sector. Exports from this source reached 77.7% of the total non-oil/gas exports; mining and agriculture contributed 11.3% and 11.0% respectively. This composition was not significantly different from 1998.

Table 1.4 Exports by Main Commodity Group

Items	1994	1995	1996	1997	1998
	In millions of $; fob				
Food	3,558	3,583	3,767	3,546	3,717
Beverages and tobacco	137	196	229	253	258
Crude materials	3,235	5,035	5,082	4,357	3,720
Mineral fuels	10,524	11,508	12,860	13,353	9,429
Animal fats and oils	1,374	1,384	1,577	2,280	1,520
Chemicals	1,010	1,524	1,726	1,883	2,092
Manufactured goods	9,470	10,438	10,796	9,703	8,772
Machinery & transport equipment	3,048	3,828	4,999	4,622	4,656
Miscellaneous manufactures	7,550	7,876	8,688	6,982	6,659
Other goods	147	46	90	6,465	8,024
Total exports	40,053	45,418	49,814	53,444	48,848

Source: Central Bureau of Statistics, Indikator Ekonomi; Buletin Ringkas.

A.2.2 Imports

Among imports, raw materials and other intermediate goods have been the leading category followed by capital goods. This reflected the high rate of investment and manufacturing growth taking place in the country until recently. It also reflected the heavy dependence of many of Indonesia's manufactured exports on imported inputs, which made increasingly large swathes of the manufacturing industry vulnerable to a rupiah devaluation.

During 1999, the value of imports declined modestly, by 2.2% to $31.3 billion. The decline was accounted for by non-oil/gas imports, which slip to $27.4 billion from $29.1 billion in 1998; oil/gas imports jump from $2.9 billion to $3.9 billion. Almost all the major components of non-oil/gas imports fell, except for raw materials, which was relatively stable (Table 1.5). These developments reflected the sluggish economic activity.

Table 1.5 Non-oil/gas Imports by Category of Goods

Categories	1998	1999	1999	
	Change (%)		Value (million $)	Growth (%)
Consumer goods	-28.7	-15.0	1,395	5.1
Raw and intermediary input	-26.7	0.9	19,700	71.8
Capital goods	-36.7	-20.0	6,342	23.1
Total	**-29.8**	**-20.0**	**27,437**	**100.0**

Source: Bank Indonesia, Annual Report.

In 1999 the value of imports of consumer goods fell sharply by 15.0% to $1.4 billion, mainly reflecting lower incomes of the people. Among the components, the fall was mainly attributable to imports of non-industrial goods for transportation, durable consumer goods, and semi-durable consumer goods (Table 1.6). Imports of raw material were virtually unchanged from their 1998 value of $19.7 billion, due to low domestic production activity. Lethargic investment demand also accounted for the downward trend on the imports of capital goods to $6.3 billion. Almost all components of capital goods imports edged lower in 1999.

Table 1.6. Imports by Main Commodity Group

Items	1994	1995	1996	1997	1998	1999
	In millions of $; cif					
Consumer goods	**1,430**	**2,350**	**2,806**	**2,166**	**1,918**	**1,395**
Food and beverages	568	1,135	1,593	843	1,167	766
Fuel and lubricants	89	111	159	139	95	120
Transport equipment	11	15	12	17	3	9
Durable goods	115	239	182	248	95	127
Semi-durable goods	272	307	303	291	181	130
Non-durable goods	265	331	363	411	218	193
Others	111	212	195	217	158	50
Raw and Intermediary goods	**23,134**	**29,587**	**30,470**	**30,230**	**19,612**	**19,700**
Food and beverages	1,205	1,672	2,117	1,860	1,295	1,453
Industrial raw material	13,331	17,227	16,758	16,155	11,243	10,898
Fuel and lubricants	2,301	2,861	3,475	3,827	2,603	5,671
Spare parts & accessories	6,297	7,826	8,119	8,388	4,471	1,678
Capital goods	**7,420**	**8,692**	**9,653**	**9,284**	**5,807**	**6,342**
Machinery	6,576	7,886	8,906	8,617	5,428	5,649
Transport equipment	844	806	747	667	380	693
Total	**31,983**	**40,629**	**42,929**	**41,680**	**27,337**	**27,437**

Source: Central Bureau of Statistics, Indikator Ekonomi.

A.3 Foreign Reserves

As a result of large capital inflows, the overall payments account generally enjoyed large surpluses, which was reflected in the accumulation of foreign exchange reserves. This situation has been dramatically reversed as a result of the economic crisis. International reserves (using the broad definition of gross foreign assets, GFA) increased sharply from the late 1980s, from $5 billion at the end of 1988 to a peak of $28.9 billion at the end June 1997. Reserves than fell sharply as a result of a massive net outflow of capital, reaching $16.6 billion by the end of March 1998. In addition to the GFA measure, Bank Indonesia has been publishing data on its net international reserves (NIR) and its liquid reserves. In mid-October 1999 NIR stood at $16.1 billion and liquid reserves at $23.8 billion.

Table 1.7 Foreign Reserves

Items	1994	1995	1996	1997	1998
	In millions of $				
SDRs	0	1	2	499	312
Reserve position at the IMF	312	401	429	0	0
Foreign exchange	11,820	13,306	17,820	16,088	22,401
Total reserve excl. gold	12,133	13,708	18,251	16,587	22,713
Gold*	1,067	1,079	1,030	809	803
Total reserve incl. gold	13,200	14,787	19,281	17,396	23,516
Gold (m troy oz)	3.10	3.10	3.10	3.10	3.10
Months of import cover	4.9	4.3	5.2	4.5	8.8

* Valued at 80% of the London price on the 15th day of the last month of the previous year
Source: IMF, International Financial Statistics.

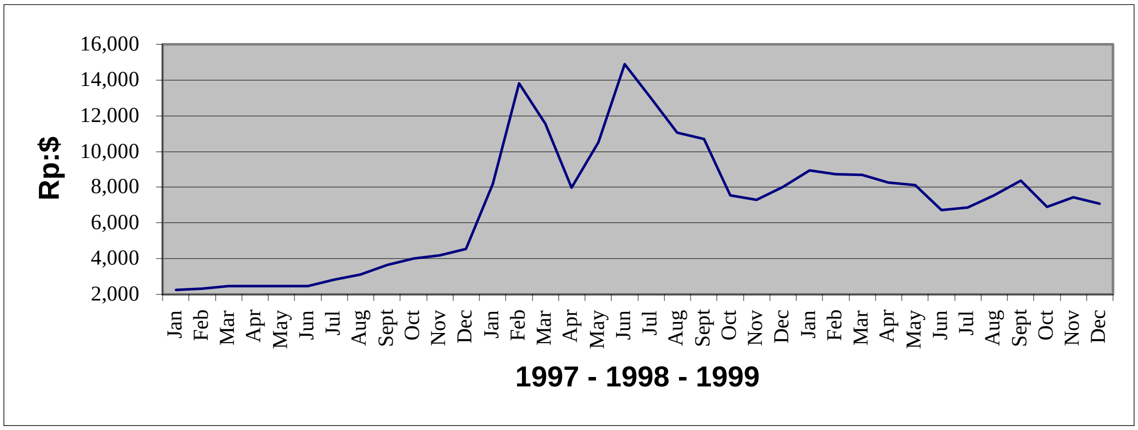
A.4 Exchange Rate and Exchange System

Indonesia is fundamentally committed to a free foreign exchange system. The foreign exchange controls that do exist are few and simple. Transfers of funds to and from foreign countries are not restricted, although incoming capital for foreign investment must be reported to Bank Indonesia for statistical purposes. Foreign currency accounts may be maintained at banks licensed to deal in foreign exchange, but banks have not been permitted to issue cheques in foreign currencies for domestic use since 1976. Withdrawals from such accounts may be made through counter cheques available at the banks and may take the form of rupiah or foreign currency cash, travel cheques or bank drafts. Overseas payments in foreign currencies may be made by bank drafts, payment orders or cable transfers.

The Asian currency crisis forced the government to allow the rupiah to float freely on August 14th 1997, and thereafter the currency was severely buffeted by a range of external and domestic developments. From Rp2,450 : $1 on the eve of the crisis at the end of June 1997, the rupaih hit lows of around Rp17,000 : $1 in early January and June 1998, about 85% below its pre-crisis level. Helped by the weakening dollar, inflows of official aid and the current account surplus, the rupiah strengthened rapidly from September 1998 and stabilized at around Rp8,000 : $1 throughout much of 1999.

The rupiah appreciated significantly in 1999 and displayed more stability than during the previous year. The main factors were the conduct of monetary policy, especially measures to manage liquidity in the banking system, and a significant improvement in inflationary expectations. Better socio-political conditions and rising confidence in the prospects for economic recovery established a solid foundation for rupiah stability.

Figure 1.3 Rupiah Exchange Rate



Source: Bank Indonesia, Indonesian Financial Statistics.

A.5 Foreign Direct Investment

The government attempted to reduce its reliance on debt to meet its external financing needs by promoting increase in foreign investment. This resulted in the adoption of a series of policy packages to liberalize the regulations governing foreign direct investment. The new regulations, introduced gradually between 1989 and 1994, restored an essentially free investment regime. Under this regime foreign investment is permitted in virtually all sectors, including infrastructure; wholly owned foreign investments are allowed; the equity limits on foreign partners in joint-venture enterprises have been rise to 95%; an earlier minimum capital requirements of $250,000 for foreign investors has been scrapped; and the divestment requirements has been eased to a token 1% of equity after 15 years. In 1999 steps were taken to speed up the approval process and tax incentives were offered for investments in certain sectors through the Presidential Decree Number 7 of 1999. The value of the foreign direct investment projects that were approved by the National Investment Coordinating Board sharply fell from $33 billions in 1997 to $13 billions in 1998 and to $10 billions in 1999. This was mainly caused by the economic crisis and political unrest. And since the onset of economic crisis many of these projects have been postponed further and some have been abandoned.

Table 1.8 Approved Foreign Direct Investment Projects by Sector

Sector	1997	1998	1999	Total from 1968 – 1999*	
				Value	Project
	In millions of $				
1. Agriculture	463.7	998.2	491.2	7,864.9	363
2. Mining	1.6	0.3	14.1	9,920.3	205
3. Manufacturing	23,017.3	8,388.2	6,929.2	148,270.5	4,137
4. Construction	306.8	197.8	153.4	1,963.1	351
5. Hotel	462.6	451.1	228.6	11,330.7	313
6. Transportation	5,900.0	79.0	102.7	13,376.0	244
7. Real estate and office building	1,397.6	1,270.9	179.4	12,611.2	211
8. Other services	2,282.9	2,177.6	2,792.0	23,461.3	1,841
Total	33,832.5	13,563.1	10,890.6	228,798.0	7,665

*From July 1968 to December 1999, after taking into account cancellation and shifting of projects from foreign to domestic investment.
Source: National Investment Coordinating Board (BKPM).

A.6 Borrowing From Abroad

For most of the past 30 years Indonesia has relied mainly on concession official borrowing to meet its financing requirement. This aid has been disbursed mainly through two consortia of official donors: the Inter-governmental Group on Indonesia (IGGI), which was established in 1966 under the chairmanship of the Netherlands; and from 1992 the Consultative Group for Indonesia (CGI), chaired by the World Bank.

By the end of 1999, Indonesia's outstanding foreign debts dropped 6.4% to $141.3 billion (Table 1.9). The amount declined because of a drop in private foreign debts, stemmed from partial repayments on maturing debts. By contrast, the government's foreign debts rose due to the disbursement of multilateral and the IMF loans. Private foreign debts amounted to $65.6 billion, or down 21.5% from the amount at end-1998. Of the total, $52.6 billion was non-bank private foreign debts, $10 billion bank debts, and $2.9 billion was in the form of debt notes held by foreign investors.

Table 1.9 External Debt Outstanding

Item	1997	1998	1999
	In millions of $		
Government	53,865	67,315	75,763
Private	82,223	83,572	65,618
Bank	14,364	10,769	10,063
Non-bank	57,588	67,515	52,630
Securities	10,271	5,288	2,915
Total	**136,088**	**150,887**	**141,381**

Source: Bank Indonesia, Annual Report.

Restructuring this debt in the wake of the crisis has proved difficult. Among East Asian countries Indonesia's private debt was most heavily concentrated in a large number of corporate borrowers rather than in a small number of banks, making any solution more complex.

Table 1.10 Indonesian External Debt

Item	1993	1994	1995	1996	1997
	In millions of $				
Total external debt	89,172	107,824	124,398	128,940	136,088
Long-term debt	71,185	88,367	98,432	96,710	97,199
Public	57,156	63,926	65,309	60,016	55,869
Private	14,029	24,441	33,123	36,694	41,330
Use of IMF credit	0	0	0	0	2,970
Short-term debt	17,987	19,457	25,966	32,230	36,004
Public & publicly guaranteed long-term debt	57,156	63,926	65,309	60,016	55,869
Long-term debt	44,263	49,968	51,250	46,148	42,524
Official creditors	17,822	19,165	20,013	17,248	15,799
Multilateral	26,441	30,804	31,237	28,899	26,725
Bilateral	12,893	13,958	14,059	13,868	13,345
Private creditors:					
Banks	7,631	7,426	6,714	5,996	5,884
Bonds	99	99	704	1,141	1,191
Total debt service	14,089	14,267	16,416	21,539	19,736
Principal	9,138	8,951	10,197	14,892	13,010
Interest	4,951	5,316	6,219	6,647	6,727
Short-term debt	840	1,142	1,284	1,533	1,610
Long-term debt	4,112	4,174	4,935	5,115	5,117

Source: World Bank, Global Development Finance.

As the burden of debt repayment was heavy and economic activity was sluggish, some indicators of external debt worthiness deteriorated beyond the standards of healthy foreign debt management. The debt service ratio (DSR) and the ratio of the debt to GDP reached 51.9% and 108.5% respectively at the end of 1999 (Table 1.11). Some of the ratios indicated that the country's capacity to service foreign debts decreased appreciably during 1999.

Table 1.11 External Debt Indicators

Indicator	1996	1997	1998	1999
	Percent (%)			
Debt-service ratio	34.0	44.6	58.7	51.9
Debt outstanding/Exports	179.5	207.8	262.0	240.0
Debt outstanding/GDP	48.9	63.6	145.8	108.5

Source: Bank Indonesia

B. Domestic Environment

B.1 Economic Growth Rate (GDP), Consumption and Investment

Prudent economic management enabled Indonesia to record consistently high rates of economic growth, well in excess of the rate of population growth, for more than three decades. This growth, which averaged more than 6% a year between 1970 and 1996, was achieved despite a number of external shocks, including sharp movements in the price of oil and in international exchange rates, which affected the term of trade and the value of the country's external debt.

As a result of the Asian economic crisis that began in Thailand in 1997 and rapidly spread throughout South-east Asia created the conditions for slowing down the growth of the economy during 1997 – 1998. With more conducive domestic and overseas conditions, signs of improvement in Indonesia's economy began to emerge in 1999. This can be seen in real Gross Domestic Product (GDP), which is estimated to have increased by 0.2% (Table 1.12), following a large contraction in the previous year. This improvement was mainly stimulated by greater private and government consumption, a pick-up in production among manufacturing sector, the services sector, and the electricity, gas and drinking water sector, as well as continuing production increases in the agriculture sector.

Table 1.12 Gross Domestic Product by Expenditure

Items	1995	1996	1997	1998	1999
	In billions of rupiah; at constant 1993 prices				
Private consumption	234,245	257,016	277,116	267,913	271,867
Government consumption	30,851	31,681	31,701	26,828	27,014
Gross domestic fixed capital Formation	112,386	128,699	139,726	90,071	71,351
Change in stocks	15,852	5,872	3,342	-11,066	-6,596
Exports of goods & services	104,492	112,391	121,158	134,707	91,517
Less imports of goods & services	114,035	121,863	139,796	132,401	78,252
Gross Domestic Product	383,792	413,797	433,246	376,052	376,902
Net factor income from abroad	-11,923	-12,486	-15,462	-27,965	-22,133
Gross National Product	371,869	401,311	417.783	348,086	354,768
Less net indirect tax	23,209	22,469	26,100	-1,623	7,771
Less depreciation	19,189	20,869	21,662	22,288	18,845
National income	329,469	358,151	370,020	327,421	328,151
Growth rates (%)					
Private consumption	15.9	9.7	7.8	-3.3	1.5
Government consumption	1.3	2.7	0.1	-15.4	0.7
Gross fixed investment	14.0	14.5	8.6	-35.5	-20.8
Change in stock (% of GDP)	4.1	1.4	0.8	-2.9	-1.7
Exports of goods & services	8.6	7.6	7.8	11.2	-32.1
Imports of goods & services	27.1	6.9	14.7	-5.3	-40.9
GDP	8.2	7.8	4.7	-13.2	0.2

Source: Central Bureau of Statistics, Indikator Ekonomi; Bank Indonesia, Annual Report 1999.

A breakdown of the economy's growth performance by sector shows that industry was the principal engine of growth. Manufacturing expanded much more rapidly than the economy as a whole. The need to ensure matching growth in infrastructure stimulated a sharp acceleration in the rate of growth of the utility and construction sectors. The electricity, gas and water component of GDP expanded by an average of around 14% a year between 1986 and 1996, while the construction sector expanded by more than 10% a year in the same period.

As a result of the economic crisis GDP growth first slowed to 4.7% in 1997, and then contracted by -13.2% in 1998, the worst performance. Declines in output occurred in several sectors except agriculture, which managed full-year growth of 0.6%, manufacturing growth of 2.2%, construction by 1.1%, electricity, gas and water grew by 7.2%, and other services by 2.8%. The worst affected sector was financial services down by -8.6% (Table 1.13).

Consumption began to recover in year 1999, recording growth of 1.4% after declining by -4.6% in previous year. Both public and private consumption increased. The increase in government consumption is in line with the increase in government routine expenditure. The factors stimulating private consumption appear to be: stability of primary goods prices; declining interest rates; strengthening of the rupiah; and continuing social safety net program.

During 1999 gross fixed investment fell by -20.8%, with the great effect of the decline accounted for by private investment. The investment decline was reflected in non-oil/gas imports of capital goods, which decline in value and volume. Lack of interest in investment was mirrored in the decline of foreign direct investment and domestic direct investment approvals. The sharp drop of investment activities was also due to stagnant financing, domestic and overseas, and expansion of new credit from bank was still very limited.

Table 1.13 Gross Domestic Product by Sector

Items	**1995**	**1996**	**1997**	**1998**	**1999**
	In billions of rupiah; at constant 1993 prices				
Agriculture	61,885	63,828	64,468	64,988	65,424
Mining	35,502	37,739	38,538	37,353	37,311
Manufacturing	91,637	102,260	107,630	94,848	96,927
Construction	29,198	32,924	35,346	21,035	21,276
Electricity, gas & water	4,292	4,877	5,480	5,582	5,986
Transport & communications	27,329	29,701	31,783	26,975	26,782
Retailing & hotels	64,231	69,475	73,524	60,253	59,591
Financial services	34,313	36,384	38,543	28,279	25,826
Other services	35,406	36,610	37,935	36,739	37,776
GDP	383,792	413,797	433,246	376,052	376,902
Non-oil/gas	350,290	378,781	398,676	341,817	343,016
Oil/gas	33,502	34,927	34,570	34,234	33,885
Growth rates (%)					
Agriculture	4.4	3.1	1.0	0.8	0.6
Mining	6.7	6.3	2.1	-3.1	-0.1
Manufacturing	10.9	11.6	5.3	-11.9	2.2
Construction	12.9	12.8	7.4	-40.5	1.1
Electricity, gas & water	15.9	13.6	12.4	1.9	7.2
Transport & communications	8.5	8.7	7.0	-15.1	-0.7
Retailing & hotels	7.9	8.2	5.8	-18.0	-1.1
Financial services	11.0	6.0	5.9	-26.6	-8.6
Other services	3.3	3.4	3.6	-3.2	2.8
GDP	8.2	7.8	4.7	-13.2	0.2
Non-oil/gas	9.2	8.2	5.2	-14.3	0.3
Oil/gas	-1.4	4.3	-1.0	-1.0	-1.0

Source: Central Bureau of Statistic, Indikator Ekonomi

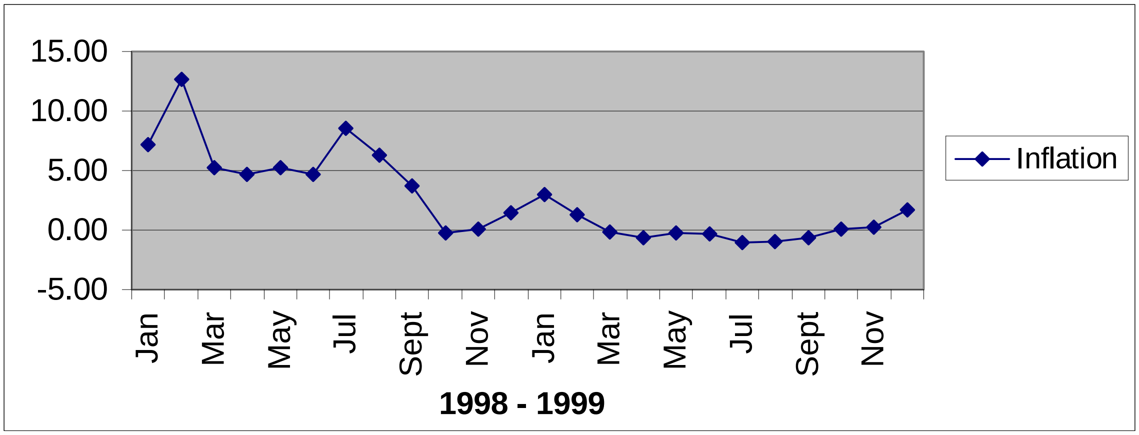
B.2 Inflation Rate

Throughout the 1980s and much of the 1990s the broadly conservative stance adopted by the monetary authorities enabled them to restrain inflationary pressures in the economy with reasonable success. Only in one year between 1984 and 1997 was the average annual rate of inflation not held to single digits, it was in 1993, 10.2%.

The onset of the crisis in 1997 – 1998 created the conditions for hyperinflation, driven by the collapse of the rupiah, the breakdown of production and distribution, and the vary rapid expansion of money supply to finance the subsidies program and to keep the banks afloat – a set of circumstances that drove inflation up to 77.6% for the year 1998.

In 1999 the inflation rate, which is measured from the change of consumer price index, nose dived to 2.01%, compared with 77.60% in the previous year. Such a low inflation rate in the reporting year was caused by improvement in the supply side of the economy. Economic growth was boosted by an increase in short-run aggregate supply. This stemmed from declining interest rates on working capital, decreasing input prices and raw materials, as well as lower prices of imported intermediate goods due to the strengthening of the rupiah.

Figure 1.4 Consumer Price Index - Inflation



Source: Central Bureau of Statistic, Statistics Indonesia.

B.3 The Capital Market Developments

The long-moribund Jakarta Stock Exchange (JSX) was re-launched in 1977, but it was not until the announcement of changes to the taxation system that put dividend and interest income on an equal footing in tax procedures in October 1988 financial reform package that the market begin to stir. The JSX index rose from 83 at the start of 1988 to a new record of 682 in April 1990. The number of listed firms rose to 104 during this period. These developments accompanied by the establishment of a privately owned stock exchange in Surabaya in June 1989. In April 1992, the stock exchange was privatized.

The region was then plunged into an economic crisis. In middle September 1998 the index fell to 292, almost 60% below its level at the end of June 1997. The JSX Composite Index increased from 398.0 at the end of 1998 to 676.9 by the end of 1999 (Table 1.14). The sharpest increase took place during the second quarter of 1999 as a result of improved investors' confidence on domestic social and political situation especially after election campaigns ended peacefully.

Recovery of capital market in 1999 was evident in a remarkable increase in trading volume compared with the previous year. In 1999, 178.7 billion shares were traded, soaring 94.9% from the volume in the previous year. Trading value increased by 48.2% to Rp147.8 trillion; 10 new companies listed shares on the JSX bringing the total number of listed companies to 319.

The capital market growth in 1999 was also reflected in rising activity in the bond market, especially during the last quarter of the year. With interest rate declining and limited lending by banks, the domestic bond market became an attractive financing option. After no new bonds were issued since 1997, 6 companies tapped funds from the bond market in 1999. As a result, the value of bond issuance rose from Rp18.9 trillion to Rp23.2 trillion (Table 1.14).

Table 1.14 Capital Market Developments

Items	1997	1998	1999				End of Period Outstanding
			I	II	III	IV	
Stocks							
Number of companies	306	309	310	313	313	319	319
Issuance							
- Volume (in billions of stock)	51,5	62,7	382,6	595,9	703,4	714,3	714,3
- Value (in trillions of rupiah)	70,9	75,9	121,4	190,2	201,5	206,4	206,4
Market capitalization (in trillions of rupiah)							
- Jakarta stock exchange (JSX)	159,9	175,7	167,3	416,1	357,7	451,8	451,8
- Surabaya stock exchange (SSE)	141,6	157,9	150,6	386,8	328,9	407,7	407,7
Trading							
JSX							
- Volume (in billions of stock)	76,6	91,7	11,0	72,5	42,5	52,8	178,7
- Value (in trillions of rupiah)	120,4	99,7	11,7	46,9	40,7	48,5	147,8
Foreign	62,9	41,6	5,9	19,4	15,6	10,7	51,6
Domestic	57,6	58,1	5,8	27,5	25,1	37,8	96,2
SSE							
- Volume (in billions of stock)	4,9	2,2	0,4	1,4	1,7	3,5	7,0
- Value (in trillions of rupiah)	10,8	3,1	0,3	3,2	5,5	4,2	13,2
CSPI							
- JSX	401,7	398,0	393,6	662,0	547,9	676,9	676,9
- SSE	351,9	351,5	349,4	645,6	460,8	566,5	566,5
Bonds							
Number of companies	70	70	70	70	71	76	76
Issuance value (in trillions of rupiah)	18,7	18,9	18,9	19,4	21,3	23.2	23,2
Outstanding value (in trillions of Rp)	15,6	14,5	14,2	14,4	13,9	15,9	15,9
Outstanding volume (in thousands of units)	242,6	202,3	181,2	176,5	171,2	174,9	174,9
Trading value (in trillions of rupiah)	7,3	4,9	1,1	1,5	1,3	1,0	4,9
Trading frequency	1,910	1,476	332	454	418	318	1,522

Source: Capital Market Supervisory Agency.

B.4 Money Supply

At the end of December 1999, M1 amounted to Rp124.6 trillion, up Rp24.1 trillion from the previous year (Table 1.15). The increase was led by Rp17.0 trillion increases in the amount of the currency in circulation. Besides rising economic activity, the increase in currency demand stemmed from a preference on the part of the public to hold cash due to fragile social and political situation. M2, the broadly defined money supply, grew by Rp75.7 trillion during 1999, reaching Rp646.2 trillion at yearend.

Table 1.15 Money Supply and Credit

Items	1995	1996	1997	1998	1999
	In billions of rupiah; end-period				
Currency in circulation	20,807	22,487	28,424	41,394	58,353
Demand deposits	31,870	41,602	49,919	59,803	66,280
Money (M1)	52,677	64,089	78,343	101,197	124,633
% Change	16.1	21.7	22.2	29.2	23.1
Quasi-money*	169,961	224,543	277,300	476,184	521,572
Money (M2)	222,638	288,632	355,643	577,381	646,205
% Change	27.6	29.6	23.2	62.4	11.9
Domestic credit	233,088	286,725	407,391	524,235	649,833
Claims on central government	-26,300	-29,057	-45,453	-28,030	397,257
Claims on public sector	10,955	15,581	20,612	27,001	18,862
Claims on private sector	248,433	300,201	432,232	525,264	233,714
Net other items	-43,076	-48,734	-119,643	-88,531	-132,724
Net foreign assets	32,626	50,641	67,895	141,677	129,096

* Time and savings deposits and foreign-exchange deposits held by private sector.
Source: Bank Indonesia, Indonesian Financial Statistics.

B.5 Employment

Rising economic activity in 1999 provided employment opportunities in almost sectors. However, the increase in the employment opportunities could not match the high growth of the labor force. This high growth resulted from the entrance of many people in working age population into the labor market, including school dropouts and housewives, due to the pressures of the economic crisis. The imbalance resulted in a rising unemployment rate from 5.5% in 1998 to 6.3% in 1999 (Table 1.16), with open unemployment rising to 6.0 million people in 1999, from 5.1 million in the previous year. And the large gap between the supply and demand for labor held down wages in 1999.

Labor supply increased by 2.3% in 1999, swelling the labor force to 94.8 million people. With a total of the 141.1 million people in the working age population, the labor force participation rate was 67.2% in 1999, up from 66.9% in 1998. This increase was partly due to new entrants of working age population, such as housewives and school dropouts, due to pressures of the crisis.

Table 1.16 Manpower Indicator

Indicator	1997	1998	1999	Change 1998-1999
	In millions of persons			In percent
Working age population	135,1	138,5	141,1	1.84
Labor force	89,6	92,7	94,8	2.30
Employed labor force	85,4	87,7	88,9	1.42
Unemployed labor force	4,3	5,1	6,0	17.50
Unemployment rate (%)	4.7	5.5	6.3	0.45
Labor force participation rate (%)	66.3	66.9	67.2	14.90

Source: Ministry of Manpower.

1.2.2 Fiscal Position

A. Government Expenditure and Public Borrowing

As of December 1999, the government's expenditures had reached 123.1 trillion rupiah, or 57.9% of the target set for the 1999/2000 fiscal year (Table 1.17). Low realizations characterized both operating and investment expenditures, and undermined the government's efforts to expedite economic recovery.

Operational expenditures were budgeted at 153.2 trillion rupiah during fiscal year 1999/2000. Until December 1999, the actual operational expenditures had reached 92.0 trillion rupiah. The payment of interest on the government's debts constitutes the largest component of the operational expenditures, amounting to 27.6 trillion rupiah. Interest payments on offshore and domestic debts were 15.3 trillion rupiah and 12.3 trillion rupiah, respectively (interest on bonds issued to re-capitalize banks). Another major spending item is civil servants' salaries, which rose to 24.3 trillion rupiah, owing to increase in salaries and pensions. Subsidies reached 14.9 trillion rupiah, largely attributable to subsidies for fuels.

As of December 1999, investment expenditures topped 31.1 trillion rupiah, which represents 52.2% of the fiscal year 1999/2000 targets. Delayed disbursement of offshore loans (due to political transition in 1999) led to low realizations of investment spending.

As of end of December 1999, the budget deficit reached 3.2 trillion rupiah or 0.4% of the GDP, which was financed by external borrowings as well as domestic sources. Net withdrawal of offshore debts amounted to 9.1 trillion rupiah, which consisted of loan withdrawal of 22.7 trillion rupiah subtracting with the repayment of the principal of 13.6 trillion rupiah. Domestic financing, which was raised through privatization of state owned enterprises, reached 3.7 trillion rupiah.

The actual disbursement of external borrowings of 22.7 trillion rupiah was considerably less than the plan of 77.4 trillion rupiah during the fiscal year 1999/2000 since the World Bank decided to delay disbursement of major loan.

During 2000, certain important presentational changes will be made to the fiscal accounts. The government will shift from a fiscal to a calendar year, which means that the government's financial operations in 2000 will cover only nine months, from April 1st 2000 until December 31st 2000. Also the format and structure of the budget, which currently follows a T-account tabular format, will be altered to government finance statistics format, which is an international standard. This change is taken to enhance transparency and accountability in drafting and implementation of the budget.

In 2000, a budget deficit will be unavoidable as the government's operational and investment expenditures will necessarily remain high to inject stimulus into the economy. Revenues and expenditures are projected to reach 137.8 trillion rupiah and 183.1 trillion rupiah respectively. The implied deficit would be 45.4 trillion rupiah equivalent to 5% of the GDP, lower that the previous year of 83.5 trillion rupiah or 6.8% of GDP. The deficit would be financed by the privatization of state owned enterprises, the sales of bank assets under IBRA and further external borrowing.

Budget expenditures are projected to reach 20.1% of GDP, up from 17.4% of GDP in last year's budget. On the operational side, payments on domestic debts of 42.4 trillion rupiah or 4.7% of GDP would be virtually equal to the deficit of the government's financial operations in 2000. This reflects the cost of servicing the government bond issued in the framework of the bank-restructuring program. Personnel expenditures are projected to rise from 2.7% to 3.2% of GDP due to the government's plans to improve the professionalism of the state apparatus by increasing civil servant salaries and pensions.

Lower investment expenditures will be undertaken in line with the implementation of wider regional autonomy and fiscal decentralization stipulated in the Act Number 22/1999 on Regional Administration and Act Number 25/1999 on the Fiscal Balance between the Central and Regional

Governments. In anticipation of the implementation of these two Acts, the government will raise the proportion of the funds to be managed by local governments from 1.3% of GDP to 1.7%.

The government will start reducing foreign borrowings. Disbursements of new loans are expected in the amount of 3.5% of the GDP compared to 6.3% in the previous fiscal year. The government will seek to reschedule the principal of official borrowings, in order to reducing the debt repayments to 0.9% of GDP lower that the previous fiscal year amounted to 2% of GDP.

Table 1.17 Government Financial Operations for 2000

Description	1999/2000*			2000**	
	Budget	% Of GDP	Actual”	Budget	% Of GDP
	In trillions of rupiah				
Total revenues and Grants	129.2	10.6	122.5	137.8	15.1
Domestic revenues	129.2	10.6	122.5	137.8	15.1
Tax revenues	99.5	8.1	81.9	97.9	10.8
Non-tax revenues	29.7	2.4	40.6	39.9	4.4
Grants	--	0.0	--	--	0.0
Total Expenditures	212.6	17.4	123.1	183.0	20.1
Routine expenditures	150.9	12.5	92.0	143.6	15.8
Personnel expenditures	33.5	2.7	24.3	29.3	3.2
Material expenditures	11.0	0.9	6.4	8.9	1.0
Local government expenditures	19.4	1.6	13.4	17.1	1.9
Amortization & interest payments	54.5	4.5	27.6	58.9	6.5
Subsidies	28.0	2.3	14.9	26.6	2.9
Others expenditures	6.6	0.5	5.3	2.6	0.3
Development expenditures	60.7	4.9	31.1	39.3	4.3
Rupiah financing	31.7	2.5	18.3	23.3	2.6
Project aids	29.0	2.4	12.8	22.1	1.8
Budget surplus/deficit	-83.5	-6.8	-3.2	-45.4	-5.0
Financing	83.5	6.8	3.2	45.4	5.0
Domestic financing	30.0	2.5	3.7	22.1	2.4
Domestic banks	--	0.0	-9.6	--	0.0
Domestic non-banks	30.0	2.5	3.7	22.2	2.4
Privatization proceeds	13.0	1.1	3.7	5.9	0.6
Recovery of bank assets	17.0	1.4	0.0	16.3	1.8
External financing	53.5	4.4	9.1	23.2	2.5
Gross drawing	77.4	6.3	22.7	31.8	3.5
Amortizations	-23.9	-2.0	-13.6	-8.6	-0.9
Total	1.224.2			910.4	

*Adjusted to new classification

**April 1st – December 31st 2000

“Preliminary figures as of December 31, 1999

Source: Ministry of Finance, State Budget (APBN) 2000, Bank Indonesia.

Table 1.18 Selected Ratios in Government Revenues and Expenditures

Descriptions	1997/1998	1998/1999*	1999/2000**	2000**
	Percent			
Operational expenditures to GDP	10.7	12.5	12.5	15.8
Gross domestic investment to GDP	3.9	3.6	2.2	2.4
Consumption to GDP	8.8	9.8	10.3	15.8
Overall balance to GDP	-0.9	-2.7	-6.8	-5.0
Primary balance to GDP	0.7	0.6	-2.4	1.5
Non oil/gas revenues to domestic revenues	72.8	73.5	83.8	71.1
Non oil/gas revenues to GDP	11.9	11.4	8.8	10.8
Tax revenues to GDP	10.3	10.1	7.7	10.8

* Revised state budget

** Budget

Source: Ministry of Finance and Bank Indonesia.

Table 1.19 Government Expenditure by Sector

Expenditure Items	Routine Expenditures		Development Expenditures	
	Budget 1999/2000*	Budget 2000**	Budget 1999/2000*	Budget 2000**
	In billions of rupiah			
Industrial sector	108,1	102,3	629,2	142,7
Agriculture and forestry sector	743,9	758,4	4.613,3	2.128,2
Waters and irrigation sector	50,1	--	3.466,2	2.219,0
Manpower sector	391,6	329,4	1.202,1	394
Trade, Financial, and Cooperation sector	85.226,8	99.155,0	19.035,6	407,6
Transportation, Meteorology and geophysical sector	382,7	299,5	8.426,6	3.179,6
Mining and Energy sector	341,3	330,1	6.607,7	1.773,8
Tourism, Post and Telecommunication sector	127,6	1055	918,1	719,8
Regional development and transmigration sector	19.749,0	17.240,3	14.545,8	16.617,7
Environment and space layout	424,8	344,2	932,7	546,3
Education, cultural, and sports	6.045,2	6.249,5	8.381,3	4.758,8
Population and family welfare sector	440,5	418,7	594,3	325,6
Social welfare and health sector	829,1	611,4	4.786,9	2.253,6
Housing sector	27,8	53,2	3.218,4	718,6
Religion sector	1.741,6	1.095,8	627,4	36,5
Science and technology sector	498,5	448,9	900,4	633,3
Law sector	982,8	888,4	230,1	116,0
Civil servant and supervision sector	6.423,8	5.427,5	900,8	492,7
Political, foreign affair, and communication sector	2.710,6	1.588,3	154,0	36,3
Military sector	9.909,7	8.235,9	2.277,4	1.886,8

*Old classification as Law No. 7/1999

**April 1st – December 31st 2000

Source: Ministry of Finance, State Budget (APBN) 2000.

B. Aggregate Tax Revenue

Fiscal year 1999/2000 was a difficult time for the government's finances. The government's effort to increase domestic revenues produced limited success as the economy was still at an early stage recovery, whereas funding from external sources was sporadic at times. Such conditions undermined efforts to use fiscal policy as the stimulus for economic recovery.

As of December 1999, domestic revenues had reached 122.5 trillion rupiah or 94.8% of the fiscal year 1999/2000 budget (Table 1.20). Oil/gas revenues far exceeded the target in line with improvement of international oil prices. In 1999, the average price of Indonesian crude oil was $21.2 per barrel, much higher than the budgeted price of $10.5 per barrel and the average 1998 price of $12.3 per barrel. Thanks to these price increases, oil/gas revenues amounted to 32.5 trillion rupiah, or 155.2% of the target of 21 trillion rupiah.

Domestic revenues from taxes have reached 81.2% of the target reflecting the success of the efforts to improve tax collections. Income tax revenues, which constituted the largest sources of tax revenues, reached 96.8% of the target. Revenues from the value added and luxury taxes are the other main components of tax revenues. Collections of these two taxes reached only 68.8% of the target.

As of December 1999, revenues from excise taxes amounted to 7.8 trillion rupiah, or 77.3% of the government's target. The increase represents the positive result of new regulations linking excises with production and mandated minimum retail prices.

Through December 1999, non-tax revenues stood at 13.3 trillion rupiah or 96.9% of the target. The revenues stemmed from the dividends paid by state owned enterprises, investment funds and services to society.

According to the budget 2000, revenues are expected to be 15.1% of GDP, up from 10.6% of GDP in previous year. Tax revenues, including oil/gas tax, are expected to increase from 8.1% to 10.8% of GDP. In part, higher tax revenues are expected from the phase-out of existing tax exemptions. Non-tax revenues are expected to rise from 2.4% to 4.4% of GDP on expected increases on oil/gas revenues. The oil price assumption was set at $18 per barrel at the fiscal year 2000 budget.

Table 1.20 Government Financial Operations for 2000

Expenditure Items	Budget 1999/2000*	Budget 2000**
	In billions of rupiah	
Total revenues and Grants	129.203	137.695
Domestic revenues	129.203	137.695
Tax revenues	99.480	97.780
Domestic tax	93.935	91.881
Income tax	45.367	53.018
Value added tax	34.597	26.258
Land & building tax	3.247	2.900
Excise duties	10.160	9.271
Other taxes	564	432
Foreign trade tax	5.544	5.898
Import duties	2.950	4.976
Export tax	2.594	922
Non-tax revenues	29.723	39.915
Natural resources revenues	18.119	30.319
Oil & gas	16.224	28.629
Other resources	1.895	1.689
Government portion on state owned enterprise profit	4.000	4.000
Others non-tax revenues	7.603	5.596
Grants	--	--
Total Expenditures	212.699	183.069
Routine expenditures	150.951	143.682
Personnel expenditures	33.569	29.355
Material expenditures	11.039	8.940
Local government expenditures	19.497	17.105
Amortization & interest payments	54.526	58.989
Subsidies	28.020	26.666
Others expenditures	4.299	2.625
Development expenditures	61.747	39.386
Rupiah financing	31.747	23.356
Regional development	16.129	15.139
Central government development	15.618	8.217
Project aids	30.000	22.189
Budget surplus/deficit	-83.495	-45.373
Financing	83.495	45.373
Domestic financing	30.000	22.189
Domestic banks	--	--
Domestic non-banks	30.000	22.189
Privatization proceeds	13.000	5.939
Recovery of bank assets	17.000	16.250
External financing	53.495	23.184
Gross drawing	77.400	31.780
Amortizations	-23.904	-8.596
Total	1.224.200	910.431

*Adjusted to new classification

**April 1st – December 31st 2000

Source: Ministry of Finance, State Budget (APBN) 2000.

Figure 1.5 Tax Revenue Component

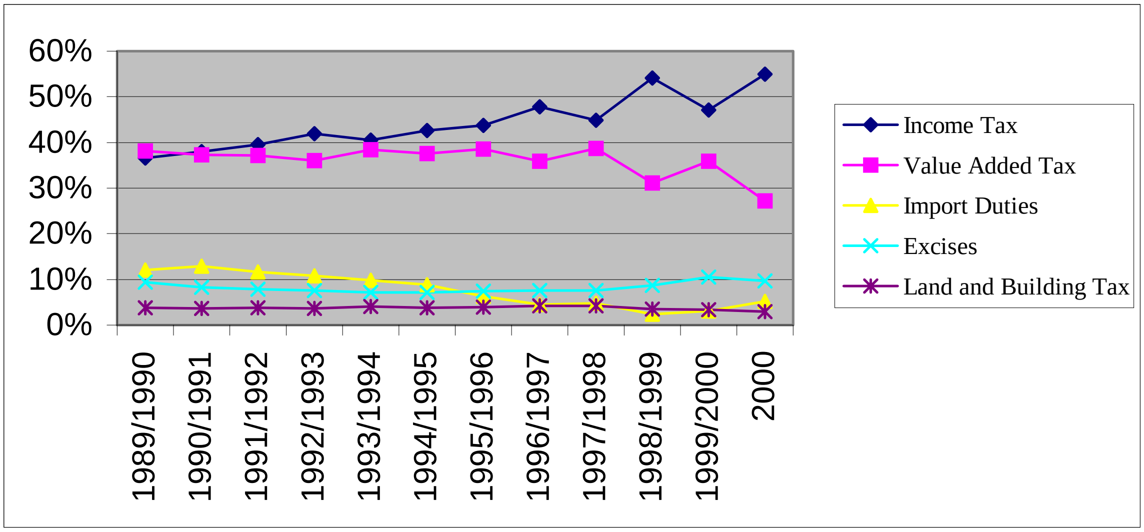


Figure 1.6 The Structure of Government Revenue 2000 Budget

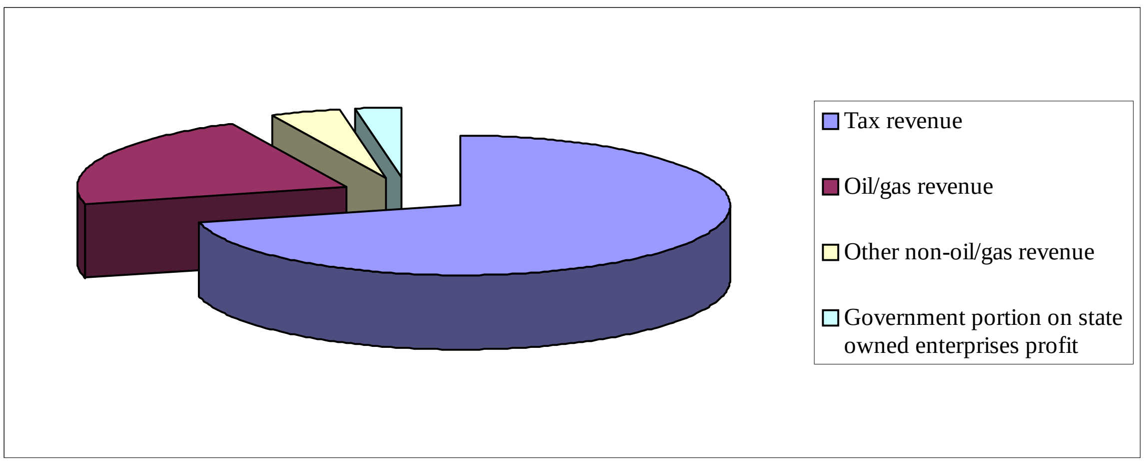
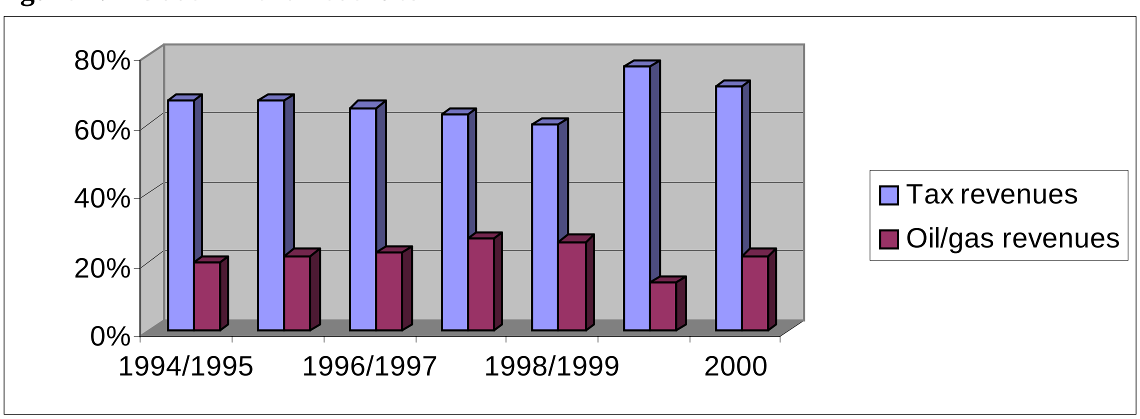


Figure 1.7 Government Revenues



1.3 Tax Structure: Institutions and the Reality

Implementing an effective tax system has played a crucial role in Indonesia's ability to achieve increased domestic revenues and maintain a sustainable approach to economic development. Drawing on the experience of other countries, yet tailored to Indonesia's particular circumstances and needs, the first major overhaul of the tax regime in 1983 was implemented through legislation coming into effect in 1984.

With the rapid development of the economy over the subsequent decade, including the emergence of business forms and practices outside the scope of the previous tax laws, major amending legislation was enacted in 1994 which took effect from January 1, 1995. While prime goals of the new legislation include a further broadening of the tax base in line with the enhanced economic capabilities of taxpayers, and securing increased revenues from taxation, its direction and objectives based on the following main considerations:

- To achieve national self-reliance in State financing and funding of national development, in which tax revenues constitute the chief source.
- To bolster efforts for equitable development by encouraging the expansion of investment, particularly in more remote and less developed areas, in context of widening development and the utilization of natural resources.
- To support efforts to increase export, particularly non-oil and non-gas exports, manufactured goods and services.
- To support the development of small enterprises and optimization of their potential, in the context of rising a segment of society from a state of poverty.
- To support the development of human resources, science and technology.
- To support the preservation of the ecosystem, natural resources and the environment.
- To support efforts to increase fairness in the participation of the people in financing development in accordance with their ability.
- To enhance efforts for creating a more proficient and clean tax apparatus and improving services to Taxpayers, including simplified and more efficient procedures, improved supervision, and improved implementation of relevant legal provisions.

The key elements of tax collection system are as follows:

- Tax collection is the realization of participation by Taxpayers in directly and collectively fulfilling tax obligations.
- Responsibility for tax collection rests with Taxpayers themselves. The government, through tax administration, is responsible for providing guidance, service and supervision in the implementation of tax obligations.
- The tax collection system is expected to avoid a complicated and bureaucratic tax administration.

1.3.1. Law of General Rules and Procedures of Taxation

(Law Number 9 Year 1994 on Amendment of Law Number 6 Year 1983)

Definition of taxpayer is any individual or body who or which, pursuant to the provisions in the tax laws, is required to fulfill tax obligations, including tax collectors or tax withholders of certain taxes. Body is a type of business organization.

Under the self-assessment system, every taxpayer must register in person at the office of the Directorate General of Taxes and obtain a Tax Identification Number. A Taxpayer Identification Number is an administrative instrument for identifying a taxpayer; for that reason, each taxpayer is issued with only one Identification Number. A taxpayer failing to register and obtain an Identification Number is subject to tax penalties. Every taxpayer subject to Value Added Tax must report his business for registration as a Taxable Firm and obtain a Taxable Firm Registration Number, which is the same number with Identification Number.

Every taxpayer shall be obliged to complete, sign and file a tax return with the office of the Directorate General of Taxes covering the taxpayer's place of registration. For an income taxpayer, a tax return functions as an instrument for reporting and accounting for the calculation of tax due and to specify: payment of tax by the taxpayer himself and or through withholding or collection by another party, and payment of withholding or collection of tax due from other individuals or bodies in a tax period. For a taxable firm, a tax return functions as an instrument for reporting and accounting for the calculation of VAT and sales tax on luxury goods actually due and to specify: crediting of inputs tax against output tax, payment of tax made by the taxable firm itself or through another party in a tax period. For a tax withholder, a tax return functions as an instrument for reporting and accounting for tax deducted, collected and deposited. The time limit for filing a tax return shall be: for a periodic tax return, at the latest twenty days from the end of a tax period; for an annual tax return, at the latest three months from the end of a tax year.

In the interest of orderly tax administration and to maintain discipline, a taxpayer who fails to comply with the formal obligation of filing a tax return within the specified time limit will be subject to an administrative penalty in the form of a fine of twenty-five thousand rupiah for a periodic tax return, and fifty thousand rupiah for an annual tax return.

The obligation of every taxpayer to pay tax due is based on the provisions of the tax laws and is not dependent upon the issuance of a tax assessment. In principle, tax is due at the moment a tax object becomes subject to tax. The time tax due is:

a) For income tax withheld by a third party, at that point in time.
b) For employee income tax withheld by an employer, or by another third party on business activities, or by a firm on VAT and sales tax on luxury goods, at the end of a tax period.
c) For income tax, at the end of a tax year.

The time limit for periodic payment of tax due at a point in time or in a tax period, for each type of tax: for individual income tax and withholding tax, ten days before the end of tax period; for corporation income tax, at fifteen days before the end of tax period.

Within ten years from the date tax is due the Director General of Taxes may issue a Tax Underpayment Assessment, which applies only to particular cases such as to taxpayers who evidently or based on the results of an audit, have not fulfilled their formal material obligations.

a) A tax underpayment assessment for income tax is only issued if a taxpayer fails to pay taxes in accordance of the tax laws. Information about underpaid tax is derived from the results of an audit of the taxpayer concerned. A tax underpayment assessment can also be issued if the Director General of Taxes possesses data other than that submitted by the taxpayer concerned and from which it can be ascertained that the taxpayer has not properly fulfilled his tax obligations. And to determine the truth of the data, the taxpayer can be subjected to an audit.
b) A taxpayer who deliberately violates tax obligations involving VAT and sales tax on luxury goods, which causes tax due to be unpaid or underpaid, will be subject to an administrative sanction through the issuance of a Tax Underpayment Assessment plus a surcharge of 100%.
c) If a taxpayer fails to keep books of accounts as prescribed in article 28 of this law or upon auditing fails to comply with the requirements of article 29, as a result of which the Director General of Taxes is unable to ascertain the true business situation and the total taxes due.

The amount of tax underpaid shall be increased by tax administrative penalties of 2% interest per month for a maximum of twenty-four months. The total amount of tax underpaid in a tax underpayment assessment shall be increased by an administrative fine of: for income tax paid by a taxpayer himself the surcharge is 50%; for income tax withheld by a person or other body 100%; and for VAT and sales tax on luxury goods the surcharge is 100%.

After conducting an audit, the Director General of Taxes shall issue a tax overpayment assessment where: for income tax and VAT, tax credit exceeds tax due or tax is paid that is not due; for sales tax on luxury goods, tax paid exceeds the amount due or tax is paid that is not due.

Where a taxpayer believes the amount of loss or amount of tax shown in a tax assessment or the withholding and collection of tax by a third party is incorrect, the taxpayer may lodge an objection with the Director General of Taxes. To enable a taxpayer to prepare an objection with sound reasons, the taxpayer is given the right to enquire about the basis for assessing tax imposed, withheld and collected, and the Director General of Taxes is obliged to meet such a request. And to prevent attempts to avoid or postpone tax payment through the making of an objection, lodgment of the objection does not prevent collection being carried out up to point of holding an assessment.

In the framework of exercising administrative supervision, the Director General of Taxes shall undertake an audit to test compliance in fulfilling tax duties, and such other purposes in the framework of implementing regulations in the tax laws. An examination may be carried out at a tax office (office examination) or at the place of a taxpayer (field examination) and may cover previous years as well as the current year. A taxpayer under examination is obliged to show and submit books, records, documents and such other necessary information pertaining to business activity.

An investigator in tax matters is a particular official in the Directorate General of Taxes who is appointed by the Minister of Justice in accordance with the laws. Investigation of a tax crime is carried out in accordance with regulations prescribed in Law Number 8 Year 1981 on Criminal Law Procedures as supplemented by its implementing provisions.

1.3.2 Law of Income Tax

(Law Number 10 Year 1994 on Amendment of Law Number 7 Year 1983)

A tax subject includes an individual, an undivided estate as a unit, a body and a permanent establishment. Tax subject shall comprise both resident and non-resident. A resident tax subject becomes a taxpayer if he receives or accrues income, while a non-resident tax subject becomes a taxpayer at the time of receipt of income from a source within Indonesia or received or accrued through a permanent establishment in Indonesia.

Furthermore, a resident tax subject shall be:

a) An individual residing in Indonesia or present in Indonesia for more than 183 days in any 12 month period, or an individual present in Indonesia in a tax year and intending to reside in Indonesia.
b) A body established or domiciled in Indonesia.
c) An undivided estate as a unit in lieu of the beneficiaries.

A non-resident tax subject shall be:

a) An individual not residing in Indonesia or present in Indonesia for not more than 183 days in any 12 month period, and a body which is not established or domiciled in Indonesia, conducting business or carrying out activities through a permanent establishment in Indonesia.
b) An individual not residing in Indonesia or present in Indonesia for not more than 183 days within any 12 month period, and a body which is not established or domiciled in Indonesia, receiving or accruing income from Indonesia other than from conducting business or carrying out activities through a permanent establishment in Indonesia.

A tax object shall be income, adheres to the principle of taxation of income in the broadest sense, that is that tax must be paid on each increment in economic capability which is gained or accrued by a taxpayer from whatever source and which can be used for consumption or to add to the wealth of the taxpayer, including:

a) Income from work connected with employment and independent work such as salary, honorarium, income derived by doctors, and so on.
b) Income from conducting business and activities.
c) Income from capital in the form of moveable or immovable property, such as interest, dividends, royalty, rents, gain on the sale of property, and other similar type.
d) Other income, such as cancellation of debt, gifts, and the like.

In calculating the taxable income of a resident individual taxpayer, non-taxable income is deducted from net income. An additional amount of non-taxable allowance over and above the personal allowance, is available to married taxpayers, as follows:

a) For an individual taxpayer 1,728,000 rupiah.
b) For a married taxpayer, an additional 864,000 rupiah.
c) For a married taxpayer whose wife's income is combined with the taxpayer, an additional allowance or 1,728,000 rupiah.
d) For an individual taxpayer, an additional allowances of 864,000 rupiah for each wholly dependent family member, including an adopted child, up to a maximum of three individuals for each family.

Taxable income is the basis for calculating the amount of income tax due. In this case there are two classes of taxpayers, namely resident taxpayers and non-resident taxpayers. For resident taxpayers, there are basically two methods for determining the amount of taxable income; the common calculation method and the calculation norm. In addition, there is a special calculation norm, which is applied to certain taxpayers based on a decree of the Minister of Finance. For non-resident taxpayers, determination of taxable income can be differentiated between: (1) non-resident taxpayer conducting business or engaged in activities through a permanent establishment in Indonesia; and (2) other non-resident taxpayers.

The tax rates applied to the taxable income shall be as follows:

Taxable Income Bracket	Tax Rate
Up to 25,000,000 rupiah	10%
In excess of 25,000,000 rupiah up to 50,000,000 rupiah	15%
In excess of 50,000,000 rupiah	30%

The amount of the tax installment payments during the course of tax year, which shall be paid each month by the taxpayer himself, shall be equal to the tax due according to the annual income tax return for the preceding tax year. Tax, which has been paid for the current year, either by the taxpayer himself or withheld and collected by other parties, may be credited against tax due at the end of the tax year concerned. Taxpayer has an obligation to settle underpaid tax due before filing an annual income tax return. If the accounting year is the same as the calendar year, any tax underpaid must be settled at the latest by March 25th following the end of the tax year.

Withholding Tax

To ensure tax payments in the current tax year are close to the total tax due for the relevant tax year, implementation of collection and payment will be effected through:

a) Withholding of tax by another party where income is earned by a taxpayer from work, service or activities performed as referred to in article 21; collection of tax on income from business as referred to in article 22; and withholding of tax on income from capital, certain services and activities as referred to in article 23.
b) Payments made by a taxpayer himself as referred to in article 25.

Payments of tax in the current tax year are regarded as installments of tax, which can be credited later against the income tax due for the relevant tax year. Having regard to ease, simplicity, certainty, timeliness and other considerations, tax payments in a current tax year are deemed final on certain types of income as provided for in article 4 section (2). Income tax, which is final, cannot be credited against income tax due.

Under article 23, the following income paid or owed by a government body, a resident taxpayer, a permanent establishment, shall be subject to withholding tax by the party obliged to pay in the amount of:

Type of payment	Tax rates
Interest including premiums, discounts and guarantee fee, except received by Bank	15%
Dividends received by individuals	15%
Royalties received except by Bank	15%
Rent and other income in connection with the use of non-land and non-building - Received by individuals and body except Bank	6%
Compensation in connection with services received except by Bank:	
- Technical services	6%
- Management services	6%
- Law and Tax Consultant services	6%
- Interior Designer services	6%
- Landscape Designer services	6%
- Accounting and Bookkeeping services	6%
- Forestry services	6%
- Cleaning services	1.5%
- Oil and gas drilling services by non-permanent establishment	4.5%
- Other oil and gas mining services	4.5%
- Non-oil and gas mining services	4.5%
- Other non-oil and gas mining services	4.5%
- Brokerage services	9%
- Surveyor services	6%
- Actuary services	6%
- Dubbing services	6%
Gifts and rewards	15%

Under article 4, section (2), the imposition of tax on income in the form of interest on deposits and other savings, income from transactions in shares on the stock exchange, income from the transfer of property of land and building and other specific income, may be regarded as final, they are:

Type of incomes	Tax rates
Income from transactions in stock exchange for founders' shares	-
Income from transactions in stock exchange for non-founders' shares	0.1%
Sales transactions in founders' shares	0.5%
Sales of shares owned by venture capital company	0.1%
Gifts from lottery	20%
Interest on deposits, savings, discounts:	
- Received by resident taxpayer	15%
- Received by non-resident taxpayer	20%
Rent and other income in connection with the use of land and building:	
- Rent by body	6%
- Rent by individual	10%

Interests, discounts on bonds which are traded in stock market:	
- Received by resident taxpayer	15%
- Received by non-resident taxpayer	20%
Construction services:	
- Construction planning services by company only	4%
- Construction working services	2%
- Construction supervision services by company only	4%
Non-law and non-Tax Consultant services	4%

Under article 26, the following income, paid by or due from a government body, a resident tax subject, a permanent establishment to a non-resident taxpayer, other than a permanent establishment in Indonesia, shall be subject to withholding tax by the party obliged to pay in the amount of:

Type of payments	Tax rates
Interests	20%
Premiums	20%
Discounts	20%
Dividends	20%
Royalties	20%
Rents	20%
Other income in connection with the use of property	20%
Compensation for services, work and activities performed	20%
Gifts and awards	20%
Pensions and other periodic remuneration	20%
Insurance premiums	10%
Income after tax of permanent establishment	20%

1.3.3 Law of Value Added Tax and Sales Tax on Luxury Good

(Law Number 11 Year 1994 on Amendment of Law Number 8 Year 1983)

Value added tax should be imposed on:

a) A transfer of taxable goods carried out in the customs area by a firm.
   A transfer of goods subject to tax is one arising in the following circumstances:
   - The tangible goods transferred are taxable goods
   - The intangible goods transferred are intangible taxable goods
   - The transfer takes place within the customs area
   - The transfer occurs in the course of business or work of the firm concerned
b) Tax is also collected at the time of import of goods. Collection is carried out through the Directorate General of Customs and Excise.
c) The provision of taxable services in the customs area by a firm.
   Provision of services on which tax is due must fall within the following circumstances:
   - The services provided are taxable services
   - The provision is carried out in the customs area
   - The provision is in the course of business or work of the firm concerned.
d) Intangible taxable goods obtained from outside the customs area and utilized within the customs area.
e) Taxable services obtained from outside the customs area and utilized within the customs area.
f) The export of taxable goods by a taxable firm.

A transferred of taxable goods categorized as luxuries by a producer or the import of such goods is not only subject to value added tax but also sales tax on luxury goods, which should be imposed on:

a) A transfer of taxable goods categorized as luxuries within the customs area by a firm which produces the goods in the course of business or work
b) The importation of taxable goods categorized as luxuries.

Sales tax on luxury goods shall be imposed only once, either at the time of transfer of the taxable goods categorized as luxuries by the firm producing them, or at the time of import.

Value added tax collection basically adheres to the accrual principle, meaning the tax becomes outstanding at the time the taxable goods or taxable services are transferred or at the time the taxable goods are imported, although at the time of transferred they may not have been completely paid for. In certain cases, the Minister of Finance may determine some other time as the moment the tax becomes due. If payment is received before taxable goods or taxable services are transferred, tax shall be due at the time of payment. If there is only partial payment or a down payment before actual transfer has taken place, the tax due is calculated based on the partial payment. Outstanding tax at the time of partial payment is included with the outstanding tax at the time of transfer. If a private person uses an intangible taxable goods or taxable services from outside the customs area within the customs area, tax starts to become outstanding at the time the private person or company begins using the intangible taxable goods or taxable services within the customs area. Consequently, outstanding tax is not related to the time of transfer, but to the time of utilization of the goods or services. If payment is made before intangible taxable goods or taxable services begin to be used, tax shall be due at the time of payment.

The rate of value added tax is 10%. The rate of value added tax on the export of taxable goods is 0%, because value added tax is imposed on the consumption of taxable goods in the customs area, consequently taxable goods which are exported or consumed outside the customs area are subject to zero percent.

Value added tax due should be calculated by applying the rate to the tax base. Input tax paid by a taxable firm at the time of acquisition or import of taxable goods or receipt of taxable services may be credited against the output tax collected by the taxable firm at the time of transferring the taxable goods or services. The crediting must be done in the same tax period. If, within a specific tax period, output tax is greater than input tax, the difference is value added tax, which shall be paid by a taxable firm. If input tax, which may be credited, exceeds output tax, the difference is surplus tax, which may be credited in the next tax period.

The rate of tax for sales tax on luxury goods may be set at different levels, with the lowest rate at 10% and the highest at 50%. The difference between the rate classifications is based on the groupings of goods classified as luxuries. The rate on the export of taxable goods categorized as luxuries shall be 0%.

Sales tax on luxury goods due is calculated by multiplying the sale price or import value by the tax rate. Sales tax on luxury goods is only collected at the time of transfer by the taxable firm, which produces taxable goods categorized as luxuries or on the import of taxable goods categorized as luxuries. Because of this, sales tax on luxury goods is not input tax, and so cannot be credited. As consequences, sales tax on luxury goods may be added to the price of the taxable goods concerned or charge as a cost in accordance with the provisions of the income tax.

1.3.4 Law of Land and Building Tax

(Law Number 12 Year 1994 on Amendment Law Number 9 Year 1983)

Land and building tax is imposed on land and building within Indonesia. A tax subject includes individuals or body that completely have a right on land, and obtain benefits from land, and possess control, and obtain benefits from building.

The tax base is the market value of the land and building. The taxable objects are taxable at minimum of 20% and at maximum of 100% of the price of land and building based on the market value. The tax rate of land and building tax is 0.5%. The exemption ceiling is as much as an amount of 8 million rupiah. The Minister of Finance determines the market value of land and building every three years in most areas and every year in rapidly developing areas.

1.3.5 Law of Stamp & Duty

(Law Number 13 Year 1985)

Documents, which are subject to stamp duty, shall be those in the form of:

a) Agreements and other papers which are made out to serve as instruments of evidence of actions, facts or situations of a civil nature.
b) Notaries' deeds, including their copies.
c) Deeds issued by land title conveyances, including their duplicates.
d) Papers referring to amounts worth more than 1 million rupiah:
   - Which state the receipt of money
   - Which declare the opening of bank accounts or keeping of money in bank accounts.
   - Which contain notifications of account balances at banks.
   - Which contain acknowledgements that money debts are totally or partly settled or calculated.
e) Certificates such as drafts, promissory notes and acceptances whose nominal price is more than 1 million rupiah.
f) Securities in whatever names and forms as long as their nominal price is more than 1 million rupiah.
g) Documents to be used as instruments of evidence before a court:
   - Ordinary letters or internal papers.
   - Papers originally exempt from stamp duty on the basis of their purpose of use, if they serve other aims or are used by other parties in ways deviating from their original purpose.

Documents referred to point a to g shall be subject to stamp duty at the rate of 2,000 rupiah, and documents referred to d to f with a nominal price of more than 250,000 rupiah but not more than 1 million rupiah shall subject to stamp duty at the rate of 1,000 rupiah, and where the nominal price is not more than 250,000 rupiah the stamp duty shall not be due. The rate of stamp duty on cheques and giro notes shall be 1,000 rupiah without nominal price limits.

1.3.6 Income Tax from the Transfer of Titles of Land and Building

(Government Regulation Number 27 Year 1996 on Amendment of Government Regulation Number 48 Year 1994)

Income tax shall be paid on income received or accrued by individuals or companies from the transfer of titles of land and buildings. Transfer of titles as referred to a sale, exchange, transfer agreement, relinquishment or handling over of titles, auction, grant, or any other method of transfer. The amount of income tax is 5% of the gross value of the transfer of titles, except for small houses and for companies that their main business are transfer of titles of land and building is 2%. With the exemption from obligation to pay income tax if the gross amount is less than 60 million rupiah, and a transfer of titles in connection with an inheritance.

1.3.7 Tax Facilities for Capital Investment in Certain Business Fields and Certain Areas

(Government Regulation Number 34 Year 1994)

In implementing the development programmed, the Indonesian nation is aware of the need to increase the role of domestic and foreign investment. Policies are needed to boost investment and equitable distribution of investment throughout the country. In conjunction with that, taxpayers making investment in certain business fields and certain areas are entitled to tax facilities, namely:

a) Accelerated depreciation and amortization.
b) Compensation for losses within a period of more than 5 years but not more than 10 years.
c) Reduced income tax on profit after income earned through foreign investment companies or permanent establishment.

Certain business fields are in economic sectors having a high priority on a national scale, particularly to increase exports and including hard crop plantations and mining business, whose geographical location and fields of activity are stipulated by Presidential Decree. Certain areas are remote areas, which economically have the potential to be developed but are difficult to reach due to poor economic infrastructures.

1.3.8 Income Tax from Sales Transactions in Shares on the Stock Exchange

(Government Regulation Number 41 Year 1994)

Each individual or company that makes a sales transaction in shares on the stock exchange is subject to withholding of income tax on the income received or accrued from the transaction. The withholding of income tax is final. The income tax withheld cannot be credited against the total income tax due on the basis of the annual tax return. All sales transaction in shares, whether founders' shares or non-founders' share, is subject to income tax of 0.1% of the gross value of the transactions. Sales transactions in founders' shares are subject to an additional income tax of 5% of the gross value of the sales transactions. The exemption of additional income tax applies to founders' shares owned by venture capital companies.

1.3.9 The Amendments of Tax Law of 2000

In August 2000, the government announced several new tax laws as amendments to the previous tax laws. The purpose of such amendments are to raise the government revenue from taxes to induce more investment from both domestic and abroad, to bring equality among those subject to taxation both horizontally and vertically, and to avoid double taxation. The new amendments tax laws are as follows.

A. The Law of General Rule and Procedures of Taxation

(Law Number 16 Year 2000 on Amendments of Law Number 9 Year 1994)

With this amended tax law the government believed that the law would strengthen the basic law as the government tools to collect revenue from tax and duty. The law explains more briefly the definition of entrepreneur, entrepreneur that subject to tax obligation, taxes payable, tax credit of income tax. And the government increases the amount of penalty of not filing tax return to become double than before. This new tax law will be effective on January 1st 2001.

B. The Law of Income Tax

(Law Number 17 Year 2000 on Amendments of Law Number 10 Year 1994)

The new amended law on income tax, which will be effective on January 1st 2001, explains more briefly about treatment on written off account receivable that can be expensed under such condition: the written off account receivable has been expended in the commercial income statement, there are some effort to collect the receivable through court, the uncollectible receivable has been announced in the public news, and the list of the uncollectible receivable should be transferred to tax office. Under the new tax law the government increased the amount of non-taxable income. And also change the tax rate applied to the taxable income of an individual taxpayer to become:

Taxable Income Bracket	Tax Rate
Up to 25,000,000 rupiah	5%
In excess of 25,000,000 rupiah up to 50,000,000 rupiah	10%
In excess of 50,000,000 rupiah up to 100,000,000 rupiah	15%
In excess of 100,000,000 rupiah up to 200,000,000 rupiah	25%
In excess of 200,000,000 rupiah	35%

And increases the amount of taxable income bracket for company and permanent establishment to become:

Taxable Income Bracket	Tax Rate
Up to 50,000,000 rupiah	10%
In excess of 50,000,000 rupiah up to 100,000,000 rupiah	15%
In excess of 100,000,000 rupiah	30%

C. The Law of Value Added Tax and Sales Tax on Luxury Good
(Law Number 18 Year 2000 on Amendments of Law Number 11 Year 1994)

Under the new amended law of value added tax, which will be effective on January 1st 2001, the government gives more explanation about non-taxable goods and non-taxable services. And increases the rate of sales tax on luxury good shall be a maximum of 75%.

D. The Law of Tax Collection with a Distress Warrant
(Law Number 19 Year 2000 on Amendments of Law Number 19 Year 1997)

The new amended tax law, which will be effective on January 1st 2001, the government add an articles that states the competence of tax authority to conduct taxpayer's compliance to fulfill tax obligations.

E. The Law of Tax on Conversion of Land and Building Ownership
(Law Number 20 Year 2000 on Amendments of Law Number 21 Year 1997)

The new tax law on conversion of land and building ownership, which will be effective on January 1st 2001, explains more briefly about the meaning of conversion of ownership of land and building and the meaning of the right on land. And also increases the tax exemption to become 60 million rupiah.

1.3.10 International Taxation Agreements

The government of Indonesia has signed up to 45 treaties with foreign countries, desiring to conclude and agree for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income. The list of the treaty is as follows.

Table 1.21 The List of Tax Treaty Rates between Indonesia and Foreign Countries

No.	Country	Starting Date	Dividend		Interest			Royalty		Branch Profit Tax
			Portf. Invest	Substant Holding	General	Spec Case	Cent Bank	General	Special Case	
1	Australia	1/7/93	15%	15%	10%	-	0%	15%	10%	15%
2	Austria	1/1/89	15%	10%	10%	-	0%	10%	-	12%
3	Belgium	1/1/75	15%	15%	15%	10%	0%	10%	-	15%
4	Bulgaria	1/1/93	15%	15%	10%	-	0%	10%	-	15%
5	Canada	1/1/80	15%	15%	15%	-	0%	15%	-	15%
6	Czech	1/1/97	15%	10%	12.5%	-	0%	12.5%	-	12.5%
7	Denmark	1/1/87	20%	10%	10%	-	0%	15%	-	15%
8	Finland	1/1/90	15%	10%	10%	-	0%	15%	10%	15%
9	France	1/1/81	15%	10%	15%	10%	0%	10%	-	10%
10	Germany	1/1/92	15%	10%	10%	-	0%	15%	10%7.5%	10%
11	Hungary	1/1/94	15%	15%	15%	-	0%	15%	-	-
12	India	1/1/88	15%	10%	10%	-	0%	15%	-	10%
13	Italy	1/1/96	15%	10%	10%	-	0%	15%	10%	12%
14	Japan	1/1/83	15%	10%	10%	-	0%	10%	-	10%
15	Jordan	1/1/99	10%	10%	10%	-	0%	10%	-	N/A
16	Kuwait	1/1/99	10%	10%	5%	-	0%	20%	-	10%
17	Luxembourg	1/1/95	15%	10%	10%	-	0%	12.5%	10%	10%
18	Malaysia	1/1/87	15%	15%	15%	-	0%	15%	-	12.5%
19	Mauritius	1/1/99	10%	5%	10%	-	0%	10%	-	10%
20	Netherlands	1/1/71	15%	10%	10%	-	0%	20%	10%5%	9%
	Renegotiation	1/6/94	15%	10%	10%	-	0%	10%	-	9%
21	New Zealand	1/1/89	15%	15%	10%	-	0%	15%	-	-
22	Norway	1/1/91	15%	15%	10%	-	0%	15%	10%	15%
23	Pakistan	1/1/91	15%	10%	15%	-	0%	15%	-	10%
24	Philippines	1/1/83	20%	15%	15%	10%	0%	15%	-	20%
25	Poland	1/1/94	15%	10%	10%	-	0%	15%	-	10%
26	Romania	1/1/00	15%	12.5%	12.5%	-	0%	12.5%	-	12.5%
27	Saudi Arabia'	1/1/89	-	-	-	-	-	-	-	-
28	Singapore	1/1/92	15%	10%	10%	-	0%	15%	-	15%
29	South Africa	1/1/99	15%	10%	10%	-	0%	10%	-	10%
30	Spain	1/1/00	15%	10%	10%	-	0%	10%	-	10%
31	South Korea	1/1/90	15%	10%	10%	-	0%	15%	-	10%
32	Sri Lanka	1/1/95	15%	15%	15%	-	0%	15%	-	20%
33	Sweden	1/1/90	15%	10%	10%	-	0%	15%	10%	15%
34	Switzerland	1/1/90	15%	10%	10%	-	0%	12.5%	-	10%
35	Syria	1/1/99	10%	10%	10%	-	0%	20%	-	10%
36	Taiwan	1/1/96	10%	10%	10%	-	0%	10%	-	5%
37	Thailand	1/1/82	15%	15%	15%	-	0%	15%	10%	20%
38	Tunisia	1/1/94	12%	12%	12%	-	0%	15%	-	12%
39	Turkey	1/1/01	15%	10%	10%	-	0%	10%	-	15%
40	UAE	1/1/00	10%	10%	5%	-	0%	5%	-	5%
41	U.K.	1/1/76	15%	10%	10%	-	0%	15%	10%	10%
	Renegotiation	1/1/95	15%	10%	10%	-	0%	15%	10%	10%
42	Ukraine	1/1/99	15%	10%	10%	-	0%	10%	-	10%
43	USA	1/2/91	15%	15%	15%	-	0%	15%	10%	15%
	Renegotiation	1/2/97	15%	10%	10%	-	0%	10%	10%	10%
44	Uzbekistan	1/1/99	10%	10%	10%	-	0%	10%	-	10%
45	Vietnam	1/1/00	15%	15%	15%	-	0%	15%	-	10%

') The treaty with Saudi Arabia is limited to both of country's airline companies.
Source: Ministry of Finance – Directorate General of Taxes.

Government domestic revenue in 2000 budget decreased by 3.2% (Table 1.22) compared to 1999/2000 budget due to the change of period of fiscal year to be January until December, so in

2000 fiscal year the period is from April to December. In fiscal year 2000 domestic sources are expected to provide 137.6 trillion rupiah. Within domestic revenues, government receipts from oil and gas sector are expected to reach 39.9 trillion rupiah, this receipts represent 29 percent of total domestic revenues. Meanwhile the largest share of domestic revenues is expected to come from non-oil and gas receipt, which are projected 97.7 trillion rupiah or 71 percent of domestic revenues. And revenues from taxes are expected to account for 88.2 trillion rupiah, equivalent to 64 percent of government income from domestic sources compared to 66.6 percent in fiscal year 1999/2000. The main sources of taxes revenues are income tax of 60 percent, value added tax of 30 percent, land and building tax of 2.7 percent, and other taxes of 7.3 percent of total taxes revenue in fiscal year 2000.

Table 1.22 Government Revenue

Description	95/96	96/97	97/98	98/99	1999/2000		2000
					Budget	Actual*	Budget
Oil/gas and non-oil/gas revenue	73,014	87,630	112,276	158,027	142,203	126,201	137,695
Oil and gas receipt	16,055	20,137	30,559	41,367	20,965	32,535	39,915
Oil	11,964	14,783	22,264	25,957	12,443	16,843	21,684
Gas	4,091	5,354	8,295	15,410	8,522	15,692	8,633
Non-oil/gas receipt	56,959	67,493	81,717	116,660	121,238	93,666	97,780
Income tax	21,012	27,062	34,388	55,943	40,626	39,310	53,018
VAT and sales tax on luxury goods	18,519	20,351	25,199	27,789	34,597	23,343	26,258
Import duties	3,029	2,579	2,999	2,306	2,950	2,480	4,976
Excise duties	3,593	4,263	5,101	7,733	10,160	7,858	9,271
Export duties	186	81	129	4,630	2,595	768	922
Land and building tax	1,894	2,413	2,641	3,566	3,247	2,751	2,375
Others	453	591	478	413	565	404	957
Non-tax and net oil receipt**	8,273	10,153	10,782	14,280	26,499	16,751	9,596
Net other revenues***	3,000	2,055	9,270	4,994	0	9,777	0
Total of domestic revenue	76,014	89,685	121,546	163,021	142,203	135,978	137,695

* As of December 31, 1999
** For 98/99 and 99/00, including of state owned enterprises
*** Errors and omissions
Source: Ministry of Finance.

1.4 Country-Specific Fiscal Issues

1.4.1 Outbreak of The Crisis

Indonesia is in deep crisis since 1997. A country that achieved decades of rapid growth, stability, and poverty reduction, is now near economic collapse. Within the space of one year Indonesia has seen its currency fall in value by 80 percent, inflation soar to over 50 percent, the economy swing from rapid growth to even more rapid contraction, unemployment climb rapidly, and the stock exchange lose much of its value. Foreign creditors have withdrawn and investors have retreated their capital. Unfortunately, the crisis hit when Indonesia was experiencing its worst drought in fifty years, and the international oil price was registering a sharp decline. Social unrest has erupted and shaken to its very core the political stability of the nation. Years of development and poverty reduction are at risk.

The IMF then announced a multibillion-dollar assistance package as a rescue plan for Indonesia that was intended to restore the economy. And recent developments have been broadly consistent with the IMF program of macroeconomic framework. Growth in the last quarter of 1999 exceeded expectations, and the economic recovery has been sustained in the first quarter of 2000. Indonesia now expects 2000 growth to be at top of the targeted 3-4 percent range. And inflation should be within the targeted 5-6 percent range.

1.4.2 Economic Restructuring

A. Fiscal Reform

The fiscal reform agenda is being implemented as envisaged. The parliament has approved the amendments law of income tax, value added tax, and general rules and procedures of taxation as already explained above. Other tax reforms affecting the tax privileges for the Integrated Economic Development Zones; the rationalization of import tariffs on capital goods; and the imposition of a flat 5 percent duty on all exempted goods with non-zero rates.

The government also remains committed to delivering the fiscal transparency, such as a performance audit of the Tax Office by the State Audit Board (BPKP), the Supreme Audit (BPK) has initiated steps to take account of all extra-budgetary funding in its audits of public institutions, which involves taking decisions about the integration of the remaining off-budget funds with the central government budget.

B. Decentralization

The government intensified preparation for implementing fiscal decentralization in 2001 within the framework of Law Number 22 and 25 of 1999, about regional government and financial relations between the central government and the regions respectively, and will be guided by revenue transfer to sub-national governments that will be consistent with expenditure responsibilities, and specific mechanisms will be developed to ensure that any borrowing by sub-national governments is kept within strict limits. Recently established Regional Autonomy Advisory Council and the Coordinating Team are now leading the decentralization process. The Minister of Finance is taking the lead in all fiscal aspect of decentralization. And the Ministry of State Apparatus has been appointed to resolve the transfer of the civil servants.

C. Privatization of State Enterprise

The government has updated its master plan for state enterprise reform and privatization for the period 2000 – 2002. The master plan promotes fast track privatization for enterprises in competitive industries, and deals with loss-making enterprises that have no prospect of returning to commercial viability. The fiscal year 2000 privatization program now includes a total of 19 enterprises. The Ministry for Investment and State Enterprises is also preparing to issue shortly guidelines on improved privatization procedures with the assistance of international consultant.

D. Indonesian Bank Restructuring Agency (IBRA)

IBRA is established to take control of high-risk institutions, or force restructuring of the institutions, or liquidate, which threaten macro stability, and to drive corporate restructuring and debt recovery. IBRA was found during the banking crisis, where in November 1997, February 1998, April 1998, August 1998, and March 1999 where the government intervened the bank with four main instruments employed were: closure; soft open bank intervention by IBRA; full takeover by IBRA; and re-capitalization. From the onset of the crisis, 65 banks have been closed, 13 nationalized, 7 private banks re-capitalized, and 4 of the 7 state banks merged, called Bank Mandiri.

Now IBRA is continuing to improve its transparency by adopting a new governance framework to ensure IBRA has the independence it needs to carry out its mandate. At the center of the framework is a new governing board, clearly separated from the political process, and composed of independent professionals, and attached to the Board will be an independent audit committee. And IBRA will report to the Ministry of Finance.

IBRA focus is to drive asset sales and debt restructurings, return assets to the private sector quickly, and achieve budgetary collection targets. For fiscal year 2000, IBRA announced a quarterly schedule of asset sales procedures and projected cash collections of 18,9 trillion rupiah. The government recognizes that the asset recovery targets require strong action be taken against all non-cooperative debtors and shareholders. The inter-ministerial Committee for Resolving the Cases of Recalcitrant Debtors was established. The committee will decide a coordinated strategy for all IBRA problem cases, including prosecutions, using IBRA special powers to take over debtors' assets, and imposing administrative sanctions.

E. Bank Re-capitalization Program

One of the government measures in the bank-restructuring program is bank re-capitalization that covers all banks, including banks under IBRA supervision, except joint banks and foreign banks offices. This program is designed to sustain banks that have viable prospect to continue to operate and grow. The bank re-capitalization program was initiated to deal with deficiency of capital that most banks faced. As an initial selection step, the government classifies banks into three categories based on their respective capital adequacy ratio (CAR). Banks with CAR of 4% or more are not required to participate in the re-capitalization program but they have to prepare their business plans. Banks with CAR from -25% up to less than 4% are required to participate in the re-capitalization program as long as they meet certain criteria. Meanwhile, banks with CAR less than -25% have 30 days to add to their equity base or improve their productive asset quality to meet the criteria for inclusion in the re-capitalization program. In determining those categories Bank Indonesia conducted due diligence involved international auditors.

F. State Bank Restructuring

With the decision having been made to merge 4 of the state banks into a new institution, called Bank Mandiri, the government focus shifted to the three remaining state banks (BNI, BRI, and BTN). Bank Mandiri now is implementing its business plan, closing unnecessary branches, and bringing virtually all of its assets and liabilities on-line. The Ministry of Finance will work with Bank Mandiri to develop an appropriate strategy for reducing the bank's dependency on high cost deposits. Meanwhile, to ensure that the bank's new policies for credit approval and risk management are executed efficiently.

Bank BNI's (Bank Nasional Indonesia) restructuring is also underway. The final tranche of re-capitalization bonds (32 trillion rupiah) was issued on July 2000, after an international consulting firm verified that the bank has complied with its interim performance contract, and an international bank was engaged to assist in credit risk management and loan workouts.

Regarding Bank BRI (Bank Rakyat Indonesia), the bank's business plan has been validated by the Restructuring Committee, an interim performance contract has been signed, and the first tranche of re-capitalization bonds issued on July 2000 for 70% of the bank's re-capitalization needs.

Regarding Bank BTN (Bank Tabungan Negara), a new management has prepared a business plan with its international advisors. The business plan which is refocusing the bank mortgage lending, has now been approved by the Restructuring Committee. The first tranche (70% of total) of its re-capitalization was approved by Parliament on July 2000.

G. Corporate Restructuring

The August 1998 Frankfurt Agreement led to the creation of an institutional framework for corporate debt restructuring which depended on the government sponsored Jakarta Initiative Task Force (JITF). JITF has provided a framework for voluntary out of court debt negotiations following guidelines known as the Jakarta Principles which are based on “London Rules” developed by the Bank of England. Between May 1st and July 15th 2000, the value of debt restructured under the JITF was $3 billion, bringing the total of restructured debt to $5 billion. With the strategic objective is to restructure a total $12 billion of debt by April 2001.

The Indonesian Debt Restructuring Agency (INDRA) was also created in late 1998 and offers a facility for hedging against devaluation of the rupiah for restructuring agreements, which are under implementation.

1.5 Conclusion: Where We Stand and Where We Go

Social and political developments have allowed the new government to take step in improving governance and transparency. A number of measures have already been taken that serve as a signal that this government breaks with the ways of the past. This includes efforts by the new government to review and dismantle government contract that were offered through corruption, collusion and nepotism. But improving governance needs to be a policy priority.

Again the political condition is absolute condition for economic recovery. The Indonesian government now is facing a difficulties associated with the upholding of the law. The Suharto case has become a major indicator of legal reform. Suharto has been granted privileges from early in the inquiry and investigation process all the way through to the present trial. Could the police, prosecutors, judges and lawyers have the courage and will to uphold the law indiscriminately according to the principle of equality before the law?

Many government programs to protect the poor have not been put in place. The real tragedy of the crisis is its effects on the poor. They are confronted by falling real wages, fewer employment opportunities, and rising prices of food and other essentials, including health and education services. To overcome these problems the government must ensure the availability of food and other essentials at affordable prices. This means subsidizing commodities, especially rice, and ensuring effective distribution. The government must create employment opportunities and help generate incomes through labor-intensive public works implemented by local communities. The government needs to preserve the availability of social services especially basic health and education in reaching the poor.

Recovering from the desperate financial crisis situation will be slow and difficult. Much depends on whether Indonesia can achieve the necessary political stability for implementing a difficult and complex agenda of economic reforms, and whether it will receive the necessary financial support from the international community. The government policy focus has to be reflected in the fundamental nature of the reforms and with consistent implementation of the reform program and adequate foreign financing there will be a good prospects that Indonesia will return to sustained growth in the medium term.

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