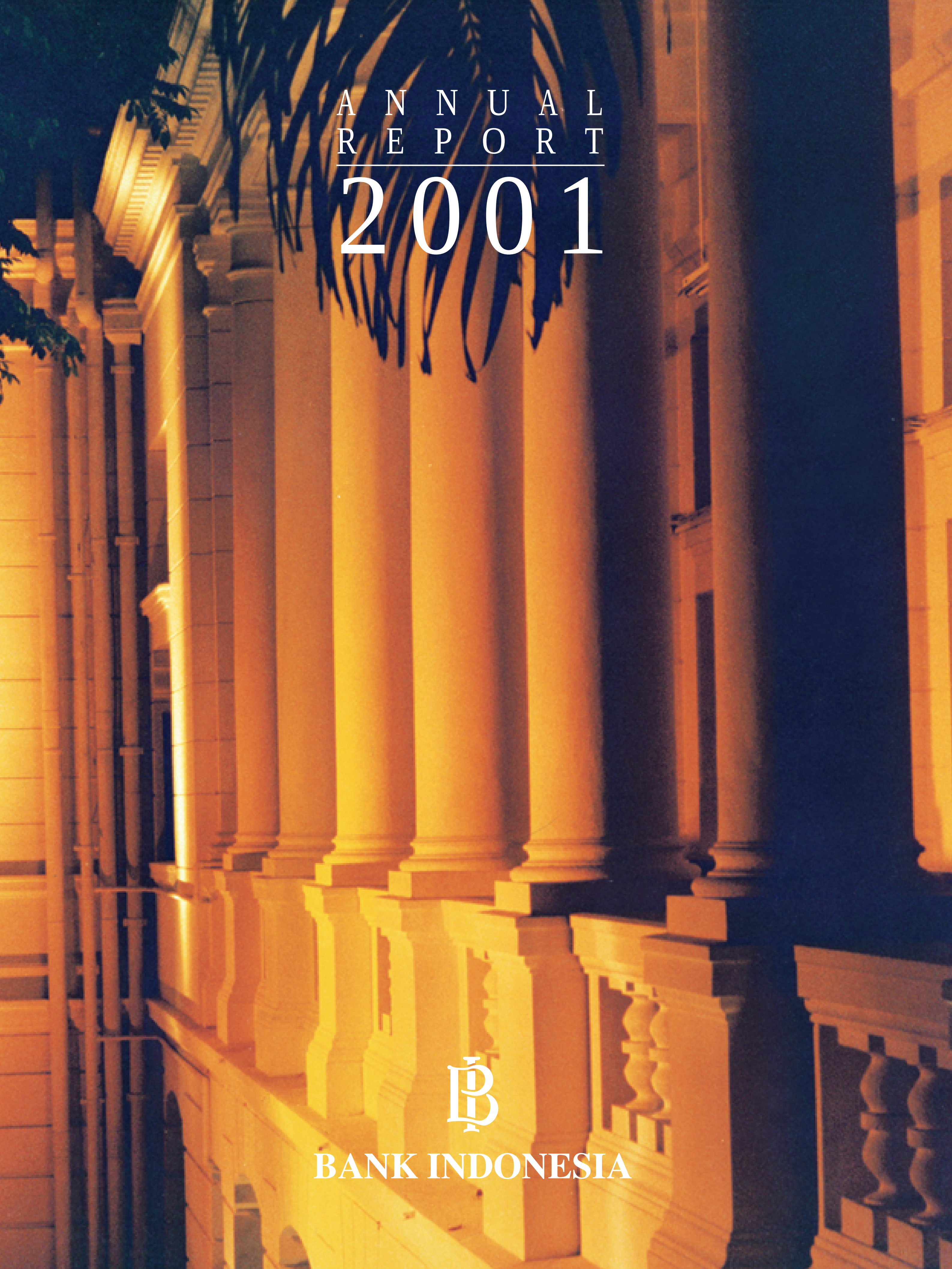

ANNUAL REPORT 2001

BANK INDONESIA

This report presents a comprehensive review on

"The Evaluation of Monetary Policies in 2001 and Policy Directions for the year 2002".

A preliminary version of this material was presented to the House of Representatives

and the public through the media on January 15, 2002, pursuant to Article 58

of the Act Number 23 of 1999 on Bank Indonesia

ANNUAL REPORT 2001

BANK INDONESIA

ISSN 0522 - 2575

Vission :

“To be recognized, domestically and internationally, as a credible central bank through the strength of our values and achievement of low, stable rates of inflation”

Mission :

“To achieve and maintain price stability by maintaining moneter stability and by promoting financial system stability for Indonesia’s long term sustainable development”

Values :

“Competence, Accountability, Integrity, Cohesiveness, Transparency”

Symbols, Reporting Period, and Source of Data

Revised figures	r
Provisional figures	*
Incomplete figures	**
Data are not yet available	. . .
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Nil or less than the last digit	– –
United States Dollar	$ (dollar)

Reporting period is January 1, 2001 to December 31, 2001

Source of data is Bank Indonesia unless mentioned otherwise

BOARD OF GOVERNORS OF BANK INDONESIA

As of December 31, 2001

Sitting from left to right :

Syahril Sabirin
Governor

Anwar Nasution
Senior Deputy Governor

Standing from left to right :

Aulia Pohan
Deputy Gubernur

Miranda S. Goeltom
Deputy Gubernur

Achjar Iljas
Deputy Gubernur

Preface

In praise of God the Almighty, allow me to present Bank Indonesia's Annual Report for the year 2001 to the respected readers. *This report is one of the manifestations of Bank Indonesia's accountability as regulated in Article 58, Act 23 of 1999 concerning Bank Indonesia. This report presents policy measures that have been adopted and results that have been achieved by Bank Indonesia in the monetary, banking, and payment system areas during 2001 as well as Bank Indonesia's policy directions for 2002. This report also describes the developments and problems that have arisen in the Indonesian and international economies during the reporting year as well as their prospects for 2002.*

The previous year saw another difficult period for the Indonesian economy. *Several underlying macroeconomic assumptions postulated at the beginning of 2001 in determining the inflation target and Bank Indonesia's policies- did not meet our expectations. Consequently, the economy grew by only 3.3%, which fell short of our earlier estimate of 4.5%-5.5%. While that growth rate was higher than that in the region, it was not adequate to absorb increasing new entrants of Indonesia's work force. Investment and exports, which had been expected to provide the main impetus for economic recovery, appeared to grow well below that in 2000. As regard the exchange rate, the rupiah depreciated quite sharply with higher volatility in 2001 than in the previous year. The depreciation gave a significant rise in the inflation rate, with the CPI inflation of 12.55%, well above our initial estimate of 6.0%-8.5%.*

The difficulties experienced in the economy during 2001 were mainly attributable to remaining domestic problems which were aggravated by the impact of the global economic slowdown, which adversely affected Indonesia's exports. The prevailing domestic problems included high business risks, bank-intermediation which had not function well and exchange rate volatility which was largely susceptible to shifts in market sentiment. While we noted progress in the last few years, challenges remained during the reporting year.

Those remaining challenges were indeed very complicated as they entailed various inter-related dimensions. *Solutions to these problems called for innovative steps, willingness to sacrifice, and close coordination among various levels had hampered decision making and implementation of important decisions in various areas. As a result, implementation of policies that had previously been agreed by consensus during the reporting year-particularly those related to bank restructuring, privatization, debt restructuring, and strengthening the legal system including apparatus—progressed only slowly. In fact, some of those policies were not implemented at all.*

These various problems have narrowed the room for Bank Indonesia to reign in inflation. *Bank intermediation which had not fully functioned hampered the monetary transmission process, thereby reducing the effectiveness in keeping inflation in check and stabilizing the exchange rate volatility. In addition, persistently high business risk had reduced incentives to invest. Consequently, expansion of production and distribution infrastructure which could have helped contain inflationary pressure was very limited. Likewise, foreign capital inflows-which could have eased the pressure on rupiah appeared to be smaller than previously expected. This combined with low confidence in the national banking sector had further limited the supply of foreign exchange. Meanwhile, excess demand for foreign exchange remain high due to substantial external debt service obligations due mainly to the slow progress in private debt restructuring in addition to existing concern over domestic, socio-political, and security instability. These factors characterized the supply of and demand for foreign exchange in 2001, which mainly beyond the control of monetary policy.*

Efforts to keep inflation in check became more difficult in 2001 because the sources of inflationary pressures stemmed mainly from the supply side or cost push inflation. *As commonly known, monetary policy has limitations in controlling inflationary pressure originating from the supply side; it can only influence economic activity from the demand side. An adoption of tight monetary policy in controling inflation originating from the supply side could have run counter to economic activity. Furthermore, its effectiveness during 2001 was still hampered by bank intermediation which had not fully functioned. It should be noted that the rise in production costs during 2001 stemmed in particular from the pass-through impact of the rupiah depreciation and from the impact of upward adjustment of administered prices such as fuel prices, electricity tariffs, and import duties in addition to a rise in minimum wages. The impact of the upward adjustments and income policy on inflation turned out to be larger than our initial estimate. Furthermore, a decline in the production of foodstuffs also contributed to inflationary pressures from the supply side.*

Despite the complexity of the problems, Bank Indonesia sought to contain the inflationary pressure through the pursuit of a tight bias monetary policy. *This stance was taken since price stability was* *a prerequisite for sustained economic development. To this end, Bank Indonesia had done its best to mop up excess liquidity in the economy so as not to fuel further pressure on inflation and the exchange rate. Operationally, this policy was conducted through the control of the growth of base money in line with a predetermined target. In view of the complexity of the situation as mentioned above, we exercised prudence that such a pursuit would not lead to an excessive rise in interest rates.*

Amid the difficulties, we also noted some favorable developments. Built upon this progress, we can move forward for sustained economic recovery in the years ahead. *Among the positive developments was the change to a new government through a democratic process, which has contributed to recently improved socio-political condition. In the banking sector, although intermediation had not fully recovered, most banks succeeded in meeting the minimum 8% capital adequacy ration (CAR) requirement set by Bank Indonesia. Furthermore, the quality of their productive assets improved significantly as reflected in a drop in non-performing loans (NPLs) ratio. Bank Indonesia has also laid a stronger foundation for the banking system resilience through the development and improvement of infrastructure and supervision system. On the external side, developed countries had taken prompt measures in the form of fiscal stimulus and easy monetary policy so as to prevent their economies from slipping into a recession, a step that has raised expectation of a global economic recovery.*

In 2002, Indonesia's economy is expected to continue facing quite serious challenges. *However, built upon previous progress as mentioned above in tandem, with the commitment of the government in continuing structural reforms, Bank Indonesia estimates that the economy will grow in the range of 3.5%-4.0% in 2002. In addition, the exchange rate has the potential to strengthen provided that the government is consistent in implementing its reform program. Inflationary pressure is estimated to remain unabated, yet at a lesser extent, due to the government's plan to introduce other further upward adjustments in administered prices in addition to the high inflation expectation.*

In line with its tasks and authority, Bank Indonesia will seek to create conducive conditions for sustained economic recovery through the maintenance of monetary stability and control of inflation. *To this end, based on domestic and international economic prospects, Bank Indonesia sets the CPI inflation target in the range of 9.0%-10.0% for 2002. In the next five years, Bank Indonesia has taken a commitment to gradually reduce inflation to around 6.0%-7.0%. I need to emphasize that starting this year Bank Indonesia adopts the CPI inflation rate as the indicator for the inflation target. Previously, as already known, in 2000 and 2001 the indicator for inflation target, was the CPI inflation excluding the impact of administered prices and incomes policies. We made this change because the CPI inflation is more readily acceptable and more transparent for the* *public compared with the inflation target indicator that we used previously. Through this change, it is expected that Bank Indonesia can strengthen its capability in influencing the public's expectation on inflation.*

To ensure achievement of that inflation target, Bank Indonesia will take the necessary policies in the areas of monetary, banking and payment system. *In addition, in view of the existing internal weaknesses that need to be addressed, we have determined to launch Bank Indonesia Transformation Program. Having completed the preparation and formulation process, some parts of the program are scheduled for implementation in 2002. In this regard, we are also seeking support from stakeholders, so as to ensure improvements in Bank Indonesia's performance. Therefore, we welcome and appreciated constructive suggestions and criticisms.*

Before concluding this preface, ***I wish to invite the readers to review what we have experienced and steps that we have taken since this multi-dimensional crisis hit this country.*** *I will summarize in the following points:*

- *This monetary and economic crisis is basically a crisis of confidence, that is, confidence in Indonesia's economic future, confidence in exchange rate stability, and confidence in legal certainty.*
- *The steps that we have taken to overcome this crisis are appropriate, as those taken in other countries that have been successful in recovering from the same crisis, such as Thailand and Korea.*
- *Initially, a national consensus had been reached on the policies that proved to be successful in bringing inflation down to a very low rate and the exchange rate to a reasonable level. However, further unfavorable developments as reflected in political turmoil, unclear policy direction, and hostile attitudes whereby parties found fault with one another, have undermined the hard-won achievements. In several instances, there has been a reluctance or lack of courage in making political tough decisions. Under such circumstances, Indonesia's economy compares to a patient taken half of a dose of medicine that naturally will not cure the illness.*
- *The coming into power of a new government augurs a new hope for improvements and renewed steps to overcome the crisis. The various preliminary measures that have been taken by the new government have strengthened confidence in Indonesia's economic prospect. Nevertheless, a number of politically difficult decisions will have to be made by the government in the coming weeks and months. To this end, to ensure success in this endeavor calls for common perspectives, determination, and a national consensus.*

Finally, on behalf of Bank Indonesia's Board of Governors, I wish to express my thanks to all Bank Indonesia's management and staff who have worked hard professionally during 2001 in assuming the mandate of Act 23 of 1999 concerning Bank Indonesia. I also wish to express my gratitude to parties outside Bank Indonesia who, *for all this time, have lent sincere support and cooperation to Bank Indonesia. To the readers, I hope that this report can be a useful reference.*

May God the Merciful bless us all and lighten our steps to a better future.

Jakarta, February 2002.

Governor of

Bank Indonesia

Syahril Sabirin

chapter 1 OVERVIEW

chapter 1

OVERVIEW

At the beginning of 2001, Bank Indonesia predicted that the economic recovery of the previous year would gather momentum during 2001. This optimism was based on the expectation that economic restructuring in various areas would achieve meaningful progress, particularly as regards corporate debt restructuring and improved bank intermediation. A stronger economic recovery was also supported by expectations that socio-political and security conditions would improve. In addition, the world economy was expected to remain strong despite a slowdown from the previous year.

Reflecting some optimism around the beginning of 2001, Bank Indonesia estimated that GDP growth in 2001 would reach 4.5%-5.5%. Besides consumption, this expansion would be achieved through investment and exports that were expected to provide the main impetus for the growth. In addition, Bank Indonesia set an inflation target, excluding the impact of administered prices and income policy of 4.0%-6.0%. Additional inflation from the impact of administered prices and income policy was expected to be around 2.0%-2.5%, hence the CPI inflation was expected to reach 6.0%-8.5%. In line with this inflation target, base money growth through the end of 2001 was set at 11.0%-12.0%.

As 2001 developed, these various assumptions and estimates fell short of previous expectations. Existing fundamental problems in the economy remained unresolved; in fact several of those problems even tended to deteriorate (Diagram 1.1). The world economy slowed and even slipped into recession at the end of the first quarter of 2001. On the domestic side, socio-political and security conditions remained unstable. During the first half of 2001 domestic environment was mainly dominated by considerable political turmoil, which climaxed with a change in administration in mid-2001. Despite some progress, economic restructuring faced a number of constraints, hence various domestic structural problems remained in tandem with persistently high business risk and uncertainties.

The prevailing problems had adversely affected economic and monetary developments through 2001. In the real sector, investment and production were mainly hampered by high business risk and uncertainty, slow corporate debt restructuring, and internal bank and corporate consolidation. Exports also slackened, due mainly to the world economic recession. In the banking sector despite some improvements, intermediation function was not fully restored. The extension of bank credit and its absorption by the real sector were not rapid enough, owing to various problems encountered by the real sector and the ongoing internal bank consolidation. In such conditions, most funds were invested in the financial assets rather than for financing investment and production in support of economic recovery. In addition, bank intermediation, which was not fully restored, also contributed to exerting pressure on the

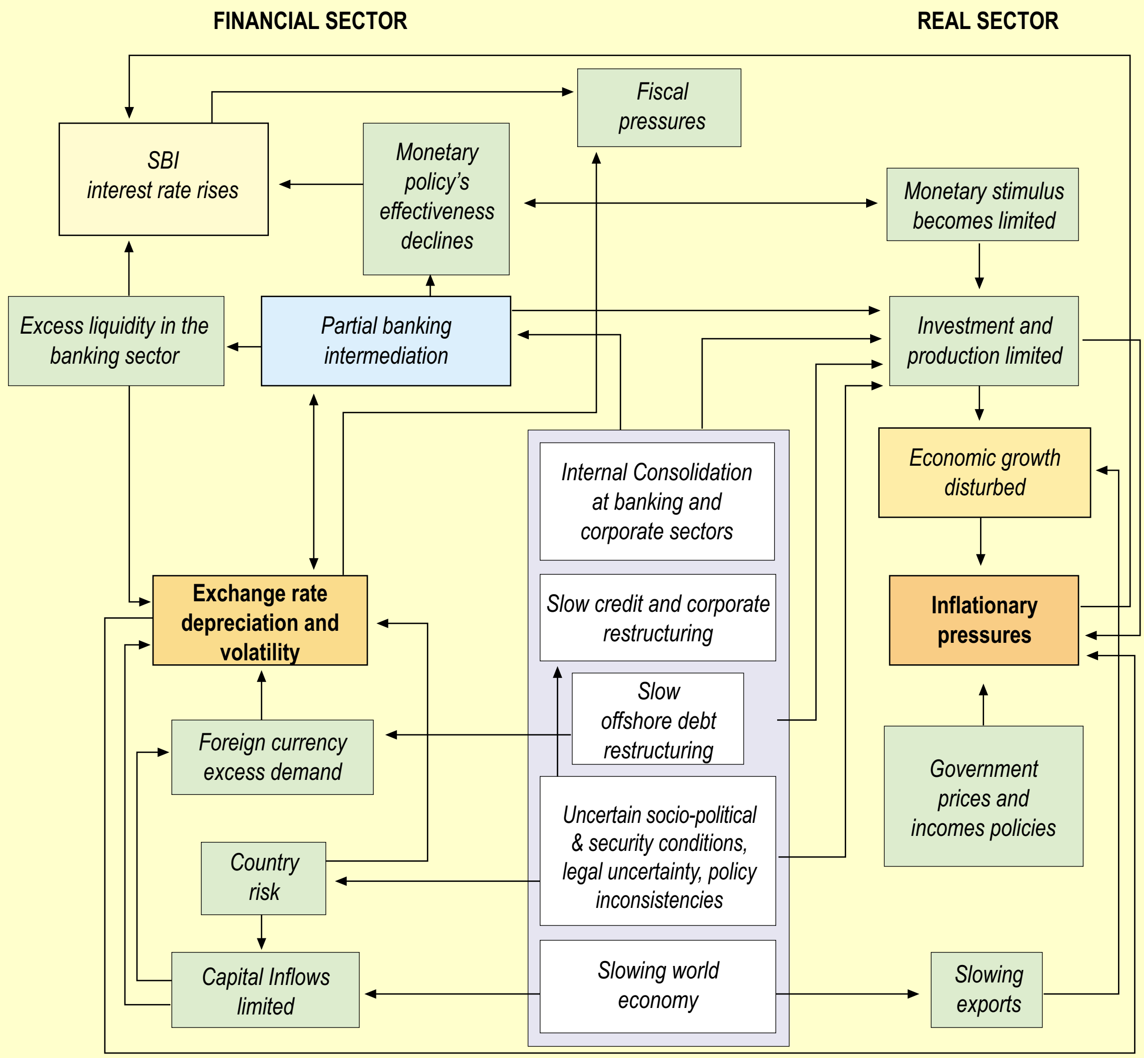

Diagram 1.1
Economic and Monetary Problems in 2001

exchange rate and inflation in addition to reducing the effectiveness of the transmission mechanism of monetary policy.

Against the backdrop, throughout 2001 economic and monetary developments in general deteriorated, as reflected in the lower economic growth, higher inflation rate, and weaker exchange rate. During 2001, the economy grew by only 3.3%, the exchange rate depreciated by 17.7% to an average of Rp10.255 per dollar, and CPI inflation hiked to 12.55%. The impact of government policies on inflation appeared to be higher (3.83%) than earlier estimated of 2.0%-2.5%.

Bank Indonesia sought to achieve the targets that had been set by utilizing the available monetary instruments and improving bank regulations. However, the existing problems earlier mentioned had made the control of base money and the achievement of the inflation target more complicated. In addition, other factors also played a role in giving upward pressure on inflation, namely the impact of government policies on prices and income policy, the pass-through impact of rupiah depreciation, and higher expectation on inflation. As regard base money, its growth was higher than the target due mainly to a surge in the demand for currency, both for transaction and precautionary motives. Under such condition, excessive monetary tightening would have led to a hike in interest rates, which might put the process of bank restructuring and economic recovery at stake.

Looking forward, given that substantive progress are made in addressing a number of domestic structural problems and introducing business risk and uncertainty, Bank Indonesia predicts that economic recovery in 2002 can be sustained. Economic growth is expected to reach 3.5%-4.0% with domestic demand, particularly private consumption, providing the main impetus. Investment and exports would also improved depending on the world economic recovery which is expected to gain momentum in the second half of 2002.

Taking into account macroeconomic prospects, prevailing high risks and uncertainties, as well as persistently high inflationary pressure (due to the impact of administered prices and incomes policies in addition to high inflation expectation), Bank Indonesia sets a realistic target of CPI inflation of 9.0%-10.0% for 2002. However, for the next five years, Bank Indonesia has committed to gradually reduce inflation to a range of 6.0%-7.0%.

To achieve that inflation target, the conduct of monetary policy will be aimed at controlling the growth of base money mainly by mopping up excess liquidity while insuring adequate liquidity consistent with the real need of the economy. Bank Indonesia will exercise prudence in implementing this policy and take measured steps, such that price stability can be maintained in order to support the process of economic recovery that will lead to sustainable growth in the long run. Operationally, monetary control will be conducted by optimizing the available monetary instruments, mainly through open market operation (OMO) and foreign exchange sterilization in order to ease pressures on exchange rate and inflation. In the banking area, Bank Indonesia's policies will be directed at strengthening banking system resilience and accelerating the recovery of bank intermediation. In the area of payment system, the policy will be directed at reducing risks in the interbank payment system that could be stabilized the financial system; supporting the implementation of monetary policy; improving the quality and the capacity of payment system services, and improving the regulation and supervision on the payment system.

The following sections provide a detailed evaluation of the Indonesian economic performance in 2001, as well as the prospects and direction of Bank Indonesia's policies for the year 2002.

INDONESIA'S ECONOMIC PERFORMANCE IN 2001

Macroeconomic Conditions

The year 2001 saw less favorable performance of Indonesia's economy. Reflecting in part the impact of deterioration in the world economy, the slowdown in Indonesia's economy was also attributable to the persistently higher risk and uncertainties; remaining domestic problems associated with debt and corporate restructuring and bank consolidation in addition to the constraint in fiscal stimulus. These developments eroded business confidence which hampered expansion in production and investment. In 2001, GDP grew by only 3.3%, well below 4.9% in 2000 (Table 1.1). While this growth was higher than that in the region, it was not adequate to provide job creation for new entrants of the labor force, which is estimated to have increased by 2.5%. Consequently, unemployment rate in 2001 increased to an estimated 6.7%-7.0%, compared with 6.1% in the previous year.

From the demand side, household consumption provided the driving force with the growth of 6.2% in 2001, well above 3.9% in the preceding year. Much of the increase in consumption was prompted by rising consumer confidence, supported by higher wages and incomes as well as better terms for consumer financing, which originated in both the banking system and financing companies (e.g., credit cards and consumer finance companies).

Exports and investment,[1] which have been expected to provide the main impetus of growth for 2001, appeared to perform unfavorably with the growth of only 4.0% and 1.9%, respectively, a marked drop from 21.9% and 26.5% in 2000. The drop in investment was reflected in the fall of realization of new investments- both foreign and domestic- and in the decline of imports of raw materials and capital goods of 8.5% and 10.2%, respectively from the previous year. The persistently high risk due to insecurity, uncertainty in law enforcement, and increasing labor disputes were among the factors contributing to the collapse in investment. Other factors which adversely affected investment were financing constraint as bank intermediation function had not fully recovered and increasing regulations associated with the implementation of regional autonomy. The deterioration in exports stemmed from the recession in world economy and worsening prices of major Indonesian export commodities. In addition, the depreciation of rupiah raise the costs of production, which

Table 1.1
Selected Macroeconomic Indicators

Item	1999	2000	2001
Gross Domestic Product (at constant 1993 price, % growth)	**0.8**	**4.9***	**3.3****
By Expenditure			
Consumption	4.3	3.9	6.2
Gross fixed capital formation	–18.2	21.9	4.0
Exports of goods and services	–31.8	26.5	1.9
Imports of goods and services	–40.7	21.1	8.1
By Sector			
Agriculture	2.2	1.7	0.6
Manufacturing	3.9	6.1	4.3
Construction	–1.9	5.5	4.0
Trade. hotel and restaurants	–0.1	5.6	5.1
Finance. leasing and service companies	–7.2	4.3	3.0
Other services	1.9	2.2	2.0
Monetary (% growth)			
M2	11.9	15.6	13.0
M1	23.2	30.1	9.6
Quasi Money	9.5	12.1	13.9
Interest Rate (%)			
SBI (1 month)	12.15	14.5	17.62
Interbank Money Market (overnight)	12.1	11.4	15.7
Time Deposit (1 month)	12.2	12.0	16.1
Working capital credit	20.7	17.7	19.2
Investment credit	17.8	16.9	17.9
CPI Inflation (%)	**2.01**	**9.35**	**12.55**
Balance of Payments			
Current Account/GDP(%)	4.1	5.3	3.4*
Debt service ratio (DSR) (%)	56.8	41.1	39.4
Foreign currency reserves in months of non-oil/gas imports	6.7	6.0	6.1
Average Exchange Rate (Rp/$)	**7,850**	**8,438**	**10,255**

Sources : - BPS-Statistics Indonesia
- Bank Indonesia

1 Investment is gross domestic fixed capital formation

weakened the competitiveness of Indonesian exports, especially those with higher import content. On this basis, the contribution of consumption, exports, and investment to GDP growth for the reporting year were 4.8%, 0.9%, and 0.6%, respectively.

On the supply side, almost all sectors expanded in 2001, albeit at a slower pace than in 2000. Several sectors expanded appreciably, including electricity, water, and gas; transportation and communication; trade, hotel and restaurants; and manufacturing. However, manufacturing and trade fell short of the previous expectation as the engine of growth. The main problems hindering the growth in these sectors were inadequate financing and higher production costs following the upward adjustments of administered prices. In addition, the weaker rupiah led producers to facing higher price on to consumers and cutting productions. As a result of continued weak investment, production capacity in the manufacturing sector shrank. Yet, on an aggregate basis, overall production capacity still exceeded aggregate demand.

On the external front, the performance of the balance of payments in 2001 was less encouraging. In line with weaker exports, the current account deteriorated in 2001, as reflected in a surplus that narrowed from $8.0 billion (5.3% of GDP) in 2000 to $5.0 billion surplus (3.4% of GDP) in the reporting year. On capital account, continuing weak private and public capital inflows caused the deficit to widen from $6.8 billion in 2000 to $8.9 billion in 2001; consisting of a deficit on private capital of $8.6 billion and a deficit on public capital of $0.3 billion. With this development, Indonesia's overall balance of payments recorded a deficit of $1.4 billion. Official foreign exchange reserves at the end of 2001 stood at $28.0 billion, equal to 6.1 months of imports and government debt repayments.

On the fiscal side, various constraints faced by the government limited its ability to use fiscal stimulus. The budgetary deficit in 2001 (according to the revised outcome of the state budget for 2001) is estimated at roughly 3.7% of GDP, which is close to the initial budgeted amounts. The realization of revenues and spending were much higher than budgeted, by 4.8% and 4.2%, respectively, above budgeted amounts. On the revenue side, realizations that exceeded the target mainly originated in oil-gas revenues due to the rupiah depreciation and to oil revenues of 2000 that were paid in 2001. Other tax revenues also reached their targets as a result of several intensification and extensification tax policies undertaken by the government. From the expenditure side, higher than budgeted spending was caused by higher current expenditures for subsidies and interest payments on bank recapitalization bonds. Larger subsidies were due to higher domestic consumption of fuel and the rupiah depreciation. There was also a correction to subsidies payments in 2000 in the amount of Rp5.6 trillion; higher payments of interest on bank recapitalization bonds was due to rises in SBI rates. For its part, the realization of capital expenditure reached only 91.4% of the budgeted amount. This stemmed from several factors, including delays in several program loans and the short time available to implement projects after the state budget was revised.

On the financing side, most of the budget deficit was covered by domestic financing, which primarily originated from sales of assets of the

Indonesian Bank Restructuring Agency (IBRA). The other sources of financing were privatization and limited amounts of foreign financing. In relation to aggregate demand, the share of the public sector in aggregate demand is estimated to have increased from the previous year, from 10.8% to 11.9% of GDP. The main factor driving this increase is the rising allocation of revenue sharing (dana bagi hasil or DBH) starting in 2001.

Exchange Rate and Inflation

As noted in the previous sections, the deterioration of Indonesia's economic condition in 2001 was due to remaining unresolved structural economic problems and high domestic risk and uncertainty. In the real sector, this condition inhibited production and investment activity. In the financial sector, these problems led banks to extending a smaller amount of credits to support productive activity. The weak link between the real and financial sectors did not only result in financing constraint for investment and production, but also a build up of excess liquidity in the banking system, which in turn exerted more pressure on the exchange rate and inflation.

In 2001, the rupiah exchange rate came under persistent pressure, with increasing volatility, despite a short-lived strengthening in the middle of the year. On average, rupiah depreciated by 17.7% relative to 2000, namely from Rp8,438 to Rp10,255 per dollar. This rate was considerably weaker than the assumption used in setting the inflation target of Rp8,000 per dollar, which was a depreciation of 22%. Between early 2001 and April the rupiah weakened to a low of Rp12,090 before stabilizing around Rp11,200 through July. Following the Special Plenary Session of the People' s Consultative Assembly, the rupiah strengthened markedly, to a peak of Rp8,485 per dollar before weakening again to around Rp10,400 per dollar through the end of 2001.

In general, the weaker exchange rate stemmed from problems in the foreign exchange market that were macro-fundamental and micro-structural in nature, which led to imbalances between foreign exchange supply and demand. This gap was aggravated by heightened risk premiums associated with rising country risk. Concerning macro-fundamental, rising risk and uncertainty during 2001 reduced foreign investors' confidence in Indonesia, which hampered capital inflows. On another side, weaker world economic performance has hammered Indonesia's exports. These two factors reduced the supply of foreign exchange in the face of foreign currency demand by the corporate sector to service foreign debt and to finance imports.

From the micro-structural side, the existing market segmentation and shallow domestic foreign exchange market placements in addition to the limited variety of money market instruments induced certain banks with excess foreign exchange liquidity to place their funds abroad. These developments resulted in a contraction of liquidity in the domestic interbank foreign exchange market and supply of foreign exchange in the economy. The weakness in the micro-structure of foreign exchange market was also due to the less developed hedging market, particularly for the medium and long-term maturities, which prompted corporations to meet their future needs for foreign exchange through early purchase in the spot market.

The gap between the demand for and supply of foreign exchange brought about increased volatility of the exchange rate. This situation was further aggravated by the negative sentiment among market players concerning political uncertainty, particularly in the period leading to the change of national leadership and uncertainty over the result of remaining structural problems, such as corporate and debt restructuring, divestment, and privatization, as well as normalization relationship with the IMF. These factors contributed to heightened country risk, which raised the risk premium and exerted pressure in the exchange rate.

The weaker exchange rate also led to stronger inflationary pressure in 2001. The depreciation brought about a pass-through impact on inflation, both directly through higher prices of imported finished goods, intermediate goods, and raw material goods, and indirectly through expenditure switching. The high import content of domestically produced goods resulted in the strong impact of rupiah depreciation on the cost of production. Evidence of the significant influence of the exchange rate depreciation on inflation was reflected in the co-movement of inflation and the exchange rate.

The surge in inflation during 2001 was also accounted for by the government policies on prices and income. Various government policies (such as increases in fuel prices, transportation fares, basic tariffs on electricity, excise on cigarettes, regional minimum wages and civil servants salaries) had a direct impact of 3.83% on the CPI. This impact was higher than the 2.0%-2.5% estimated at the beginning of the year due in part to the much higher price adjustment than initially estimated at the beginning of the year and due to the postponement in the adjustment of administered prices. As fuel and electricity were the inputs of almost all products, their increase in price resulted in higher production cost (cost-push inflation).

In addition to the weakening exchange rate and the impact of government policies, the acceleration of inflation rate in the reporting year was also due to high inflation expectation. In general, inflation expectation was adaptive in nature. Hence, public expectation on inflation was mainly determined by actual inflation in the preceding years. The high expectation on inflation last year was also attributable to the weakening exchange rate and the implementation of government policies on prices and income. On the contrary, inflationary pressures from aggregate demand remained subdued as economic growth slackened and production capacity in the manufacturing sector was still underutilized. However, output in the agricultural sector declined due to a contraction in the production of food.

On the basis of these developments, during the reporting year, the inflation rate accelerated to 12.55%, well above 9.35% in 2000. Excluding the impact of government policies, inflation stood at 8.72% in 2001, which was above Bank Indonesia's target of 4.0%-6.0%. As previously mentioned, the rise in inflation outside the impact of administered price was in part accounted for by the significant exchange rate depreciation in addition to high inflation expectation.

Monetary Policy and Developments

In coping with the persistent pressure on inflation and exchange rate, Bank Indonesia had made its best endeavor to ease the pressure as reflected in the policies introduced in the areas of monetary and exchange rate. In the monetary area, Bank Indonesia adopted a tight-bias monetary policy so as to control the growth of base money in line with its predetermined target. This was meant to absorb excess bank liquidity, which could potentially weaken the exchange rate and give rise to inflation.

With a view to keeping the growth of base money target in check, monetary policy was implemented mainly through the open market operation (OMO), especially through the auction of one- and three-month SBI. To absorb excess liquidity, the OMO was complemented with rupiah intervention so as to maintain the growth of base money within its target and maintain stability of the interbank money market interest rate. However, as bank intermediation was not fully restored, the absorption of banks' excess liquidity through these monetary instruments often drove interest rates upward. Therefore, in order to limit excessive rise in interest rates, Bank Indonesia also recoursed to foreign exchange sterilization, which increased the supply of foreign exchange in the market. This was mainly intended to mop up the expansion of base money originating from government's rupiah spending financed by foreign exchange revenues.

The increase in the supply of foreign exchange through foreign exchange sterilization in addition to being used to absorb base money was also aimed at easing the pressure and volatility of the exchange rate. However, given the excess demand in the foreign exchange market, the sterilization would only be effective if supported by other policies that limit the ability of market players to conduct speculative activities. Therefore, during the reporting year, to help stabilize the exchange rate, Bank Indonesia introduced a policy designed to limit rupiah transactions by non-residents and launched an on-site supervision on banks that were major players in the foreign exchange market. This policy was based on the finding that non-residents tended to use rupiah as a means to speculations, which exerted considerable pressure on the exchange rate. This policy proved to be very effective in easing pressure stemming from speculation by non-residents[2] as reflected in a drastic drop of their rupiah vostro account with domestic banks.

As the year unfolded, the control base money was not fully effective owing to various factors beyond Bank Indonesia's control, particularly the public behavior in holding currency and ineffectiveness of the transmission mechanism of monetary policy as bank intermediation function was not fully restored. The growth of base money averaged 18.2% in 2001, or up by 15.4% by the end of 2001, well above its target of 11.0%-12.0% set at the beginning of the year. By component, much of this increase was primarily accounted for by the strong growth of demand for currency by the public, averaging 20.1% in 2001.

The surge in the demand for currency by the public was prompted among others by a significant shift in Indonesia's economic structure as reflected in the larger role of small-and medium- scale businesses and the informal sector which used more self financing than bank credit. In addition, the heightening socio-political uncertainty in 2001 also induced demand for currency for precautionary motives.

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2 The Issuance of Bank Indonesia regulation No.3/3/2001 dated 12 January 2001 regarding the restrictions on rupiah transactions and foreign currecncy credit offered by banks.

The strong demand for currency amid the prevailing problems in the implementation of monetary policy had complicated the absorption of base money. Although various instruments have been applied to absorb liquidity (namely, OMOs foreign exchange intervention and rupiah intervention), base money target was frequently missed. Under such a condition, absorbing base money by raising SBI rate might not be very effective. In view of this condition, especially after the end of the third quarter of 2001, Bank Indonesia sought to absorb excess liquidity in the banking without pushing excessive increase in interest rates.

Throughout 2001 the one-month SBI rate rose gradually by 309 basis points (bp) to 17.62%; the three-month SBI rate rose by 332 bp to 17.63% by end-December. The rise in SBI rates during 2001 did not significantly affect deposit rates, mainly as a consequence of banks' heavy dependence on SBI placements and their taking the wider spread between SBI and deposit rates, given the limited bank intermediation. For their part, one-month deposit rates rose by 411 bp to 16.07%, mainly due to change in the maximum guaranteed interest rate, which was changed twice during the reporting year. The direction of the movement of deposit rates throughout the reporting year were closer to changes in the guaranteed interest rate. In line with the increase in nominal deposit rates, the real deposit rate rose by 91 bp, to 3.52%. This is still well below the real rate during the pre-crisis period, especially in light of high-risk premiums at present.

Although the real deposit rate was far lower than its pre-crisis level, this small increase in the real deposit rate was sufficient to shift public portfolios from assets used for transaction purposes to assets used for savings purposes. This is reflected in the larger increase in time deposits as compared with more liquid assets, such as savings and demand deposits. This stands in sharp contrast to developments during 2000, when the shift was in the opposite direction, to more liquid assets. In line with the rise in time deposits, at the end of the year broad money (M2) increased by 13.0% (y-o-y), higher than the M1 growth of 9.6%. On average, the growth of M2 was lower than the growth of M1.

Banking Policy and Developments

In a continuation of policies adopted by the Government and Bank Indonesia in the preceding year, the bank restructuring strategy in 2001 covered two main parts, namely: (i) the bank rehabilitation program, which covered government guarantees for commercial banks and Bank Perkreditan Rakyat/BPR (rural credit banks), recapitalization of commercial banks and bank credit restructuring programs; and (ii) improvement of the banking system resilience program, which covered the development of infrastructure, the improvement of corporate governance, as well as improvement in regulations and banking supervision.

Under the bank rehabilitation program in 2001, Bank Indonesia put emphasis on the achievement of the minimum 8% CAR (capital adequacy ratio) target that had to be fulfilled by end-2001[3] and the maximum 5% indicative target of non-performing loans (NPLs). In line with these efforts, Bank Indonesia is also improving the pattern of banking supervision as has been laid out in the master plan regarding the effectiveness of bank supervision. This includes the implementation of risk-based supervision and a forward-looking approach as an enhancement of compliance-based supervision (compliance audit). The improvement of this supervision approach refers to the 25 Basel Core Principles for Effective Banking Supervision, which have already been applied internationally. Meanwhile, enhancement of the banking resilience program is aimed at creating a banking system that will be more resilient to shocks. As integral parts of the national banking system, in 2001 development of *sharia* banks and BPRs was also undertaken.

In order to promote small- and medium-scale businesses, Bank Indonesia has undertaken various efforts to utilize small-scale business entities through a technical support program (PUKM). This program consists of: (i) training programs extended to BPRs and commercial banks in financing small business entities; (ii) conducting research on potential small-scale (micro) businesses that can be financed by banks; (iii) providing comprehensive information regarding small-scale business that can be accessed through the Internet, covering information on potential regions, types of financing and small export industries. This information is expected to be useful for small businessmen as well as for banks in developing their micro financing programs.

As a result of implementing the above policies, the banking sector performance over the year 2001 has improved, particularly fulfillment of the 8% CAR and 5% NPLs. This was in line with 2001 strategic targets of the bank restructuring program, which emphasized achievement of the CAR and NPLs targets. In this regard, bank capital structure has generally improved as reflected in the increase in the number of banks that have met the 8% CAR requirement. By the end of 2001,[3] 138 out of 145 banks met the minimum 8% CAR requirement. NPLs also improved significantly, falling to12.1% from 18.8% in the year 2000, mainly due to the write-offs of non-performing loans, restructuring and settlement of credits, transfer of credits to IBRA, as well as extension of new credits. Improved performance of the banking sector was also reflected in an increase in banking profitability. Banks' net interest margin (NIM) rose from an average Rp1.9 trillion in 2000 to Rp3.2 trillion in 2001. This increase mainly stemmed from a positive spread brought on by the increase in SBI rates and from large earnings on government bonds, which accounted for some 45.3% of banks' total interest earnings. Banks' interest earnings from credits represented only 32.2%. This high dependence on interest earnings from bonds indicates that bank restructuring has not been able to fully restore bank intermediation.

Although the banking sector performance indicators showed meaningful progress during 2001, this sector still faces challenges, particularly the intermediation function, which has not fully recovered. This was reflected in limited absorption of new credits by the real sector, which by end-2001 reached only Rp56.8 trillion (44.6%) out of the committed credit supply of Rp127.3 trillion. This low absorption capacity by the real sector is in line with the decline of business confidence in conducting investment and production activities as a consequence of high risk and uncertainty throughout the reporting year. Weakness in the intermediation function of banks was inherent in the ongoing bank consolidation process in fulfilling prudential regulations.

3 Position at November 2001.

Unfavorable development of credit and corporate restructuring also contributed to slow recovery of bank intermediation. Up to December 2001, restructured credits (fully paid) by IBRA reached only Rp11.6 trillion or 3.7% out of the total non-performing credits of Rp310.7 trillion. Other categories, namely proposed restructuring and those at the MoU stage, have reached Rp19.7 trillion and Rp60.9 trillion, respectively. Credit restructuring facilitated by the Bank Indonesia Credit Restructuring Task Force reached a cumulative amount of Rp91.8 trillion. Restructuring of private foreign debts reported to Bank Indonesia is accounted for by only 68 corporations with a total value of $4.1 billion, or just 13.7% of the outstanding non-performing corporate foreign debts of $30 billion. The slow restructuring of private foreign debts is due to disagreements over terms and conditions as between debtors and creditors, a decline in the collateral value of credits, high country risk which induces higher interest costs and prohibits foreign investors from taking over the corporate foreign debts, volatility of the exchange rate, and uncertainty in law enforcement.

Payment System Policy and Developments

During 2001, Bank Indonesia continued to enhance the national payment system to ensure that it is efficient, fast, secured, and reliable in order to support the effectiveness of monetary policy and the creation of a healthy banking system. In a broader sense, payment system policies consist of those concerning money circulation and those concerning the enhancement of Bank Indonesia's services in the area of payment flows.

In the area of money circulation, Bank Indonesia made efforts to meet the public's needs for banknotes and coins for payment purposes and to ensure that money in circulation was in good condition. In 2001, Bank Indonesia increased the supply of money to meet increased public demand for currency in line with the development of several national economic indicators and in response to the celebrations of Ramadhan, Idul Fitri, Christmas, and New Year 2002, which fell close to each other.

The outstanding amount of money in circulation (Uang Kartal Yang Diedarkan/UYD) during year 2001 tended to rise. Its position at the end of December 2001 reached Rp91.3 trillion, which is a rise of 1.8% from the position at the end of December 2000 of only Rp89.7 trillion. This increase stemmed from huge withdrawals by the public with regard to the celebration of religious holidays and New Year.

Viewed by type of money, the ratio between bank notes and coins during year 2001 was little changed, with respective shares of 98% and 2%. Viewed by denomination, the Rp100,000 and Rp50,000 denominations held the largest shares (41.4% and 28.9%, respectively) of total circulated money. In addition to providing currency in sufficient amount, Bank Indonesia also maintained the quality of currency held by the public by adopting a clean money policy. This entailed withdrawing and destroying banknotes that were no longer fit for circulation (known as Pemberian Tanda Tidak Berharga/PTTB) and replacing the destroyed banknotes with new ones.

Despite a decline in the number of counterfeit notes discovered in 2001, Bank Indonesia continued to promote cooperation with related institutions, among others with Coordinating Board for Eradication of Counterfeit Money (Botasupal). Bank Indonesia also undertook specialized activities, such as circulating posters and stickers concerning easy ways to identify rupiah banknotes; making preparations for public service advertisements on television; and holding socialization activities concerning the features of authentic rupiah banknotes. In addition to those preventive efforts, Bank Indonesia also adopted repressive efforts by undertaking coordination and cooperation with related institutions in arresting and bringing to court parties involved in the counterfeiting of rupiah.

In the area of non-cash payment flows, in order to enhance stability of the financial system and to increase the effectiveness of monetary policy, Bank Indonesia has taken steps regarding the payment system's security, procedures, and products. These included: (i) development of Bank Indonesia's Real Time Gross Settlement (BI-RTGS) system as the mechanism for interbank settlement of large-value and/or urgent transactions. In 2001, this was implemented in 12 Bank Indonesia Regional Offices (Kantor Bank Indonesia/KBI). (ii) Development of a Long Distance Clearing Information System (SIKJJ) in order to improve the efficiency and effectiveness of electronic and automatic clearing operations. (iii) Re-arrangement of current (giro) account relations between Bank Indonesia and external parties in order to expand the utilization of current accounts at Bank Indonesia by external parties to maintain stability of the rupiah.[4] And (iv) arrangements for the operation of payment system services using non-cash payment instruments and supporting services, for the purpose of confirming inter-institutional authority limits in the regulation of payment system services.

4 Issuance of Bank Indonesia regulation number 3/11/PBI/2001 which replaces Bank Indonesia regulation number 2/24/PBI/2000 concerning Current (Giro) Account Relations Between Bank Indonesia and External Parties.

ECONOMIC PROSPECTS AND POLICY DIRECTIONS IN 2002

Challenges Ahead

The evaluation on economic performance in 2001 indicates that various fundamental problems and risks remained unresolved. As earlier expected; in fact, in some respect the situation deteriorated. These conditions have hindered Indonesia's economic recovery and complicated the control of base money. Resolution of those problems will be the key of improving the prospect for economic recovery in the years ahead. Those various risks and uncertainties are as follows:

- **First**, the slow progress in corporate debt restructuring. This has hindered the pace of economic recovery and the extension of bank credits, because the corporation undergoing the restructuring program constitute the major segment in the economy.
- **Second,** bank intermediation has not fully restored. On one hand, this has limited financing for production and investment while on the other hand there is excess liquidity in the banking sector which has the potential to exert pressure on the exchange rate and inflation, and reduce the effectiveness of monetary policy.
- **Third,** the heavy burden of the state budget, mainly due to a large subsidies and huge government debts. Asset recovery by the IBRA and State Owned Enterprises (SOEs) are estimated to be inadequate to cover the burden

of government debts. In such condition, there is little room of fiscal stimulus to accelerate the economic recovery.

- **Forth,** legal uncertainty persists and problems remain in implementing economic policies in various other areas. These conditions hamper economic restructuring and delay improvements in Indonesia's country risks and impede economic recovery.
- **Fifth,** the emergence of various problems associated with the implementation of regional autonomy which are not conducive to investment in the region. In addition, inefficient utilization of General Allocation Funds (Dana Alokasi Umum) could further limit fiscal stimulus.
- **Sixth,** on the external front, the world economy is still in recession as 2002 begins and an improvement is anticipated only in the second semester. This will reduce external demand for Indonesian products. In addition, the implementation of AFTA (starting early 2002) will provide new export opportunities but the opening of domestic market to foreign competitors could also threaten domestic producers.

Macroeconomic Prospect

The prospects of Indonesia's economy in 2002 are affected by developments in the global economy, mostly notably the major industrialized countries such as the United States, Japan and the European Union which are currently experiencing a slowdown. However, the aggressive use of fiscal stimulus and expansionary monetary policy in those countries is predicted to accelerate economic recovery during the second semester of 2002. In view of the weakening world economy, Indonesia's economic and monetary developments in 2002 mainly rest on the strength of domestic demand. Given that a number of domestic structural problems are resolved and certain risks and uncertainties successfully addressed, Bank Indonesia estimates that the economic recovery will be sustained in 2002. These, combined with expansion in exports and investment and the progress in bank restructuring program are expected to support economic growth of 3.5%-4.0% in 2002.

On the demand side, economic growth in 2002 would be dominated by consumption, which is driven by rising salaries and income and increased financing for consumption, originating in banks and financing companies, especially credit card and consumer finance companies. However, it should be noted that consumption is expected to decelerate from 2001. Meanwhile, investment and exports are forecast to record slightly higher growth than in 2001. Investment would be constrained by remaining fundamental problems in the real sector, persistent risk and uncertainty and limited financing as bank intermediation has not fully restored. Exports though higher will remain subdued, mainly due to the weak world economic growth. Unlike exports, imports are forecast to increase in line with higher consumption and investment.

On the supply side, almost all sectors would contribute to moderate growth in 2002. In line with the dominant role of consumption as the main engine of growth, the biggest share of growth would come from manufacturing and trade sectors. Some manufacturing sub-sectors would increase sharply, for example, food and beverages and motor vehicles.

Industries that produce the main export products such as textiles, footwear and wood industries would decline. Meanwhile, the trade sector, particularly retail trade, would experience a relatively large increase due to strong private consumption, the main engine for the domestic economy. Growth in the mining sector would be modest, mainly due to uncertainty in law enforcement and security issues. Other sectors, such as construction, would be revived in line with the Jakarta Outer Ring Road and housing projects that reflect greater housing credits. The only sector that remains gloomy is agriculture due to the prospects for a return of El Niño and unsettled issues concerning the production and distribution of fertilizers. Export-oriented plantation commodities would decline in line with lower world demand.

In 2002, Indonesia's balance of payments would improve relative to the previous year. This is reflected, among others, in the rising official foreign exchange reserves due to stronger capital flows. Meanwhile, the current account would remain in surplus (about $3.1 billion), but somewhat narrower than in 2001; imports would outpace exports. Meanwhile, the deficit on capital account would continue to narrow, owing to a smaller deficit on private capital and a larger surplus on government capital. This would be supported by larger government capital inflows, originating in drawdowns of loans (which were delayed in 2001) from donor countries and from the rescheduling of bilateral debts associated with the Paris Club.

Exchange Rate and Inflation Prospects

The prospects for the rupiah exchange rate in 2002 will be influenced by fundamental conditions in the foreign currency market (such as the continuing limited supply and the ongoing high demand for foreign currency) as well as by market sentiment. The rupiah has the potential to strengthen in 2002, whereas depreciation pressures will tend to decline relative to the past year, considering that political uncertainty is predicted to improve in 2002. A significant strengthening of the rupiah is expected to take place beginning in the second half of 2002, in line with improved political, financial and economic risks. This forecast would be more optimistic if in the near future there were to be improvements in the implementation of government programs; market perceptions would improve, including by significant assets sales by IBRA and privatization of SOEs. However, if these risks increase, the rupiah would weaken slightly. Against this background, the rupiah in 2002 is forecast in the range of Rp9,500 to Rp10,500 per dollar.

Inflation in 2002 will be influenced primarily by government pricing policy and by inflationary expectations. As was the case in preceding years, the impact of government policies is expected to be quite high. Government plans to increase the price of fuels, basic electricity tariffs, and the cigarette excise tax are predicted to impact appreciably on inflation in 2002. Inflationary expectations would be high, being influenced by the high inflation in 2001, and by planned government prices and incomes policies.

In addition, inflationary pressures on the demand and supply sides are predicted to rise as the result of expanding private consumption that will not be fully satisfied by the supply side. Inflationary pressures would be even greater if agricultural production and food supplies are disrupted by El Niño in 2002.

Inflation Target for 2002 and the Medium-Term Targets

Taking into account the various macroeconomic developments and prospects for inflationary pressures, Bank Indonesia sets the target for year 2002 CPI inflation rate in the range of 9.0%–10.0%. However, within 5 years term, Bank Indonesia has committed to gradually reduce inflation to around 6.0%–7.0%.

In this regard, it should be noted that unlike preceding years, Bank Indonesia is changing the type of inflation used as inflation target, from core inflation (i.e., inflation excluding the impact of government prices and incomes policies) to CPI inflation. The considerations for this change are : (i) CPI inflation constitutes the rate of price change that is directly felt by the public, and thereby, the use of this type of inflation target can be more readily accepted by the public; (ii) the use of CPI inflation is more transparent for the public relative to core inflation, which needs deeper understanding as regards its method of calculation; (iii) by using a more acceptable and transparent inflation target, public expectations as regard inflation will be more easily influenced by Bank Indonesia's inflation target.

In addition to the change in the type of inflation used as target, starting this year Bank Indonesia will announce a medium-term inflation target. The medium-term inflation target is expected to be used by the public and business players as a reference for their medium-term planning. In this way, medium-term inflationary expectations can be directed to a lower inflation rate without sacrificing the ongoing recovery *(Box : Setting Bank Indonesia's Inflation Target).*

Policy Directions

Taking into account economic prospects, the inflation target, and the various challenges that will be faced in 2002, Bank Indonesia will endeavor to consistently adopt policies in the areas of monetary, banking, and the payment system.

In the monetary area, policy will be aimed at controlling base money by absorbing excess liquidity according to the real needs of the economy. This policy will also be conducted by maintaining a real positive interest rate of around 4.0%–5.0%. Operationally, monetary control will be conducted by optimizing the available monetary instruments, mainly through open market operation (OMO) using the SBI auction. This effort will be supported by sterilized foreign exchange intervention. These steps will be cautiously and measurably conducted such that price stability can be maintained in support of the economic recovery, and in the long run sustainable economic growth can be achieved.

In the banking area, the main policy priority will be the strengthening of banking system resilience. To achieve this, Bank Indonesia will continue implementation of the 25 Basel Core Principles for Effective Banking Supervision. Details are set out in the Master Plan for the Enhancement of Effective Bank Supervision. Efforts will be continued to maintain an 8% minimum CAR, particularly for banks whose capital structures are still susceptible to interest rate increases, weakening exchange rates, and declining credit quality. Big banks whose risks are high and that are involved in international operations will be encouraged to raise their CAR above 8%. In addition, in order to promote stability of the financial system, Bank Indonesia is reviewing a national bank landscaping which is integrated with the development of other financial institutions.

Meanwhile, in order to revive bank intermediation, Bank Indonesia will push banks to extend more credit to sectors that are considered to be ready and have relatively low risk (such as export credits and credits for small- and medium-scale enterprises), while continuing to observe prudential banking principles. Bank Indonesia will also improve several regulations to speed up the bank intermediation function. Furthermore, the promotion of sound banking will be supported by continued efforts to reduce the national NPLs figure by forcing banks to reach the 5% NPLs target by end-2002. In the meantime, improvements in banking infrastructure would be done by encouraging the development of bank *syariah* and BPRs. As a further step to improve banking infrastructure, Bank Indonesia and the Government will prepare a Deposit Insurance Institution and a supervisory body for the financial services sector.

To support stability of the financial system and the effectiveness of monetary policy, policies in the payment system area will be directed towards the acceleration of development and implementation of a national payment system that is efficient, accurate, secured, and reliable through the enhancement of payment system's service quality. In money circulation area, policies will put emphasis on the use of security features on new issues of currencies that can be visually detected and can be detected by touch. In addition, the money distribution channel will be rearranged to give more assurance as to the availability of money at all Bank Indonesia regional offices and the enhancement of cash services to the public.

Meanwhile, on the non-cash payment side, policies are directed towards development of the payment system supervision mechanism. This is meant to promote the realization of a payment system that is secured and efficient and to safeguard the stability of the financial system from the possibility of systemic failures that can occur when a payment system participant experiences credit and liquidity risks. In addition, Bank Indonesia will continue efforts to regulate the operation of payment system services using non-cash payment instruments and supporting services. There will be related efforts to cope with failures on the part of clearing participants in concluding their settlement obligations.

Conclusion

In closing, the policies adopted by Bank Indonesia in 2002, will be inseparable from the overall macroeconomic policy framework. In this context, Bank Indonesia's policies support the creation of a climate conducive to overall economic recovery. On another side, the success of Bank Indonesia policies will depend very much upon policies in other areas as well as developments concerning various risks and uncertainties. As such, policy coordination becomes a very important factor in supporting the success of the overall economic recovery. Such policy coordination would produce a credible economic package that will revive confidence of all players in the economic recovery.

On the internal side, Bank Indonesia will continuously adopt various steps to improve its internal management through the launch of Bank Indonesia Transformation Program. This program would be completed in 2002, covering substantial changes on

Bank Indonesia's mission and vision in this changing era, which prompted Bank Indonesia to be able to anticipate and to adjust itself to changes on national and global scales. These changes force Bank Indonesia to be more systematic and integrated in conducting this transformation process. All this is done to promote transparency, accountability, integrity, and competency. In its implementation, the transformation program also renews Bank Indonesia's organizational apparatus, human resource management, information technology system, and relations with stakeholders *(Box : The Bank Indonesia Transformation Program).*

box

Setting Bank Indonesia's Inflation Target

Article 7 of Act 23 of 1999 regarding Bank Indonesia states that Bank Indonesia's main task is to achieve and maintain stability in the value of the rupiah. Further, Article 10 states that in carrying out its tasks, Bank Indonesia is obliged to announce an inflation target and monetary targets in relation to the achievement of that inflation target.

One of Bank Indonesia's efforts in carrying out its main task is to determine an appropriate inflation target by taking into consideration macro-economic conditions. In light of present and future economic conditions, setting the inflation target is intended to support efforts to achieve that target by influencing public expectations through the implementation of a monetary policy that supports economic recovery. For this, various aspects of setting the inflation target need to be reviewed, namely: setting of the type of inflation target, the time period for achieving the inflation target; and the level of inflation target that is going to be achieved.

TYPE OF INFLATION TARGET

In general, inflation can be defined as "…a situation in which there is a persistent upward move-ment in the general price level…"[1]. This definition points to two important matters: i) continuous price rises (a persistent upward movement); and ii) price rises occurring in all categories of goods and services (a general price level movement). As a general indicator of price changes, inflation based on the consumer price index (CPI) is widely used in Indonesia and in a number of other countries. Its popularity stems from the high frequency of its release and being the closest indicator to mirror the changes in the cost of living.

However, sometimes movements in the CPI do not reflect the development of inflation as defined above. Changes in the CPI may stem from high variability in relative prices among the many goods and services included in the CPI, as well as from strong non-fundamental influences such as seasonal factors, and from the impact of government policies on prices and incomes in Indonesia. These considerations may have implications for the accuracy of conducting monetary policy to control inflation.

To investigate this situation, Bank Indonesia has undertaken various studies[2] to obtain indicators that better reflect fundamental changes in prices.[3] Such indicators would be used by Bank Indonesia not only as a guide in setting monetary policy but also as an alternative inflation target. This research has produced several measures of core inflation, where each method excludes shocks from CPI inflation in a different manner.

One approach for calculating core inflation is the 'trimmed mean approach'. Statistically, this approach

1 A.J. Hagger (1977), Inflation: Theory and Policy, The Macmillan Press Ltd.

2 W. Santoso, R. Anglingkusumo, 'Underlying Inflation As A Price Indicator Relevant For Moneterary Policies: A Review for Indonesia', BEMP Num. 1 Vol.1, July 1998 and A.R. Hutabarat, F. Majardi, R. Anglingkusumo, E.D.Tjahjono, E. Haryono, B. Pramono, H. Alamsyah, 'Calculation of Core Inflation in Indonesia', BEMP Vol.2 Num. 4, March 2000.

3 Changes of prices caused by aggregate economic conditions.

is the most robust in the sense that it truly reflects the persistent change in price. However, this approach is relatively difficult to explain to the public because of the technical factors involved in its calculation. The second approach, known as the 'exclusion method', excludes certain commodities from the CPI basket permanently based on the volatility of their price movements. In addition, some commodities whose prices are administered by the government also being excluded. Removing those commodities permanently from the CPI basket would generate a new basket of goods and services that better reflects the development of fundamental prices, yet is easy to understand. The third approach, the 'specific adjustment method', eliminates special influences on aggregate prices through adjustments at specific times when shocks occur. This method only excludes the impact of government prices and incomes policy from inflation at certain times (also known as 'net inflation'). The resulting inflation figures from the latter method have been used by Bank Indonesia in order to establish inflation targets for the last 2 years.

Various in depth reviews were countinously conducted to determine the most appropriate type of inflation target. Among the various criteria that need to be considered in determining the appropriate measure of inflation namely predictability, controllability, and acceptability, for the year 2002 Bank Indonesia opts to place more importance on the acceptability criterion (that is, choosing the type of inflation that is more readily acceptable to the public). This would hopefully encourage the public to be more willing to use the inflation target as an anchor in their economic activities. As a result, it would be easier for Bank Indonesia to influence the public's inflationary expectations.

The inflation measure that best fulfills the acceptability criterion is CPI inflation, because this measure is traditionally used as inflationary indicator in Indonesia. By contrast, the measure of inflation used by Bank Indonesia in 2000 and 2001 (inflation excluding the impact of government policies) has lower acceptability level and the technical difficulties make it hard to replicate and verify. Accordingly, Bank Indonesia will use CPI inflation for its target in 2002, and bear the consequences of low predictability and controllability that arise from the many shocks that it reflects. Meanwhile, other core inflation indicators with higher levels of predictability and controllability can be used as guidance for Bank Indonesia in formulating its monetary policies.

The Level of Inflation Target and the Time Horizon for its Achievement

Determination of the optimal inflation level and the time period for achieving it requires a comprehensive review. In this regard, various matters have to be considered including the characteristics of inflation, the effectiveness and variability of monetary policy, the impact on economic recovery process, and an estimate of the sources of inflationary pressures that are outside the influence of monetary policies.

Review of CPI inflation's characteristics shows that inflationary movements in Indonesia are greatly influenced by price fluctuations of certain goods in the CPI basket (that is, by relative price changes). With prices exhibiting high kurtosis, that is an extreme price movement of some commodities, and chronic right skewness, that is related to assymetric distribution, inflation in Indonesia may be more reflective of disruptions in the distribution of goods and services and seasonal factors. This characteristic implies that it is difficult to reduce inflation in Indonesia to a low rate.

Review on the effectiveness of monetary policy in influencing inflation shows quite a long lag before the effect takes place. This review considers the trade off between inflation and economic growth in the effort to control inflation.[4] The long lagged effect of monetary policy gives limited room for the policy to undertake disinflation process in a short period.

Achieving significant disinflation over the short-term (say, 1 year) may require exceptionally tight monetary policy, which could endanger the economic recovery. However, by undertaking disinflation over the medium term (say, 5 years), inflation could be reduced gradually to quite a low target rate without the need for extremely tight policies. By setting the inflation target this way, monetary policy has sufficient flexibility to encourage the economic recovery, while gradually reducing the public's inflationary expectations in line with the medium-term inflation target.

Other research, based on various economic models developed by Bank Indonesia,[5] demonstrates that with cautious implementation of monetary policy, Bank Indonesia can undertake disinflation towards quite a low level within the medium-term without endangering economic recovery. This disinflation process is based on several main optimistic assumptions, namely:

- Government policies in raising administered prices will have eased over the medium-term, particularly due to the elimination of fuel subsidies and the end of electricity tariffs increases so that these prices will be in line with the international levels.
- A more stable exchange rate occurs, resulting from: reduced foreign currency demand pressures; improved financial market structure; recovering bank intermediation; and reduced risks from non-economic factors. These are expected to dilute the pass-through effect of exchange rates to inflation.
- Bank intermediation has returned to normal, resulting in an improved transmission and effectiveness of monetary policy.
- Problems in the real sector are already solved and investment realizations are improved to the point where increases in aggregate supply match aggregate demand growth, thereby taking demand pressure off inflation.
- Bank Indonesia's credibility, nurtured through consistent implementation of monetary policy and realistic inflation targets, holds down inflationary expectations.

Based on the above considerations and taking into account macroeconomic conditions and the factors influencing inflation rate, the optimum CPI inflation target to be achieved within the short-term (year 2002) is set in the range of 9%–10%. The CPI inflation target for the medium-term, which Bank Indonesia will make an effort to achieve without hampering the economic recovery, is set at 6%–7%.

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4 A.R. Hutabarat, R. Anglingkusumo, F. Majardi, R.E. Wimanda, 'Research on Optimal Policy Rules for Forward-Looking Inflation Control', BEMP Vol.2 Num. 3, December 2000 and R. Anglingkusumo, C. Ligaya, 'Measuring Inflation in Forward-Looking Monetary Policy Implementation', BEMP Vol.2 Num. 4, March 2000.

5 Bank Indonesia Model (MODBI), Bank Indonesia General Equilibrium Model (GEMBI), and Small Scale Macroeconomic Model (SSMM).

box

The Bank Indonesia Transformation Program

With the effectiveness of Act 23 of 1999, Bank Indonesia is to undertake basic changes in accordance with the spirit of the Act, namely independence, transparency, and accountability. At the same time, the changing demand on national and global scales requires Bank Indonesia to undertake a number of fundamental changes. On a national scale, reforms in the implementation of public policy demand governance improvements at Bank Indonesia, which imply increased transparency and accountability in the process of policy determination. In addition, the financial and monetary crisis that began in 1997 requires that the central bank improve its image and rebuild its credibility in order to gain public confidence, which is vital for the effectiveness of monetary policy. On a larger scale, the credibility of a country's central bank greatly influences international confidence.

These considerations have prompted Bank Indonesia since 2000 to undertake an evaluation on its vision and mission, organization, work patterns, and human resource development. Formally, since February 2001 the various reforms have been formulated in a systematic, comprehensive and integrated way into the Bank Indonesia Transformation Program. This strategic change program is undertaken to accelerate the creation of a new Bank Indonesia, which will be better able to anticipate change and adapt to new circumstances, as well as to meet the expectations of stakeholders. This target is achieved through the re-formulation of Bank Indonesia's vision and mission, strategic values, and strategic objectives. Operationally, ten strategic changes (covering the areas of monetary policy, banking, payment system, and internal mana-

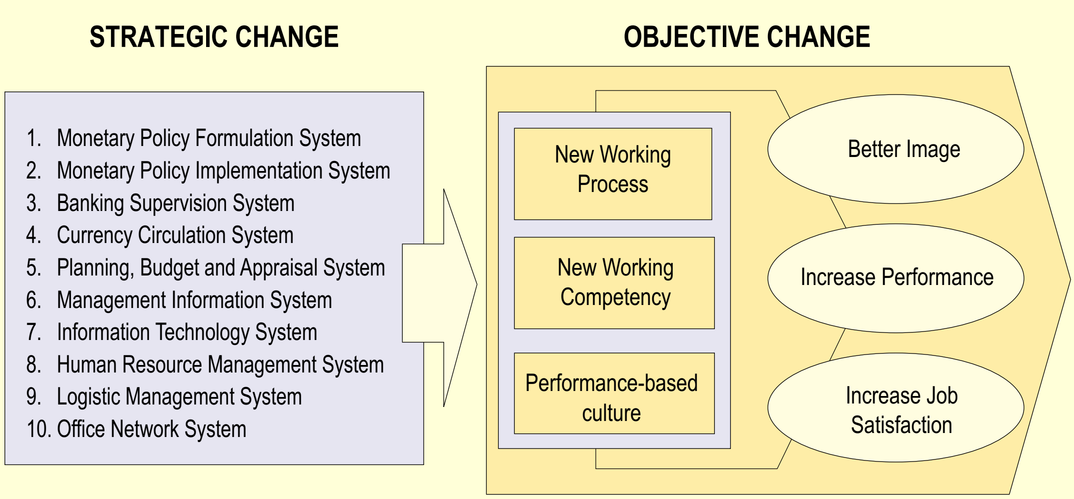


Diagram 1.
Strategic Change in Transformation Program

gement) have to be managed in an integrated way to achieve certain targets for change. These include new work processes, new work competencies, and a new work culture based on performance to enhance Bank Indonesia's performance and image (Chart 1).

In the monetary field, transformation is aimed at enhancement of the quality of monetary policy formulation and economic research, as well as the quality of monetary policy implementation with the focus on achieving monetary stability. This objective is achieved by reconfirmation of strategic objectives, process improvements, and enhancements of human resources, as well as organization in the monetary sector. In the banking area, the target of transformation is the attainment of a banking sector which is in line with international standards, including all the preparations needed for the transferring of the bank supervision function to the Supervision Institution for the Financial Services Sector. Technically, this is undertaken by designing an early warning system to support the implementation of risk-based supervision and financial stability function. In addition, the transformation program in the banking sector designs training and certification programs for bank supervisors and auditors in relation to risk-based supervision. In light with the segregation of the bank supervision function, the transformation program is to design a contingency plan for transferring that function to the new institution and a concept for Bank Indonesia's organization in relation to its role in maintaining financial system stability in Indonesia. In the internal management area, the transformation program would enhance good governance through rearrangement of the planning, budgeting, performance management, human resource management, information technology management, information management, and logistic management areas

chapter 2 MACROECONOMIC CONDITIONS

chapter 2

MACROECONOMIC CONDITIONS

Indonesia's economic growth slowed in 2001, but to a pace that was still better than the growth experienced by other countries in the ASEAN region. Real Gross Domestic Product (GDP) expanded by 3.3%, down from 4.9% in the previous year (Table 2.1). This outcome was lower than Bank Indonesia's beginning of year projection of 4.5% – 5.5%.

This slowdown was attributable to unfavorable domestic and external developments. Domestically, there was slow progress in debt and corporate sector restructuring, and in ongoing internal consolidation of banks, as well as a heavy financial burden on the government. In addition, there was continuing high risk and uncertainty related to rising social and political tensions and to weak law enforcement. This caused a deterioration in business confidence, which undermined production and investment and hampered further economic expansion. From the external side, the world economy began to slow in quarter I-2001 and it deteriorated further after the World Trade Center (WTC) tragedy on 11 September 2001. This disrupted advanced countries' economies, including those that have been Indonesia's important investors and trading partners.

Table 2.1
Gross Domestic Product

Item	1999 Growth	1999 Contri-bution	2000* Growth	2000* Contri-bution	2001** Growth	2001** Contri-bution
	Percent					
GDP (Real)	**0.8**	**0.8**	**4.9**	**4.9**	**3.3**	**3.3**
By Expenditure						
Consumption	4.3	3.3	3.9	3.1	6.2	4.8
- Private	4.6	3.2	3.6	2.6	5.9	4.2
- Government Consumption	0.7	0.1	6.5	0.5	8.2	0.6
Investment[1)]	-18.2	-4.5	21.9	4.4	4.0	0.9
Export and Service	-31.8	-11.4	26.5	6.4	1.9	0.6
Import and Service	-40.7	-14.3	21.1	4.4	8.1	1.9
By Sector						
Agriculture	2.2	0.4	1.7	0.3	0.6	0.1
Mining	-1.6	-0.2	5.1	0.5	-0.6	-0.1
Manufacturing	3.9	1.0	6.1	1.6	4.3	1.1
Electricity, Gas & Water supply	8.3	0.1	8.8	0.1	8.4	0.1
Construction	-1.9	-0.1	5.5	0.3	4.0	0.2
Trade, Hotel & Restaurant	-0.1	0.0	5.6	0.9	5.1	0.8
Transportation & Telecommunication	-0.8	-0.1	9.4	0.7	7.5	0.6
Financial Institution	-7.2	-0.5	4.3	0.3	3.0	0.2
Services	1.9	0.2	2.2	0.2	2.0	0.2

1) Investment is gross domestic fixed capital formation
Source : BPS-Statistics Indonesia

In this environment, the demand-side sources of economic growth, particularly investment and exports, did not develop as expected. Instead, economic growth depended mainly upon consumption, both from the household and government sectors. On the supply side, almost all economic sectors expanded, although at lower rates than 2000; only the mining sector contracted. Manufacturing and the trade, hotel, and restaurant sector, which were expected to boost economic growth, could not provide much stimulus, mainly due to various constraints that limited expansion in those two sectors.

Slower economic activity impacted on employment, because the provision of new job opportunity could not match growth of the workforce. Deteriorating employment conditions were reflected in, among others, rising unemployment, vigorous strikes, labor disputes, and layoffs.

AGGREGATE DEMAND

At the beginning of 2001, Indonesia's economy was expected to expand robustly by 4.5% - 5.5%. Growth would originate in exports, investment, and continuing strong consumption spending. This quite optimistic estimate was based on the expectation that several important internal problems, such as debt and bank restructuring, would significantly improve. On the external side, global economic conditions were expected to remain conducive to Indonesia's exports.

As 2001 progressed, not all of these assumptions came to fruition. A number of important domestic matters, such as credit and corporate sector restructuring and bank intermediation have not shown any meaningful progress. This was further complicated by developments in the world economy; it started to slow approaching the end of quarter I-2001 and deteriorated further after the 11 September 2001 WTC tragedy, and this impacted unfavorably on Indonesia's external sector.

During the reporting year, economic growth largely originated in domestic activities (domestic demand). There was rapid growth in consumption spending, 6.2%, well above the growth in 2000 that was expanded by 3.9%. Investment and exports slowed to 4.0% and 1.9%, respectively. Rising demand that was driven by consumption and was not match by adequate investment led to deterioration of capital stock formation.

In 2001, **consumption** contributed 4.8% to GDP growth, far higher than in the previous year's 3.1%. This was due to the rapid growth in consumption spending and consumption's large share of GDP. By component, high consumption spending occurred in both the household and government sectors, with growth of 5.9% and 8.2%, and contributing to GDP growth of 4.2% and 0.6%, respectively (Chart 2.1). This high growth of consumption spending was still below its average pre-crisis growth when it averaged more than 7% annually. Higher household consumption stemmed from rising disposable incomes and improved consumer financing from both banks and other financing institutions. Rising disposable incomes originated in higher minimum wages and back payments of salary

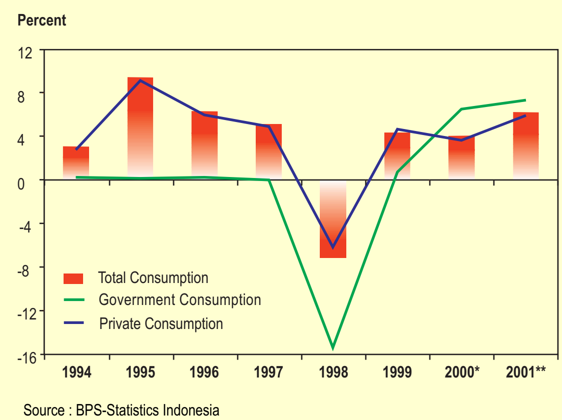


Chart 2.1
Consumption Growth

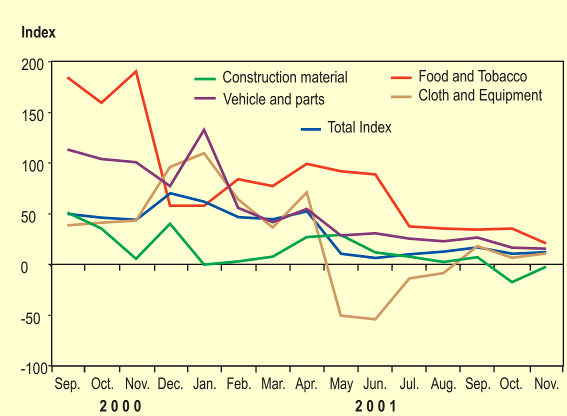
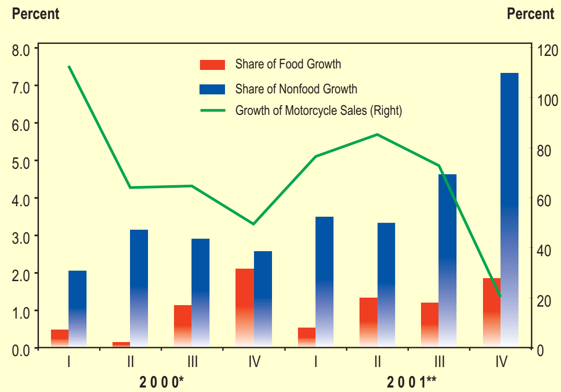
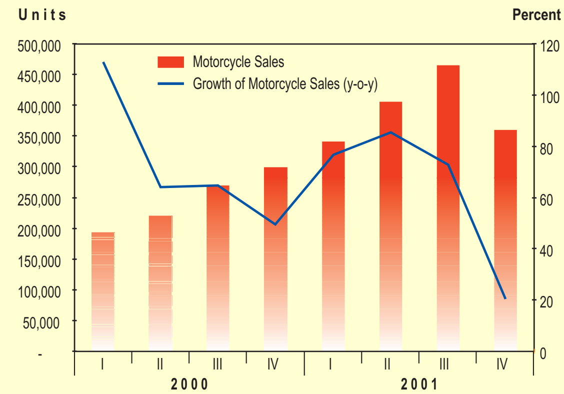


Chart 2.2
Retail Sales Survey



Source : BPS-Statistics Indonesia

Chart 2.3
Share of Growth of Consumption Expenditure by Group



Source : GAIKINDO

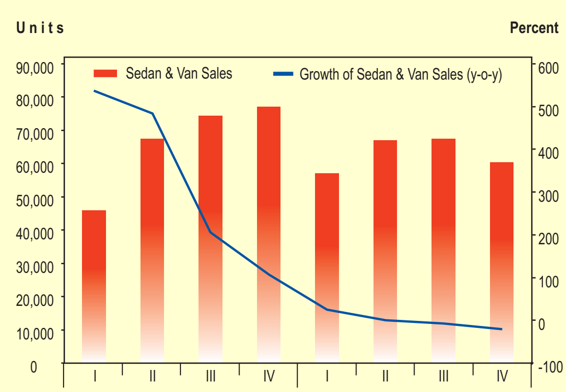
Chart 2.4
Motorcycle Sales

increases for civil servants and members of the Armed Forces and the Police. Meanwhile, improved consumer-financing was reflected in ongoing high growth of consumer credits extended by banks and in the usage of credit cards.

Higher household consumption was reflected in various indicators (e.g., motor vehicle sales) and results of surveys conducted by Bank Indonesia and other institutions (e.g., the retail sales and consumer surveys). Results of the retail sales survey conducted by Bank Indonesia showed that total sales in 2001 rose by 25.8% relative to 2000 (Chart 2.2). Based on this survey, retail sales expanded in almost all good categories that are surveyed, the only exception being fuels. The major contributors were: handicrafts and toys; foodstuffs, beverages, and tobacco; and household equipments. This was in line with the trend in household consumer spending, which continued to be concentrated in non-foodstuffs, for instance durable goods such as motorcycles. Consumer spending on foodstuffs itself also recorded quite a sharp rise, yet its contribution was lower than the contribution of non-foodstuffs (Chart 2.3).

After a slowdown in 2000, motorcycle sales were on an upward trend in 2001 and that trend was steep during the first nine months of the year. This rise was prompted by imports of motorcycles from China, which were relatively cheap and complemented by accessible financing (Chart 2.4). In addition, sales of sedans and vans remained high in 2001, but total units sold were actually down from 2000 (Chart 2.5).

A number of surveys conducted by other institutions also indicated rising consumption, for



Source : GAIKINDO

Chart 2.5
Car and Van Sales

example, the consumer tendency survey of the Central Statistical Agency (BPS) and the consumer confidence survey by the Danareksa Research Institute. The consumer tendency survey indicated rising consumer optimism towards economic conditions, which boosted private consumption spending. In line with this, Danareksa's survey also indicated rising consumer confidence, especially in the second half of 2001, prompted by expectations of improved economic conditions under the new political administration.

The rise in household spending was also reflected in more financing for consumption, for instance, consumer credit from banks and financing companies in the form of credit cards. During 2001, the annual growth of consumption credit reached 45.7% and was particularly strong in the first half of 2001 (Chart 2.6). In addition, the use of credit cards has widened markedly, as reflected in the number of credit card holders, which increased by 31.8% during 2001; the volume of credit card transactions grew by 41.4%. The use of debit cards was also on the rise, although not as steeply as credit cards. The total

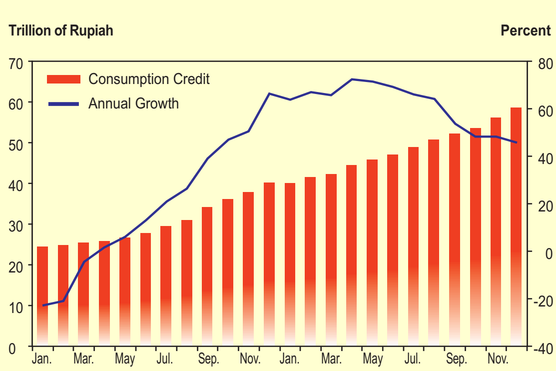


Chart 2.6
Consumption Credit

Table 2.2
Non-cash Electronic Payment Instruments

Item	1998	1999	2000	2001
1. Credit Card				
Number of Holders				
(In thousands of person)	2,028.4	2,043.8	2,622.6	3,457.2
Volume of Transactions				
(In trillions of Rp)	4.9	10.4	13.6	19.2
2. Debit card				
Number of Holders				
(In thousands of person)	5,374.4	12,111.0	13,103.7	13.587.5
Volume of Transactions				
(In trillions of Rp)	2.6	3.2	4.7	6.7

number of debit cardholders has risen by 3.7%, while the total transaction volume rose by 42.2% (Table 2.2). Another indicator, consumption financing, also grew rapidly, particularly at the beginning of 2001 and in November of that year. It recorded an annual growth of 58.0%. Consumer financing has tended to slow since the beginning of quarter II-2001 (Chart 2.7), in line with rising interest rates.

Bank Indonesia's consumer survey also indicated rising household consumption spending in line with improved consumer confidence. This was

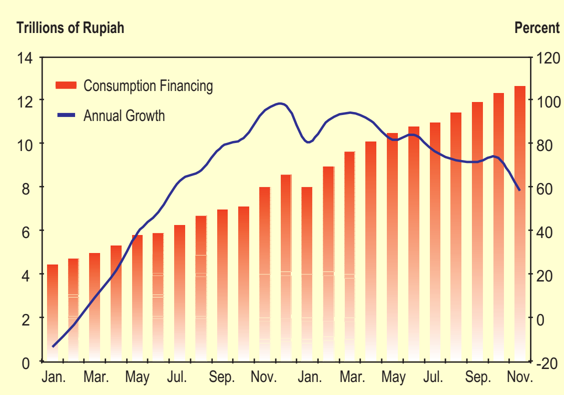


Chart 2.7
Consumption Financing

mainly prompted by improved consumer expectations around the time of the transition in national leadership. Another factor was improved financial conditions of respondents compared with the previous period. Survey respondents also remained optimistic as regards rising incomes, both their current income and expected income in the coming 6–12 months. Overall, consumer optimism was reflected in the consumer confidence index, which began rising at the beginning of the year and peaked in August in line with optimism towards the new government administration. However, that consumer optimism could not be maintained and it generally deteriorated through the rest of the year, despite a slight improvement at year end (Chart 2.8).

Continuing strong consumption was also reflected in the demand for currency held by the public, which continued rising. Strong demand for currency suggested ongoing needs for currency for transaction activities, which in part financed consumer spending.

Viewed by origin of goods, the rise in consumption was satisfied by both domestically produced goods and imports. This was reflected in imports of consumption goods, which rose rapidly in the first half of 2001, before slowing towards the end of the year. The rise at the beginning of the year may have been partly precautionary in light of the possibility of a continuing depreciation of the rupiah brought on by rising uncertainty in advance of the transition in national leadership. By type of goods, the largest increase occurred in non-durable consumption goods, which grew by 21.9%. Imports of raw materials for foodstuffs and beverages grew by 3.4% and 0.2%, respectively (Chart 2.9).

As noted, the various indicators of consumer spending (including consumer credit and consumer financing) confirm a rapid increase in consumption in the reporting year, particularly at the beginning of the year followed by a slowdown in the second half of 2001.

As was the case with household consumption, government consumption in the reporting year also expanded rapidly, by 8.2% compared with last year's 6.5%. This rise in government consumption may be related to the implementation of regional autonomy, whereby a major part of regional govern-

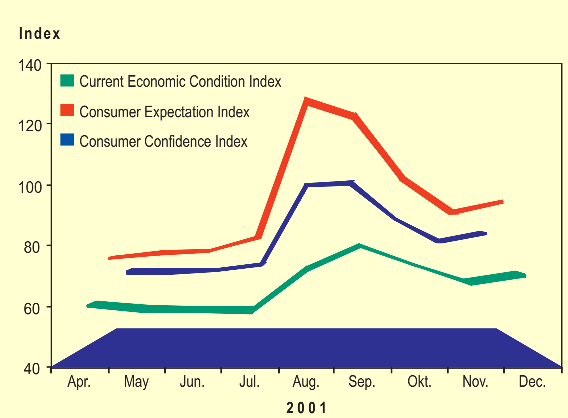


Chart 2.8
Consumer Survey

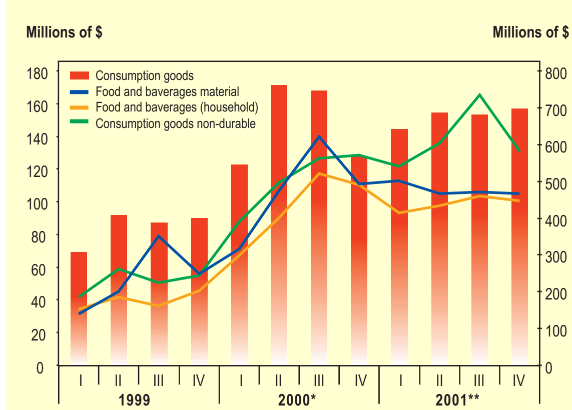


Chart 2.9
Consumption Goods Import

ment spending was allocated for personnel and material expenditures. The rise in regional governments' consumption spending was larger than the decline in central government consumption, resulting in the increase of total expenditure.

Investment was a secondary contributor to economic growth in 2001.[1] It expanded by 4.0%, which represented a contribution towards GDP growth rate of 0.9%, far lower than past year's 21.9%. Low investment was caused by a large number of factors, such as: increasing uncertainty; security disturbances; unpredictability in law enforcement; limited bank intermediation; less conducive regional regulations for investment activities related to the implementation of regional autonomy; negative sentiment due to the delays in drawdowns of loans from the International Monetary Fund (IMF); relatively high domestic interest rates; and slow foreign debt restructurings. Consequently, companies tended to focus more on internal consolidation, which caused low realization of new investments and little expansion of production capacity. *(Box : Calculation of the Capital Stock Using the Perpetual Inventory Method).*

In general, slow investment was reflected in low realizations of new investments—undertaken by both foreign and domestic companies—and in declining imports, particularly those related to business, such as raw materials and capital goods. During the period January – October 2001, the values of raw material and capital good imports declined by 8.4% and 10.3%, respectively, compared with the same period in the previous year. Meanwhile, during 2001, the realization of foreign direct investment was only

Table 2.3
Ratio of Realized to Approved Foreign and Domestic Investments

Item	1999	2000	2001
Domestic Investment			
1. Investment plan approved			
– Number of project	228	355	249
– Value (billions of rupiah)	53,168	92,410	58,673
2. Investment realization			
– Number of project	29	22	5
– Value (billions of rupiah)	1,741	1,031	95
3. Ratio of realized to planned investment (%)			
– Number of project	12.7	6.2	2.0
– Value	3.3	1.1	0.2
Foreign Investment			
1. Investment plan approved			
– Number of project	1,174	1,521	1,317
– Value (billions of rupiah)	10,892	15,420	9,028
2. Investment realization			
– Number of project	214	96	15
– Value (billions of rupiah)	1,285	897	53
3. Ratio of realized to planned investment (%)			
– Number of project	18.2	6.3	1.1
– Value	11.8	5.8	0.6

Suorce : BKPM

0.6% of the total value of approvals. The realization of domestic investments was similarly low, only 0.2% of total investment approvals (Table 2.3). Viewed by approvals, investment for the chemical industry was the largest, both for foreign and domestic investment. By location, the largest foreign investment were in East Java and Riau; the largest domestic investment were in Riau and South Sulawesi.

Other indicators of investment activities also suggested low investment growth, such as the results of the business activity survey conducted by Bank Indonesia and the business tendency survey conducted by the Central Statistical Agency. The business activity survey showed that the number of respondents undertaking investments tended to drop,

1 Investment, as a flow concept, is defined as Gross Domestic Fixed Capital Formation (GDCF)

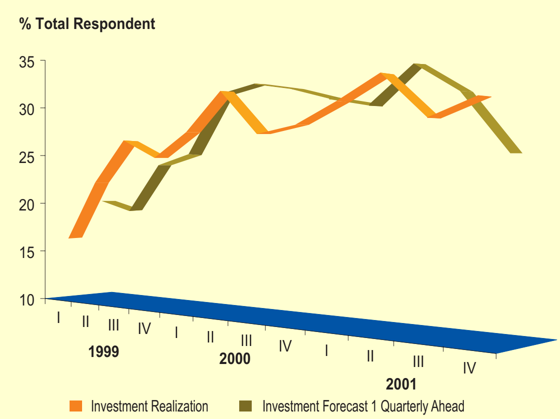
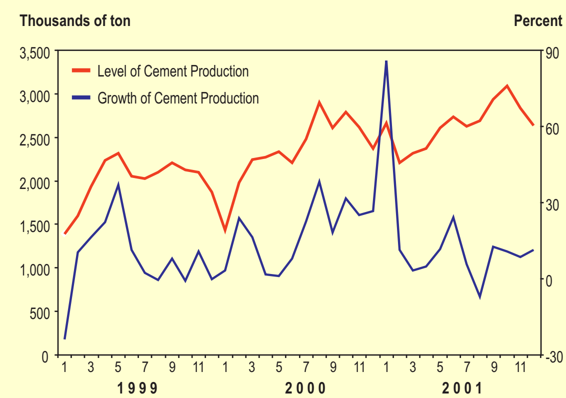


Chart 2.10
Investment in Business Survey



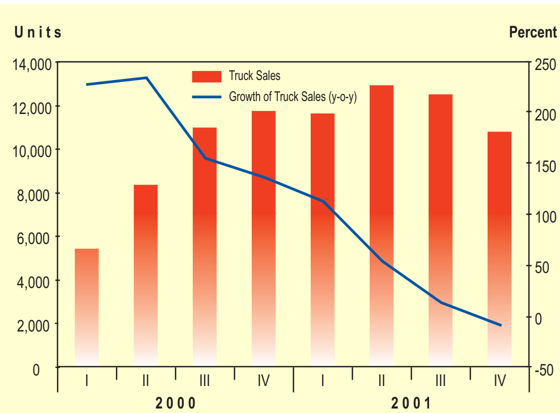
Source : Indonesian Cement Association

Chart 2.12
Cement Production

although it did rise a bit at the end of the reporting year (Chart 2.10). In line with the results of the business activity survey, the business tendency survey showed diminishing optimism on the part of business people towards company and business conditions.

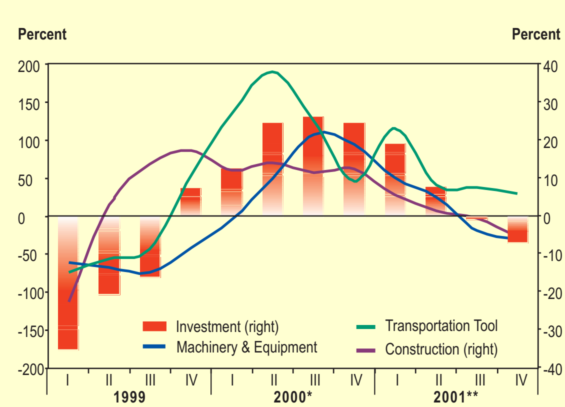
Slower investment activity was also suggested by a number of prompt indicators for investment, such as sales of trucks and cement production. Both slowed towards the end of the year (Chart 2.11 and Chart 2.12). Truck sales have slowed quite sharply since mid-2000 and this continued through the end of quarter IV-2001, which recorded a decline of 8.1%. Cement production began to slow in quarter II-2001; cumulatively during the first 11 months of 2001, it grew by 12%, compared with 17% during the same period a year earlier. This pattern of cement production was in line with construction investment during the reporting year, which declined markedly compared with the year before (Chart 2.13).

Low investment growth was partly caused by bank intermediation not having fully recovered, and



Source : GAIKINDO

Chart 2.11
Truck Sales



Source : BPS-Statistics Indonesia

Chart 2.13
Investment by Type

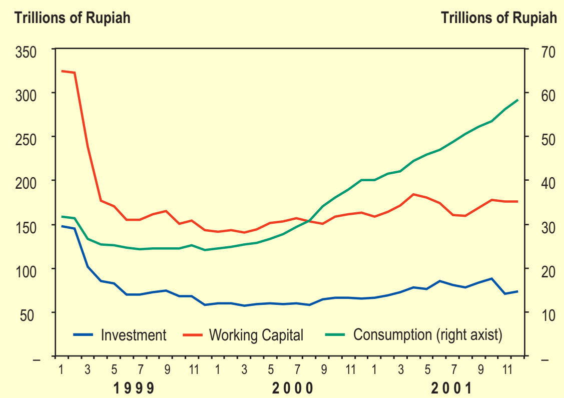


Chart 2.14
Banking Credit by Usage

funds available for investment, particularly from domestic sources, remaining limited (Chart 2.14). This was reflected in marketable securities, such as bonds and SBIs, which continued to dominate banks' asset. Investment financing during the reporting year originated largely from companies' own funds, which showed an increase although in limited amount. Based on a survey conducted by Bank Indonesia, the use of own funds by companies may have increased from 40% to 60% of their total business financing.[2]

These conditions have limited domestic financing for investment in the real sector. This was reflected in a continuing large savings-investment gap, although it narrowed slightly from last year. The ratio of the savings-investment gap relative to GDP reached 3.4% in 2001, down from 5.2% in 2002 (Table 2.4). This decline was mainly caused by a wider government deficit, which stemmed from a sharp increase in current expenditure, particularly for subsidies and interest payments.

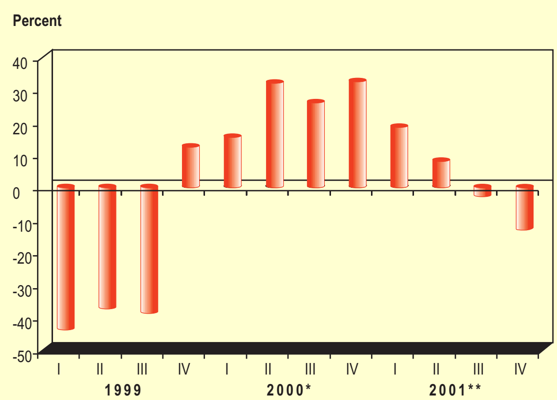
2 Research on Credit Crunch by Financial Market Structure and Development Studies Division-Bank Indonesia

Table 2.4
Saving-Investment Gap

	1998	1999	2000	2001
	Current Price			
Government				
Saving	48,0	62,9	36,1	6,6
Investment	49,8	74,2	64,4	61,3
Deficit (–)/Surplus (+)	–1,8	–11,2	–28,3	–54,7
Private				
Saving	236,4	222,9	344,9	406,9
Investment	193,3	166,1	249,5	300,9
Deficit (–)/Surplus (+)	43,1	56,8	95,4	106,0
Total				
Saving	284,4	285,9	381,0	413,5
Investment	243,0	240,3	313,9	362,2
Deficit (–)/Surplus (+)	41,4	45,5	67,1	51,3
	% of GDP			
Government				
Saving	5,0	5,7	2,8	0,4
Investment	5,2	6,7	5,0	4,2
Deficit (–)/Surplus (+)	–0,2	–1,0	–2,2	–3,7
Private				
Saving	24,7	20,1	26,7	27,6
Investment	20,2	15,0	19,3	20,4
Deficit (–)/Surplus (+)	4,5	5,1	7,4	7,2
Total				
Saving	29,8	25,8	29,5	28,0
Investment	25,4	21,7	24,3	24,6
Deficit (–)/Surplus (+)	4,3	4,1	5,3	3,4
GDP (in trillions of Rp)	955,8	1.110,0	1.282,0	1.476,2[1]
Current Account (in billions of $)	4,1	5,8	8,0	5,0
Average Exchange Rate (Rp/$)	1.008,8	7.850	8.438	10.255

1) GDP at current price = assumption used in 2001 State Budget

The smallest contributor to growth in GDP in 2001 was **exports of goods and services**, which recorded growth of 1.9% and contributed only 0.6% to GDP expansion. This was far lower than last year when it reached 26.1% (Chart 2.15). Slower exports were caused by several factors, including constraints on the production of exports and weak demand for export goods in foreign markets. On the domestic side, slower exports were particularly due to rising uncertainty and security incidents, which disrupted production. Examples include Exxon Mobil Oil in Arun and Caltex mining in Pekanbaru. Rising uncertainty



Source : BPS-Statistics Indonesia

Chart 2.15
Goods and Services Export in GDP

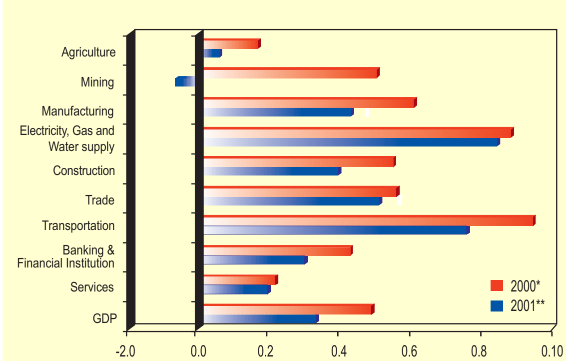
and security disruptions were related to: heated socio-political conditions in the run-up to the transition in national leadership; conflicts between ethnic groups; and unrest related to regional disintegration issues. In addition, vigorous demonstrations and labor strikes have occurred in several important export industries (such as textiles and footwear) and these have dis-puted exports.

On the external side, slower exports stemmed from declining world economic growth, including in countries that have been Indonesia's major trading partners, such as the US and Japan. At the beginning of 2001, the US and Japanese economies were estimated to grow by 4.1% and 2.2%, respectively. In the event, the US recorded lower growth and even slipped into recession at the end of quarter III-2001.[3] Meanwhile, the Japanese economy contracted. Weakened economic growth in these two countries caused a slowdown in the world economy, followed by generally lower prices in the international market. Both have pushed down Indonesia's export growth.

In line with slower exports, **imports** also slowed sharply, although they rose for a while at the beginning of 2001. Imports of goods and services recorded growth of 8.1% in 2001, far lower than 21.1% in 2000. Slower imports were roughly in line with decelerating investment, and disrupted domestic restructuring and industry revitalization. Imports of raw materials and capital goods, which are generally used to support investment and production, declined steeply, by 8.5% and 10.2%, respectively. In addition, lower import growth was due to the rupiah exchange rate, which depreciated and fluctuated quite sharply during 2001.[4] This raised the price of imports measured in rupiah. Import growth was dragged down further by partial restoration of bank intermediation function which limited business financing, including for the purchase of imports for business activities.

Aggregate Supply

Viewed from the production side, almost all economic sectors expanded in 2001, albeit at slower



Source : BPS-Statistics Indonesia

Chart 2.16
GDP Growth by Sector

3 The National Bureau for Economic Research (NBER) estimates that US economy entered recession in March 2001
4 Overall, the rupiah exchange rate depreciated by 17.7% against the US dollar

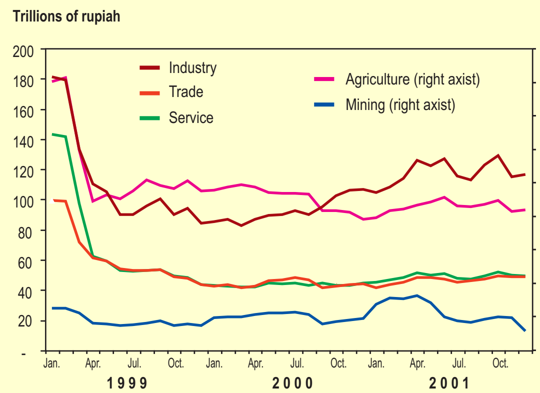


Chart 2.17
Banking Credit by Sector

rates than 2000. The only exception was the mining and quarrying, which experienced a contraction (Chart 2.16). The slowdown was related to a number of problems that were still weighing on the economy, such as continuing high uncertainty in the social, political, security, and legal areas; slow progress in foreign debt, credit, and corporate restructuring; unfavorable world economic conditions; and limited credit from the banking sector (Chart 2.17).

Manufacturing, followed by trade and transportation, remained the largest contributing

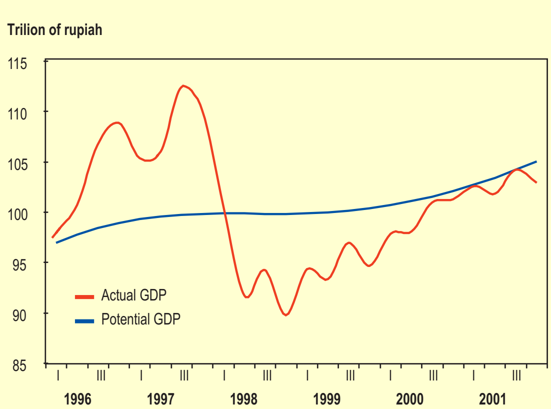


Chart 2.18
Output Gap

sectors. Agriculture recorded its lowest growth since 1998.

Lower overall economic growth was accompanied by low growth of investment, originating in both new investment and expansion of existing activities, which limited the increase in potential output. Meanwhile, actual output has increased rapidly in the past two years, causing the output gap to narrow, which in turn puts pressure on prices (Chart 2.18).[5]

Short-Term Supply

On the supply side, slower growth occurred in almost all economic sectors, with almost all sectors still recording positive growth. As was the case last year, manufacturing, and trade and transportation (which account for about 50% of GDP) continued to make the largest contributions to GDP growth. Meanwhile, the agriculture and plantation sector (which is the second largest sector after manufacturing and which was the *'prima donna'* of sectors for a while at the beginning of the crisis) grew by less than 1%, the lowest since the 1998 crisis.

As already mentioned, large ongoing problems faced by Indonesia's economy have hampered efforts to expand total economic capacity. Optimism over the national leadership transition, which improved economic conditions for a while, could not be sustained. In addition, the implementation of regional autonomy created a number of new problems, such as adding to the high cost economy, which hampered business. Another important problem related to regional autonomy was deteriorating policy coordination, in particular as it related

5 The output gap is the difference between actual output and potential output. Potential output is measured using the HP filter method

to the economy, between the central government and the regional governments or between regional governments. These various problems prompted many investors to delay implementation of their investment plans.

On the external side, economic developments abroad did not contribute much to the growth of domestic economic activity. A slowdown in the world economy, which began early in the reporting year, was amplified by the WTC tragedy. In addition, a follow-on impact from the tragedy has caused a decline in tourism, which has hurt business in the trade, hotel, and restaurant sector. At the same time, prices in the world market have trended down—including for agriculture and mining commodities—which impacted unfavorably on agriculture and mining.

These various problems have depressed foreign capital inflows into Indonesia, at a time when domestic financing was in short supply. In turn, expansion of economic capacity has been very limited and there are indications that several economic sectors have even slumped.

In the last three years, **manufacturing** has always been the largest contributor to economic growth. In 2001, the growth of this sector was 4.3%, with a contribution to GDP growth of 1.1%, largely from non-oil/gas industry. The most notable sub-sectors in this regard were: foodstuffs, beverages and tobacco; transportation machinery and complementary equipment; and chemicals and rubber goods. However, there were a number of problems that held down business activity in this sector in 2001. The main problem was limited financing for business activities, which was reflected, among others, in the relatively small rise in investment credits. In conditions where there is continuing high uncertainty concerning the business climate, foreign investment inflows could not be expected in any meaningful amount. This was magnified by a number of investors having transferred their businesses to other more promising countries, such as China and Vietnam.

In addition to the problem of limited financing, the industrial sector was further weighed down by the impact of government policies related to price and tariff adjustments. These policies raised production costs, which made it difficult for business people to expand their businesses. Higher production costs—which largely arose from adjustments to basic electricity tariffs and fuel prices whereby fuel prices in the international market are used as the basis for determining fuel prices for domestic industries—required this sector to make quite large adjustments. In addition, sluggishness in the world economy hit the export-oriented industrial sector. Also, problems in trade regulations have limited the room for maneuver of Indonesian exports, especially the implementation of trade barriers, such as anti-dumping regulations and human rights-related problems imposed by trading partners.

With weaker exports, the production of goods in 2001 focused on the domestic market. Another matter hampering Indonesia's export trade was government regulations, such as the prohibition on imports of unproccessed leather hides. While this prohibition was meant to prevent hoof and mouth disease from entering Indonesia, it disrupted the leather processing industry.

To cope with these various constraints and unfavorable developments, the government has made various efforts to spur the growth of manufacturing. For example, the government allowed import of used heavy equipment and computers to meet the need for cheap capital goods for domestic industry. Another measure was the lifting of the import ban on printed matter with Chinese characters, which would attract investors from Taiwan-China, Hong Kong, and Singapore. In addition, in order to bolster development of the domestic machinery industry, the government has provided relief from import duties on imports of raw/additive materials and components for machinery and rolling motor assemblies. However, those efforts have not been fully successful in overcoming the manufacturing slowdown.

The **trade, hotel, and restaurant** sector also boosted economic growth. This sector grew significantly, by 5.1% in line with continuously rising consumption demand, in particular for foodstuffs and retail goods. Relatively high growth in this sector mainly came from domestic trade, which was reflected in rapid expansion of the retail sector and the opening of several new locations for retail trade in a number of large cities of Indonesia. The growth was in line with rising consumer financing facilities, such as consumption credits that could be utilized by the household sector. Expansion of this subsector was also reflected in the property survey, which showed a rise in the occupancy rate in trade centers, particularly for retail business.

Meanwhile, the hotel subsector declined sharply, particularly after the WTC tragedy. This was also reflected in the property survey, which experienced a sharp decline in hotel occupancy rates; during the same period, hotel tariffs did not increase in any meaningful way (Chart 2.19).

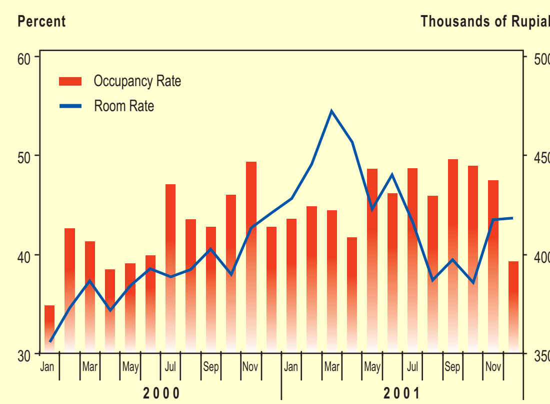


Chart 2.19
Hotel Occupancy Rate

The **transportation** and **communication** sector recorded high growth of 7.5% and became the third largest contributor to GDP growth rate. Highway transportation remained the main engine of growth in this subsector. Meanwhile, growth in the communication subsector still stemmed in substantial part from rising demand for new telephone lines and expanding activity in the cellular telephone operating business.

The **financial, rental,** and **service company** sector grew by 3.0%, down from 4.3% in 2000, mainly contributed by banking. While some banks are expanding credits, this subsector slowed due to continued bank disintermediation. This was mirrored in the composition of banks' asset portfolios, which were still dominated by SBIs and bonds. Slower growth in this subsector was also suggested by developments in bank credit, which grew by only 11.5%, slower than the previous year's 15.5%.

Agriculture, which was a mainstay of growth at the beginning of the crisis, experienced very low growth, only 0.6% in 2001, the lowest since 1998. Several problems contributed to low growth in this sector, including high prices for fertilizers and pesticides; low quality of seeds; disruptions to production due to natural disasters; and infestations of pests and plant disease. Those various problems caused a decline in productivity. Another problem was price fluctuations, specifically the basic price of *gabah* (unhulled paddy), which reduced the incentive for farmers to grow more. Due to these problems, the production of a number of important commodities (such as rice, corn, and soybeans) declined.[6] In the reporting year, rice production only reached 49.6 million tons of milled dried *gabah*, a decline of 4.5% compared with the previous year. Meanwhile, production of corn and soybeans reached 9.2 million tons of dried shelled corns and 0.8 million tons of dried shelled soybeans, respectively, representing declines of 5.3% and 19.7% compared with 2000.

Long-Term Supply

As described, the various problems in the real sector limited additions to overall economic capacity (potential output). There was low investment in both new projects and expansions of existing business activities. Also, there was rapid growth of the workforce, which was still dominated by low quality workers.

Limited additions to economic capacity from new investments were indicated by the business activity survey, which showed a decline in both investment realizations in quarter three and investment interest in the last quarter of the reporting year (Chart 2.10). The low level of new investment was clear from investment realizations that were virtually nil (as a proportion of approvals), for both domestic and foreign investment. There was also low growth in investment credits.

Meanwhile, limited additions to economic capacity originating in expansions of existing businesses were reflected by low utilization rates in the industrial sector, as shown by Bank Indonesia's manufacturing sector survey. Results of that survey up to November 2001 indicate that although aggregate capacity utilization in manufacturing was still low, there were a number of subsectors that have experienced quite sharp increases in utilization rates, such as the foodstuff, beverage, and tobacco industry and non-metal quarrying. Industries recording an average utilization of 65% of installed capacity included: quarrying and plastics; textiles, ready-made clothes, and leather goods; and the paper, printing, and publishing industry. The metal-goods industry and the base metal industry experienced a decline in their utilization rates (Chart 2.20). Continuing low utilization rates in manufacturing indicated that the extent of ongoing internal problems, which have limited the utilization of existing capacity. In addition, the ongoing

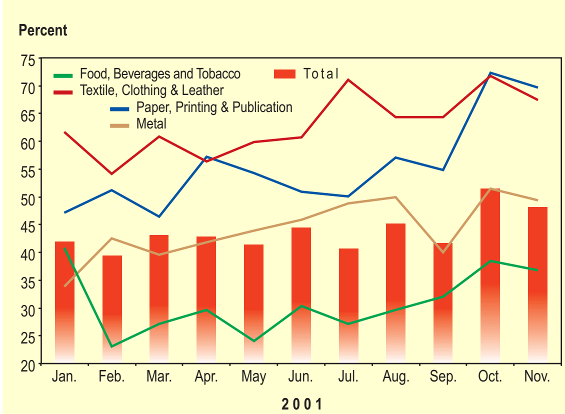
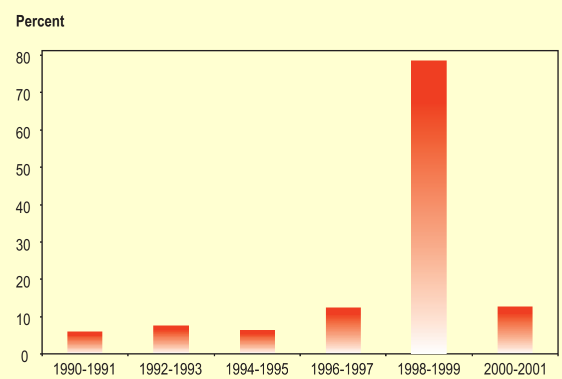


Chart 2.20
Utilized Capacity

6 Preliminary figures from the BPS-Statistics Indonesia



Source : BPS-Statistics Indonesia (processed)

Chart 2.21
Incremental Capital Output Ratio

environment of high uncertainty and business risk caused businesses to delay expansions of capacity.

These conditions paint a picture of essentially low growth of potential output in 2001. By contrast, actual output expanded relatively rapidly, which caused the output gap (the difference between potential and actual output) to narrow appreciably.

The trend toward a narrower output gap is dangerous. If quick efforts are not made to raise potential output, pressures on prices will begin to increase, especially in the light of sharp increases in capacity utilization in industries that produce goods that are included in the CPI basket. If the various problems that have limited new investments and business expansions are not dealt with quickly, continued increases in actual output could lead to higher CPI inflation in the coming period.

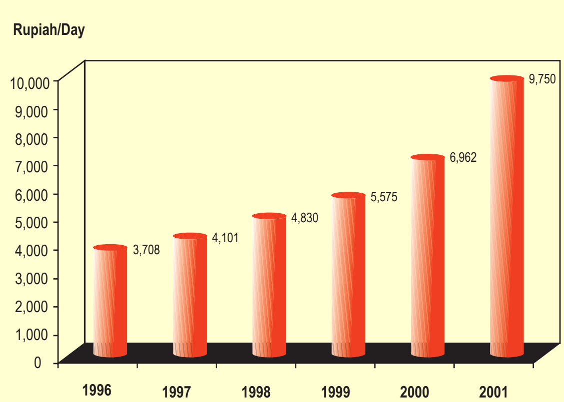


Chart 2.22
Provincial Minimum Wage (average)
in Rp/Day

The various problems faced by Indonesia's economy, as described earlier, have caused economic efficiency to remain below pre-crisis levels. In order to measure the efficiency of an economy from one period to another, one common indicator is the Incremental Capital Output Ratio (ICOR).[7] During period 2000–2001 Indonesia's ICOR improved somewhat relative to the period of 1998 – 1999 (Chart 2.21), but it remains above pre-crisis levels. This is evidence that in 2001 the economy remains less efficient as it was in the pre-crisis period.

Labor Issues

The slowdown in the economy in 2001, described earlier, has had an unfavorable impact on labor conditions. This was reflected in a decline in the ratio of total employment in the formal sector to total labor force, because increases in the labor force were not matched by sufficient new jobs. However, the total number of unemployed people and semi-unemployed people did not increase in a meaningful way because some of those workers unable to find employment in the formal sector, shifted to the informal sector.

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7 Formula used to calculate ICOR between t_2 and t_1 :

$$ICOR_{t_1,t_2} = \frac{\sum_{t=t_{1-1}}^{t_{2-1}} GFCF_t}{GDP_{t_2} - GDP_{t_1}}$$

GFCF = Gross Fixed Capital Formation

Meanwhile, labor welfare, which is measured by provincial minimum wages, increased on average, although it remains below the minimum cost requirements. Labor disputes colored the reporting year as reflected in a continuing incidence of strikes and layoffs.

The total labor force in 2001 is estimated at 98 million individuals, which represents an increase of nearly 2.5% over the previous year. This rise in numbers has not been followed by a rise in quality, as reflected by the continuing large proportion of labor force with only primary school education, some 63.5% or around 62 million individuals. The United Nation Development Program (UNDP) survey showed that Indonesia's Human Development Index (HDI) ranked 109th among 147 countries.[8] Based on year 2000 population census, the total population of working-age (15 years and above) was 141.2 million individuals, 67.8% of whom (95.7 million individuals) were classified as in the labor force. In 2001, this figure is estimated to have risen to 98 million people. Of this total labor force, around 93% are working while 7% are openly unemployed. However, around 36% (or 35 million) of the total working population worked less than 35 hours per week. By type of work, most of the working population (45.3%) was in the agriculture sector. Although the total working population increased, the working population in the formal sector declined, while the number in the informal sector rose.

The economic slowdown, low investment, and still low education level of the labor force resulted in unemployment rising from 6.1% in 2000 to 6.7%–7.0% in 2001.[9] By location, the total number of unemployed people in the cities was larger than in the villages. By gender, the total number of unemployed women was larger than unemployed men.

High open unemployment weakened the bargaining power of labor in wage negotiations. This was reflected in the relatively small rise of administered minimum provincial wages. In 2001, on average, minimum provincial wages rose by 33.7%, to Rp295,981/month (Chart 2.22), while the minimum living requirement cost, which is the basis for the calculation of minimum wages, increased by an average of 21.7%, to Rp323,798/month. Consequently, the minimum provincial wages determined by the government could only fulfill, on average, 91.4% of labors' minimum living requirement cost. Nevertheless, there are currently 10 provinces where the minimum provincial wages can meet the minimum living requirement cost, namely North Sumatra, DKI Jakarta, West Java, East Java, West Kalimantan, Central Kalimantan, South Kalimantan, South East Sulawesi, North Sulawesi, and East Nusa Tenggara.

The situation where many companies still have not fulfilled the requirement of the minimum provincial wages and other claims, such as, participation in labor employment insurance scheme (Jamsostek) and the religious holiday allowance, spurred labor disputes in the reporting year. Up to September 2001,[10] there had been 164 strikes involving 107,523 workers and resulting in 1,148,778 lost work-hours. Meanwhile, the number of workers laid off in 2001 was a bit lower than the previous year, 58,006 workers. The continuing high number of layoffs was due to deteriorating business conditions, particularly

8 Suara Pembaruan newspaper dated 13 July 2001.
9 Suara Pembaruan newspaper dated 13 July 2001.
10 Source: the Department of Labor and Transmigration, 2001.

businesses that were export-oriented. Textile and textile products, which is a labor-intensive industry, experienced the highest loss, partly because many of its products were aimed at the export market. The textile and textile products industry, which currently employs around 1.2 million workers, is likely to lay off between 10%–20% of its workers, if economic condition do not improve.[11]

11 Data from the Indonesian Textile Association as published in Suara Pembaharuan newspaper dated 23 October 2001.

box

Calculation of the Capital Stock Using the Perpetual Inventory Method

In economic textbooks, aggregate supply explains the relationship between prices and goods produced by companies in an economy.[1] In this context, macroeconomic analysis often differentiates between short-run and long-run aggregate supply. In the short run, aggregate supply can change when , among others, there is a change in production inputs, with existing available production capacity. In the long run, a change in aggregate supply-often called 'potential output'-occurs when existing economic capacity also changes. Empirically, estimates of aggregate supply for the long term (potential output) can use several approaches from simple ones, such as smoothing GDP data, up to a more complicated ones, which estimate an equation for an aggregate production function.

Considering the importance of potential output for analysis and projections of inflationary pressures, Bank Indonesia is currently estimating potential output using the production function approach, where one of the main variables is data on the capital stock.

In general, the capital stock is defined as the inventory of all types of capital goods in the economy (such as, buildings, machinery, transportation equipment, cattle, and other capital goods)[2] that make a sustainable contribution to the production process. In practice, data on the capital stock provide a picture of the position of capital goods, which is formed by a process of investment accumulation over a certain period of time. Within the 1968 SNA terminology, this investment is known as Gross Fixed Capital Formation (GFCF) or Formation of Gross Fixed Capital. Up to now, data on Formation of Gross Fixed Capital have been calculated and published periodically by the Central Statistical Agency.

Data on the capital stock is generally used: (1) to obtain a picture of net product (net value add) of the results of a production process, namely total production value minus depreciation (consumption of fixed capital); (2) to calculate wealth, which is acquired from the result of formation during a certain period; and (3) to calculate productivity and efficiency of an economy.

Basically, there are two approaches used to develop data on capital stock, namely the direct and indirect methods. The direct method comprises Direct Observation of Capital (DOC), a Fixed Asset Accounting Simulation Model (FAASM), and an Anchored FAASM. Direct calculation is performed by collecting data on the capital stock directly from the financial statements of companies and government administration. The DOC method is the most common direct method, due to more accurate data, asset life measurement, as well as time length of usage (discard patterns). However, in implementation, the direct methods require very high financing and large human resources in terms of quality as well as quantity.

1 N.Gregory Mankiw, Macroeconomics, 3rd edition, Worth Publishers, 1997, page 503

2 According to the concept of System of National Account (SNA) of 1968, capital goods do not include intangible assets

Meanwhile, the indirect capital stock calculation methods focus more on the utilization of secondary data. One popular indirect method is the Perpetual Inventory Method (PIM), where the capital stock is estimated using the available secondary data, namely data on Formation of Gross Fixed Capital. There are two requirements in order to use the PIM method to produce reliable data, namely the availability of accurate and detailed Formation of Gross Fixed Capital data and certain explicit assumptions, namely asset life, distribution pattern, and depreciation methods. In broad outlines, the calculation of capital stock using the PIM method is performed by cumulating capital investment (Formation of Gross Fixed Capital) over a certain period and netting out capital goods that have been used up (retired) and capital goods that have been depreciated during that period.

Several countries such Holland, Britain, Germany, Australia, and Canada have already had data on capital stock for a long time, although with different calculation methods. Meanwhile, in Indonesia, available information on the capital stock is still limited. Research into the capital stock in Indonesia includes Keuning (1988 and 1991), Central Statistical Agency (1995), and Timmer (1999).

In light of the importance of information on the capital stock, in 2000 Bank Indonesia undertook a preliminary review on the possibilities for collecting data on the capital stock for the manufacturing industry sector. From a number of alternatives for the calculation of the capital stock, the review concluded that the PIM method was the best method to be used in calculating the capital stock in all economic sectors. The main criteria for choosing the PIM method were, among others, cost efficiency and the available human resources. As a follow-up, in 2001, Bank Indonesia in cooperation with the Central Statistical Agency, estimated the capital stock based on the 'wealth' concept by using the PIM method.

The results of the calculation of the capital stock based on the 'wealth' concept by using 1993 constant prices are presented in two concepts, namely the Gross Capital Stock (GCS) and Net Capital Stock (NCS). The GCS figure is obtained after calculating a number of capital goods that are retired during a certain period without allowance for depreciation. The NCS estimates are obtained by calculating total capital goods after deducting their depreciation value.

Mathematically, the relation between NCS, GCS, and the size of GFCF can be formulated as follows :

$$NCS_i = NCS_{i-1} + GFCF_i - AdjD_i$$

$$GCS_i = GFCF_i - ret_i + GCS_{i-1}$$

$$\sum_{i=1}^{n} GFCF = GCS_n + \sum_{i=1}^{n} re$$

NCS	=	Net Capital Stock
GFCF	=	Gross Fixed Capital Formation
AdjD	=	Adjusted Depreciation
ret	=	Retirement
i	=	period of year
n	=	end of period of capital stock

Simulation of these capital stock data indicate that both measures of capital stock (GCS and NCS) always experienced positive growth. The GCS index grew from 103.3 in 1980 to 201.9 in 2000 (Chart 1).

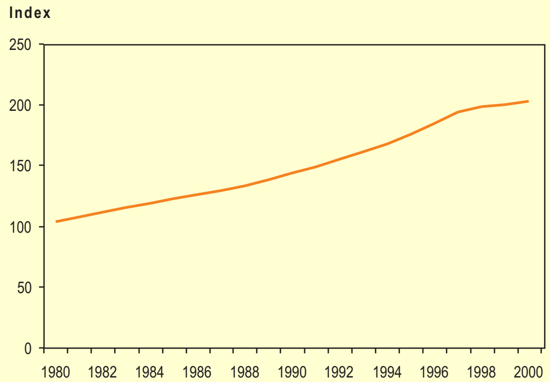

Chart 1
GCS Index Indonesia

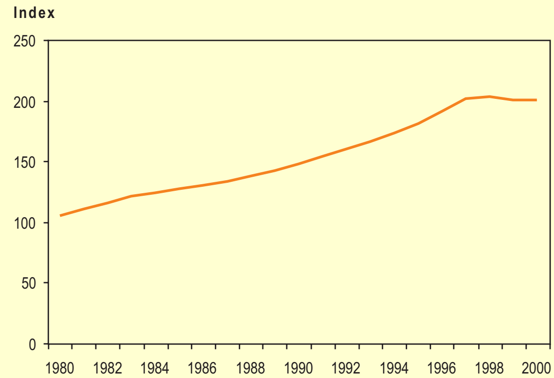

Chart 2
NCS Index Indonesia

During the same period, NCS index increased from 105.1 to 200.5 (Chart 2). The average annual growth of capital stock is almost the same for GCS as for NCS, namely 3.4%. The prolonged economic crisis since mid 1997 is reflected in a temporary decline in capital stock, which is marked by the slowing of NCS growth in 1998 to 0.8% and even its contraction for some time in 1999, of 1.2%.

Based on the shares of each type of capital stock, Indonesia's capital stock during the last 20 years period has been dominated by 3 big groups, namely construction, machinery and transportation. The share of construction, which was 60.0% in 1980 rose to 75.7% in 2000; the share of transportation dropped from 23.2% (1980) to only 4.0% (2000). The share of machinery is roughly unchanged, at around 15.9%.

chapter 3 THE EXCHANGE RATE

chapter 3

THE EXCHANGE RATE

During 2001, the rupiah exchange rate was generally under strong downward pressures, although it did appreciate sharply for a while at mid-year. Overall, it depreciated by around 17.7%, from an average of Rp8,438 in 2000 to Rp10,255 per dollar in 2001. These strong pressures were related to increasing country risk in line with rising uncertainty concerning domestic socio-political conditions. In addition, despite some progress, several macro and micro economic fundamentals still faced a number of problems (Chart 3.1). As a result of the pressures for depreciation, the real exchange rate became more undervalued, which put considerable pressure on inflation. In coping with this development, Bank Indonesia has made various efforts to optimize its use of all available policy instruments. In addition, implementation of several economic restructuring programs continued but did not fully met the expectations of all parties. Such efforts will be continued and improved in the expectation that they will improve economic fundamentals, reduce the foreign currency demand-supply gap and improve market confidence. Moreover, these various efforts will need to be complemented by conducive socio-political conditions, which are an inseparable element of strengthening public confidence in the economic recovery process.

Various risk factors, which had been expected to improve in the middle of the reporting year, turned out to be worse than anticipated. Up to mid-2001, uncertainty over the domestic socio-political situation increased, marked by political turbulence, several incidents of social unrest and the threat of national disintegration from several regions. These developments resulted in deteriorating market confidence and persistent negative sentiment towards the rupiah. Following the transition of national leadership, the domestic political situation was on an improving trend and there was rising optimism regarding sustainability of the economic recovery. This was reflected in a recovery of market confidence, which was marked by a steep appreciation of the rupiah exchange rate. However, that appreciation did not last long. Market confidence slipped again, particularly due to the condition of macro and micro economic fundamentals, which still faced a number of problems.

On the macro-fundamental side, and despite some significant progress, several economic restructuring programs were moving slowly. This could be particularly seen in the debt and corporate restructurings, privatization and divestments, and efforts to revitalize the banking and corporate sector. Slow improvements in these areas stemmed from rising complexity of the problems; weak institutional support; legal uncertainty; and security concerns. In addition, world economic conditions were unfavorable for the external sector.

These conditions limited foreign currency inflows, causing a shortage of foreign currency in the market. By contrast, demand for foreign currency

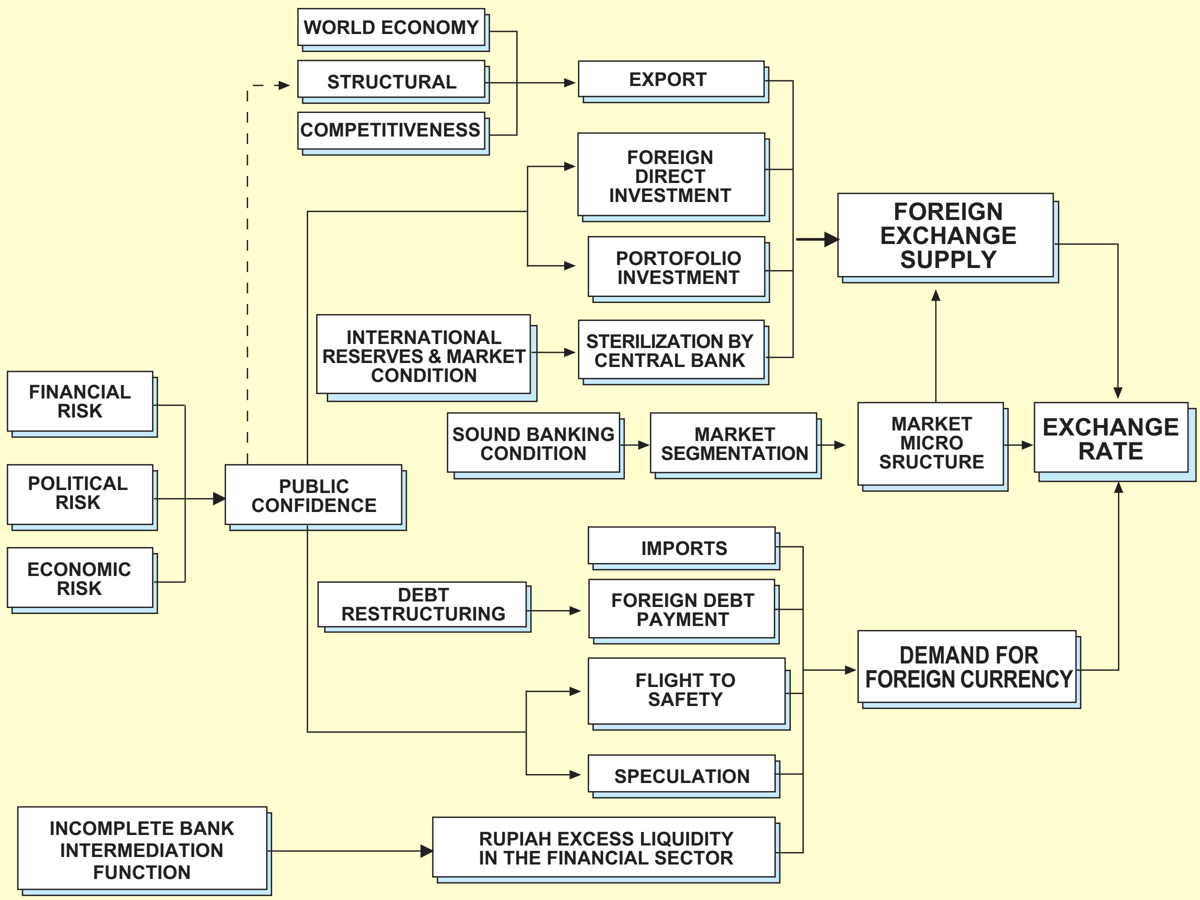

Diagram 3.1
Problems of Exchange Rate in 2001

remained high, both for import needs and repayment of private sector foreign debts. High demand for foreign currency was aggravated by excess rupiah liquidity in the financial sector, particularly because bank intermediation had not fully recovered yet .

On the micro-fundamental side, various basic weaknesses inherent in domestic financial markets colored Indonesia's economy. This was reflected in continuing financial market segmentation and in an underdeveloped hedging market. Market segmentation weakened the pricing mechanism; [1] the price for foreign currency did not represent the strength of market players as a whole, but reflected only the strength of several players that held majority market shares.

INFLUENCING FACTORS

Development of the rupiah exchange rate during the reporting year was influenced by various

1 An efficient market price formation mechanism operates in conditions where prices reflect the strength of market players as a whole, instead of representing only a few market players

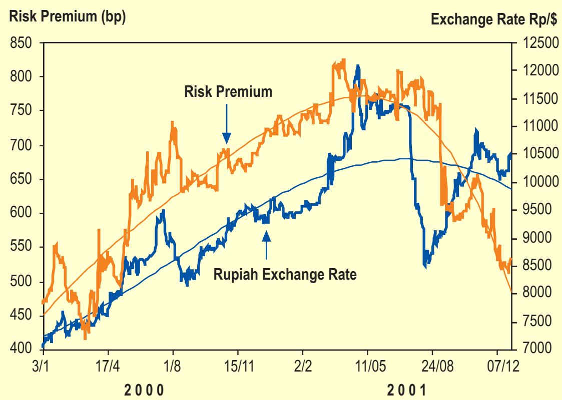

Chart 3.1
Trend of Rupiah Exchange Rates and Risk Premium

uncertainties in the socio-political arena and in the economic and financial fields. Since the economic crisis broke, exchange rate fluctuations have been persistently colored by socio-political uncertainty, which may have started a vicious circle of economic problems. The close relationship between socio-political uncertainty and exchange rate fluctuations were indicated by co-movement between risk premiums[2] and the exchange rate over the last several years (Chart 3.1).

Socio-political uncertainty can cause exchange rate fluctuations both directly and indirectly. The direct effect is the immediate reaction in the form of foreign currency buying (or selling) due to a change in market players' sentiment after socio-political incidents. Indirectly, socio-political uncertainty influences exchange rates through changes in (domestic and international) public confidence that partly determine capital flows, and these flows have an impact on foreign currency demand and supply.

During 2001, market sentiment was greatly influenced by domestic socio-political uncertainties, which tended to rise despite some improvement in the second half of the year (Chart 3.2). During the first half of 2001, market confidence continually deteriorated, due to rising political conflicts, several incidents of social unrest and the threat of national disintegration from several regions. Consequently, the rupiah was subject to persistent pressures for depreciation. After the transition of national leadership in July 2001, market confidence tended to improve, spurred by the expectation that an end to political crisis might provide a foundation for revival of the economy from prolonged crisis. With improved market confidence, the rupiah appreciated quite sharply. However, towards the end of the reporting year, market confidence worsened again and the rupiah came under additional pressure following the World Trade Center (WTC) tragedy on 11 September 2001. This tragedy raised the temperature of international politics, which heightened feelings of insecurity among foreign investors. The tragedy caused international investors to be more cautious due to rising global risks, which put pressure on the majority of regional currencies, including the rupiah.

In addition to socio-political uncertainty, exchange rate fluctuations in 2001 were also due to continuing low public confidence in micro and macro economic fundamentals. Low public confidence resulted particularly from various economic restructuring programs that still faced a number of constraints. Economic problems were becoming increasingly complex; there was weak support from the institutional system; the legal system remained unpredictable; and security concerns increased.

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2 Risk premiums are defined here as the difference in yield between Indonesia's Yankee Bond and the benchmark US Treasury Note, where both are 10 years tenor, with maturity in 2006

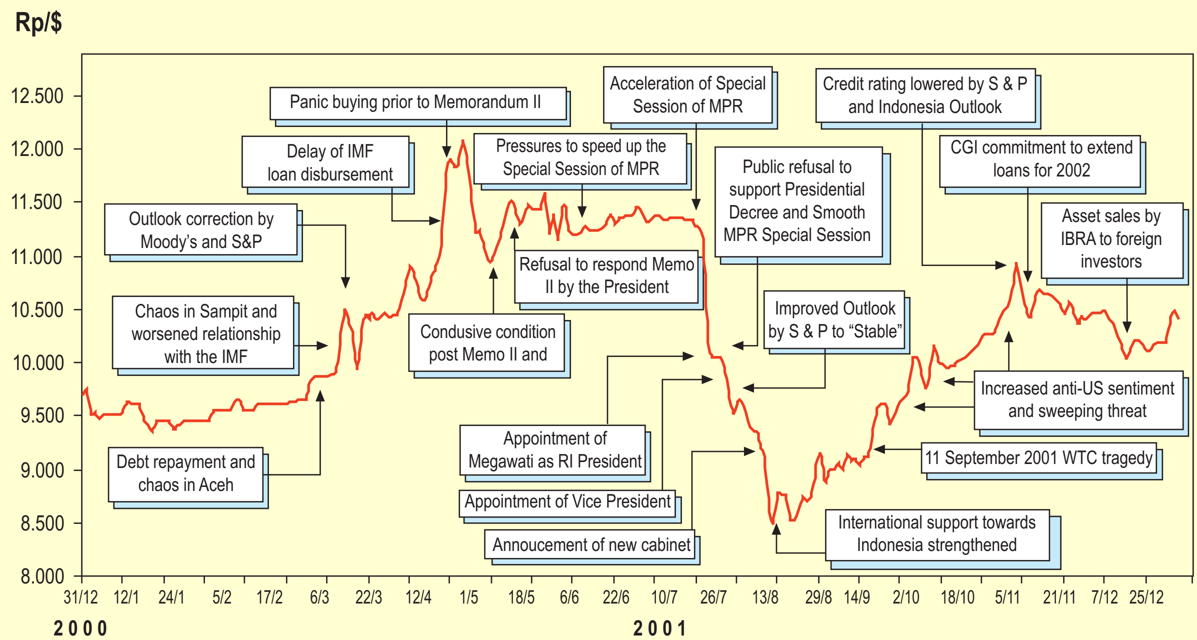


Chart 3.2
Rupiah Exchange Rate Developments and Sentiment Factors

Public confidence was also influenced by perceptions that the government's financial burden was becoming heavier; the processes of private sector debt and corporate restructuring, privatization and divestment were moving slowly; bank intermediation was not operating normally; and implementation of regional autonomy had encountered a number of problems. In addition, the great sensitivity of several economic problems to exchange rate and interest rate fluctuations caused the circle of economic problems to widen, which reduced public confidence still more.

The burden of government spending, particularly to finance very large subsidies and domestic bond interest payments, was one of the areas considered to be very susceptible to interest rate and exchange rate fluctuations. In addition, repayment of government foreign debts was very much dependent on the success of negotiations with the donor institutions. Outcomes in this regard had an appreciable influence on market expectations and were often used as a reference point by a number of international debt rating institutions in determining Indonesia's sovereign credit rating. Weakening of public confidence in fiscal sustainability was also due to slow privatization of several state-owned enterprises and sales of assets under the management of the Indonesian Bank Restructuring Agency (IBRA). Both were expected to be important sources of government financial revenue.

Continuing weak economic fundamentals was one of the main factors influencing the exchange rate by creating an imbalance between demand and supply in the foreign currency market. At one side, foreign currency demand during the reporting year remained high, particularly for the real needs of the economy, such as the financing of imports and repayment of foreign debts. In addition, speculative and asset safeguarding (flight to safety) activities driven by socio-political uncertainty remained a source of foreign currency demand. On the other hand, foreign currency supply remained limited due to private capital inflows being hindered by unfavorable domestic and external conditions.

On the micro side, deteriorating market confidence in the rupiah was often reflected in very sharp exchange rate fluctuations. This was due to domestic foreign currency markets not being liquid and sufficiently deep, which was particularly the result of various basic weaknesses inherent in the domestic market's structure *(Box : Understanding Rupiah Exchange Rate Dynamics Through the Structural Micro-Market Model Approach)*. Micro market structure, in both the foreign currency and domestic money markets, was still marked by segmentation arising from differences in financial risks.

In segmented market conditions, several banks with dominant market shares had excess foreign currency liquidity due to limited secure domestic placement opportunities, either in the form of credits to business or in the domestic foreign currency inter-bank money market. This was mainly due to poor domestic business prospects and limited credit lines to local banks. The limited credit lines stemmed from continued low confidence in local banks, the majority of which had weak balance sheets and were still susceptible to systemic risk, despite the government guarantee program.

As a result of this high domestic placement risk, there was a tendency towards rising placements in offshore money markets in short-term instruments, particularly by a number of big banks with access to offshore markets. Financing for those off-shore placements came in part from rupiah funds mobilized in the country, which put pressure on the exchange rate when the rupiah was converted to foreign currency. In addition, the conversion from rupiah to foreign currency also occurred through swap transactions by utilizing the spread between the implied swap premium rate[3] and the rupiah interest rate.

The weak structure of the local foreign currency market was also indicated by an under-developed hedging market, which limited opportunities for reducing the risk of exchange rate fluctuations. Hedging instruments, such as swap and forward transactions, are only available for relatively short maturities. Meanwhile, the supply of hedging funds for medium- to long-term transactions, which are actually very much needed to provide more certainty in real sector activity, are not available in sufficient amounts. As a result, future foreign currency needs are often met by early purchases in the spot market.

Rising foreign currency demand in the spot market creates depreciation pressures on the rupiah, particularly when foreign currency buying by big market players creates a chain reaction (bandwagon effect) in the market. Routine entrance of these big players into the market often spurs early foreign currency purchases by a number of banks. These may be followed by other market players (herd behavior),

3 The implied swap premium rate is the rate of swap premium plus the interest rate on foreign currency savings.

including those that actually need the foreign currency sometime in the future. It becomes easier for depreciation pressures to emerge, particularly when there is excess rupiah liquidity in the money market. In condition like this, rupiah liquidity mainly circulates within the financial sector and may be used for short-term profit in the foreign currency market and the money market, rather than being channeled to the productive sector.

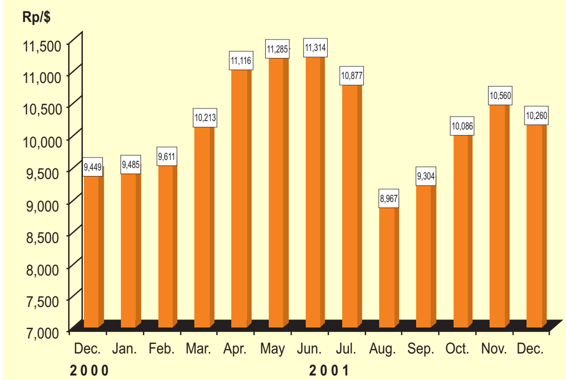


Chart 3.3
Daily Average Rupiah Exchange Rate

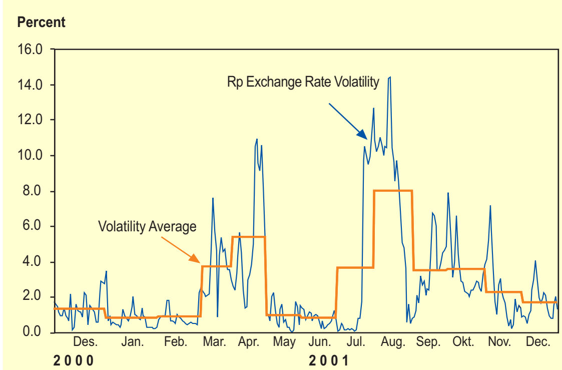


Chart 3.4
Volatility of the Rupiah Exchange Rate

RUPIAH EXCHANGE RATE DEVELOPMENTS

During 2001, the rupiah exchange rate weakened by 725 points or 7.0% against the dollar, from Rp9,675 at the end of 2000 to Rp10,400 per dollar at the end of 2001. On an average daily basis, the depreciation was quite sharp; the rupiah weakened by 1,817 points or 17.7%, from Rp8,438 in 2000 to Rp10,255 per dollar in 2001 (Chart 3.3). That depreciation was accompanied by high volatility.[4] On an average daily basis, exchange rate volatility rose from 2.2% in 2000 to 2.8% in 2001, and peaked at 14.4% for a while in mid-August 2001 (Chart 3.4).

Exchange rate developments in 2001 can be viewed in four phases. In phase one, the rupiah showed a weakening trend in the first four months in 2001, reaching its lowest value of Rp12,090, before closing at the level of Rp11,600 at the end of April 2001. During the second phase, the rupiah exchange rate was relatively stable around Rp11,200 until the close of the special session of the People's Consultative Assembly. In the third phase, which began after the special session of the People's Consultative Assembly on 21 July 2001, the rupiah exchange rate strengthened sharply until reaching a peak value of Rp8,485 per dollar on 14 August 2001. In the fourth phase, the rupiah exchange rate weakened again, passing through the psychological barrier of Rp10,000.

In the first phase, depreciation pressure on the rupiah exchange rate was mainly influenced by market sentiment, spurred by concerns over political and security conditions that accompanied the impeachment process—through memorandums I and II—of the national leadership at that time. These uncertain conditions created expectations of a future weakening of the exchange rate, which immediately triggered dollar

4 Daily exchange rate deviation from a 22-day moving average (1 calendar month)

buying, causing the rupiah to weaken quite sharply. In coping with exchange rate fluctuations, Bank Indonesia made efforts to absorb excess liquidity from the money market through open market operations (OMOs), supported by sterilization in the foreign currency market. This policy continued to be implemented during the reporting year, consistently and at a measured pace. In addition, on 12 January 2001, Bank Indonesia issued regulation number 3/3/2001, which aimed to limit rupiah transactions by non-residents with the potential to be used for speculation *(Box : Limitation on Rupiah Transactions and Foreign Currency Credit Extensions by Banks).*

In the second phase, the domestic political situation was even more colored by deteriorating confidence in the national leadership. This, in turn, strengthened the support for the need to hold the special session of the People's Consultative Assembly, which was expected to produce new national leadership. In light of these developments, on 21 May 2001 the international rating institution, Standard & Poor's (S&P), reduced Indonesia's sovereign credit rating from B- to CCC+. Further, in the People's Representatives' plenary meeting on 30 May 2001, the People's Consultative Assembly was finally asked to hold the special session. Despite this development, few market players took a position because the exchange rate was very much undervalued. Instead, they adopted a wait and see attitude towards political developments during the approach of the special session of the People's Consultative Assembly, which caused the exchange rate to be relatively stable around Rp11,200.

In the third phase, optimism towards the political situation improved in line with the success of the special session of the People's Consultative Assembly in electing a new national leadership. This condition was expected to be the new foundation for Indonesia to escape from prolonged economic crisis, which would prompt a sharp appreciation of the rupiah. During this period, support for the new government from within the country and abroad continued to grow, prompting the rupiah exchange rate to strengthen further; it reached its highest value (Rp8,485 per dollar) on 14 August 2001.

In the fourth phase, the rupiah weakened again, including breaking through the psychological barrier of Rp10,000, through the end of 2001. This depreciation pressure was partly due to foreign currency buying by corporations to take advantage of the strong rupiah after the transition of national leadership. At the same time, market confidence started to deteriorate again as the result of rising uncertainty over several economic restructuring programs. Although the political situation tended to improve, market players had not seen signals of improvement on the side of economic fundamentals.

Market confidence was particularly influenced by the perception over the large size of government debts (both domestic and offshore) which were considered to be a serious threat to fiscal sustainability. The seriousness of the government's financial condition was confirmed by S&P on 2 November 2001, by a further downgrading of Indonesia's sovereign credit rating from CCC+ to CCC with negative outlook. This meant that there was a possibility that Indonesia's sovereign credit rating would be further reduced in the coming period. The government's plan to request foreign debt rescheduling through the Paris Club III forum became the main reason for S&P to reduce

Indonesia's sovereign credit rating. S&P even threatened to again reduce Indonesia's sovereign credit rating to their lowest level, namely Selected Default (SD), if interest on Indonesia's Yankee Bonds had to be rescheduled as a consequence of the implementation of the comparability of treatment principle in the Paris Club. Market confidence worsened further due to delays in the release of IMF loans in the amount of $400 million. These funds were finally released in August 2001, having been delayed since December 2000.

Meanwhile, the international political crisis following the terrorist incident in the United States on 11 September 2001, further impacted on the domestic situation due to strong reactions by insecure foreign investors in the country. The various incidents heightened Indonesia's country risk as confirmed by the Hong Kong-based Political & Economic Risk Consultancy (PERC). Based on the results of PERC's review, Indonesia's country risk rose from 7.3 to 7.6. However, near the end of the year, the rupiah strengthened again for a short while, due to foreign currency supply from IBRA and rising needs for rupiah in advance of several religious holidays that nearly converged in December 2001.

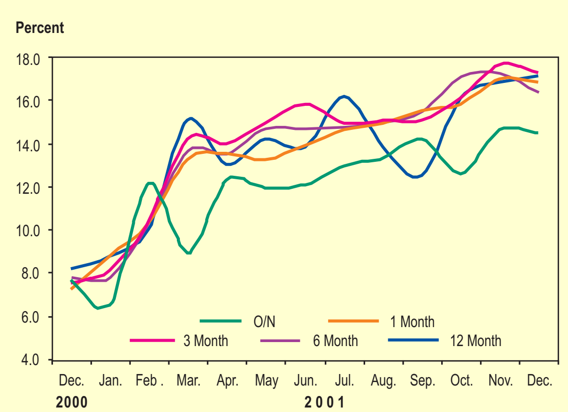


Chart 3.5
Development in Swap Premium

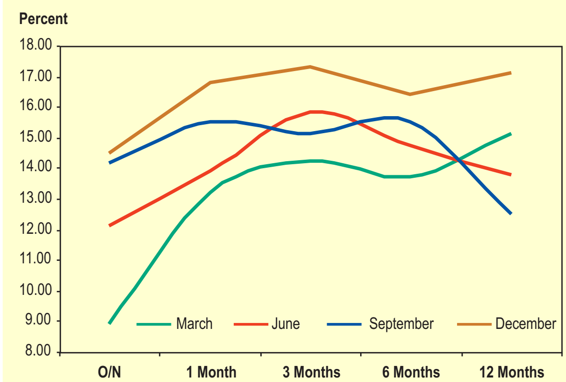


Chart 3.6
Swap Yield Curve

The rise in Indonesian country risk was also marked by sharply higher average swap premiums for all terms and the risk premium (Charts 3.5 and 3.6). The average swap premium for overnight, 1 month, 3 month, 6 month, and 12 month terms soared from, respectively, 3.86%, 4.97%, 5.02%, 4.89%, and 4.95% in 2000 to 11.98%, 13.88%, 14.36%, 14.20%, and 13.85% in 2001. Within the same period, the average risk premium rate rose from 603 bp to 712 bp (Chart 3.1).

In line with soaring swap premiums, covered interest rate parity[5] (for 1-month term) worsened. During almost the entire review period, the covered interest rate parity was negative. On a point-to-point basis, covered interest rate parity worsened from 0.55% at the end of 2000 to –0.83% at the end of 2001 (Chart 3.7). Although the nominal interest rate differential widened as the result of rising domestic nominal interest rates and declining offshore interest

5 Covered interest rate parity JIBOR (1 month) – SIBOR (1 month) – Premi Swap (1 month)

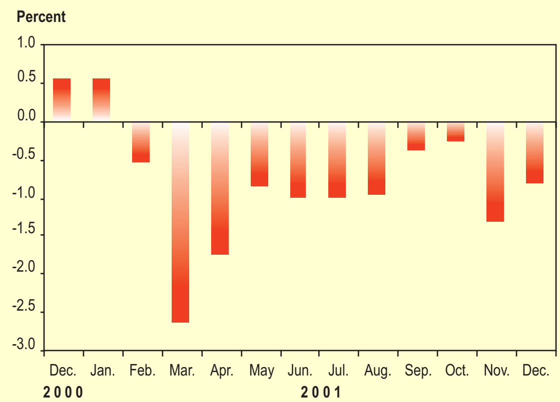


Chart 3.7
Covered Interest Rate Parity

rates, it was the steep rise in swap premiums that caused covered interest rates to be consistently negative. This is indicative of the continuing high risks, which could not be covered by the difference in nominal interest rates, and which reduced investors' willingness to hold rupiah-denominated assets.

The weakening trend of regional currencies versus the dollar in 2001 had a contagion effect, which also put the rupiah under further pressure. The slowdown in the world economy (especially the US), has

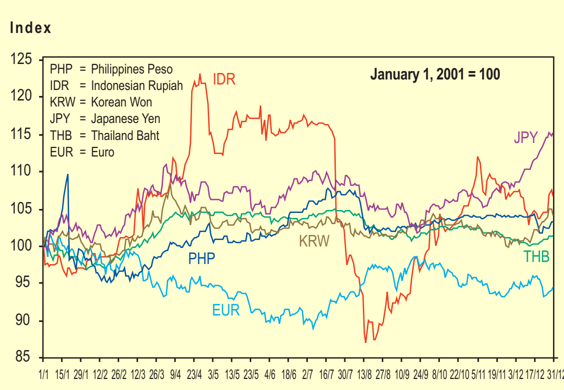


Chart 3.8
Development in Exchange Rate Index of Several Currencies

caused declining demand for the exports of several Asian countries. This has added to the pressure on the currencies of those countries (Chart 3.8).

FOREIGN CURRENCY SUPPLY AND DEMAND

The various factors influencing the rupiah exchange rate during 2001, as described above, can also be viewed from the equilibrium condition of demand and supply in the foreign currency market. The depreciating trend of the rupiah, and its high volatility, reflected strong foreign currency demand that was not matched by supply in the foreign currency market. The existence of this gap caused the rupiah to be very susceptible to changes in market sentiment.

On the supply side, potential supply in the foreign currency market would normally arise from export revenues, foreign capital inflows in the forms of direct foreign and portfolio investment, drawdowns of offshore loans, and foreign currency intervention by the central bank. During 2001, most of these sources were subject to various limitations, which hampered the supply of foreign currency to the market. The limited supply was particularly prompted by unsettled domestic conditions, a weakening world economy, and several structural problems that hampered foreign currency flows into the country. For its part, the central bank's role as foreign currency supplier to the market was very much dependent on the availability of foreign currency reserves.

Fundamentally, depreciation pressures on the rupiah reflected the external sector's performance, as indicated by a narrowing current account surplus and a widening of the capital account deficit (see Chapter 6 - Balance of Payments). The current account surplus in 2001 was only $5.0 billion or 3.4%

of GDP, far lower than 2000's surplus of $8.0 billion or 5.3% of GDP. The narrower current account surplus was mainly caused by weaker exports and the continuing large deficit on services. During 2001, Indonesia's exports trended downward in line with the sluggish world economic conditions, and magnified by the WTC tragedy in the United States. Exports in 2001 were $58.7 billion, down from $65.4 billion in 2000. The services deficit was dominated by interest payments on foreign debts. The current account surplus in real terms (cash basis) could be much smaller if not all of the export earnings were transfered into domestic economy.

The exports performace in 2001 was mainly affected by the sluggish world economy despite the rupiah depreciation, in both real or nominal term. The real depreciation happened as the nominal depreciation exceeding domestic inflation. The real effective exchange rate (REER) declined from 69.6 in 2000 to 67.8 in 2001 (Chart 3.9). The bilateral real exchange rate index (BRER) also declined in 2001, from 54.8 in 2000 to 49.3, much more than the BRER indexes of a number of other Asian countries such as China, South Korea, Singapore, Malaysia, and Thailand, although those countries also experienced real depreciations in 2001 (Chart 3.10).

During the same period, the deficit on capital account is estimated to have reached $8.9 billion, compared with $6.8 billion in 2000. This was due to government capital flows, which shifted into deficit in 2001, while private capital flows remained in substantial deficit. The continuing wide deficit on private capital was due to limited foreign currency gross inflows and to continuing gross capital outflows. Weak inflows (both direct foreign investment and purchases of marketable securities in the money and capital markets) were mainly caused by the uncertain domestic situation. This was related to continuing weak support for business security, legal uncertainty and the socio-political situation. Meanwhile, continuing capital outflows mainly stemmed from ongoing large payments on private foreign debts and substantial portfolio placements into offshore money markets.

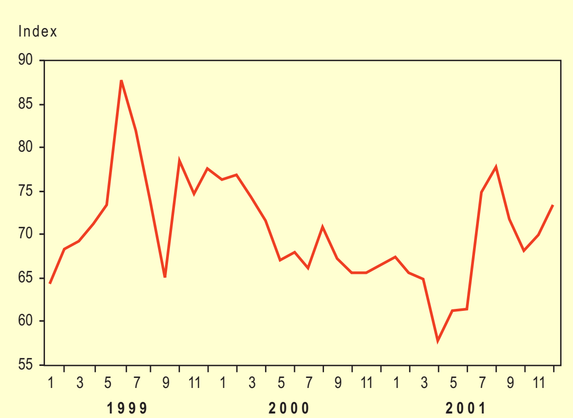


Chart 3.9
Real Effective Exchange Rate

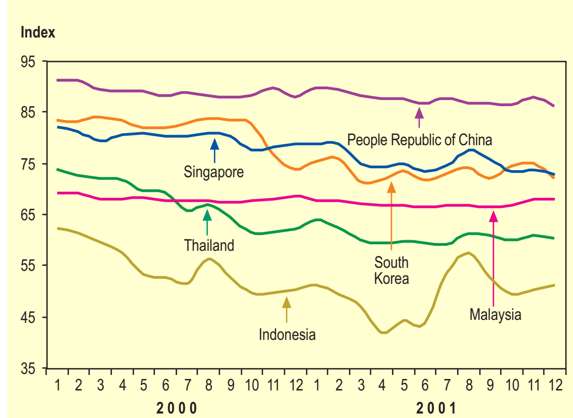


Chart 3.10
Bilateral Real Exchange Rate

The rise in the portfolio placements into off-shore money markets was mainly the result of high risks within Indonesia. These high risks limited domestic supplies of foreign currency into the interbank money market.

Overall, Indonesia's balance of payments in 2001 was in a deficit of $1.4 billion, having recorded surpluses during the previous three years. This reflected limited sources of foreign currency, including for the domestic money market.

The situation on **the demand side** of this market contrasted sharply with supply side factors. Amid short supply of foreign currency in the market, demand remained strong and tended to rise due to genuine demand, speculative motives and actions to safeguard assets (flight to quality). In general, this was spurred by deteriorating market sentiment as the result of various risks and uncertainties that were on the rise. In practice, it is still difficult to differentiate among those three demand motives, considering they often occurred simultaneously. However, of the three motives, it was genuine demand that played the dominant role, particularly probably for import financing and for servicing off-shore debt.

Foreign currency demand for imports remained high, although smaller than the previous year. Aside from imports, foreign currency demand was strong for servicing of foreign debt, particularly by the private sector. Large foreign debt repayments were reflected in a decline in outstanding foreign debt during the reporting year (see Chapter 6 - Balance of Payments).

Strong foreign currency purchases by corporations for imports and private foreign debt repayments amid short supply of foreign currency put downward pressure on the rupiah. In practice, the timing of foreign currency purchases by corporations was not always in line with the schedules for foreign currency needs for future imports or with the repayment schedules of foreign debts. It was also influenced by expectations of future directions of the exchange rate. Expectations of a weaker exchange rate often prompted corporates to buy early in the spot foreign market, rather than to hedge their transactions. This was due to the underdeveloped condition of the swap market, particularly for medium- and long-term maturities. In addition, foreign currency demand by corporations-particularly among big players-often spurred speculative transactions by other market players (herd behavior).

The size of foreign currency demand that was purely for speculative motives is difficult to measure. However, speculative demand often emerged when market sentiment weakened in reaction to heightened uncertainty stemming from economic and non-economic factors.

INTERBANK FOREIGN CURRENCY TRANSACTIONS

Rising rupiah exchange rate volatility was in line with a change in the pattern in the domestic foreign currency market. Cumulatively, interbank foreign currency transactions[6] declined by 4.0% from $298.0 billion in 2000 to $286.1 billion in 2001 (Table 3.1). By type of transaction, swaps transactions still dominated the composition of interbank foreign currency transactions during 2001 (Chart 3.11). However, during the same period, swaps transactions declined by 18.3% from $187.6 billion to $153.2 billion, while

6 Specifically for dollar-rupiah transactions

Table 3.1
Dollar-Rupiah Interbank Foreign Exchange Transaction

Volume	2000	2001
	Million Dollar	
Spot	109,045.6	128,372.6
Forward	1,385.9	4,533.0
Swap	187,596.8	153,225.1
Total Volume	**298,028.3**	**286,130.7**

spot transactions actually rose 17.8% from $109.0 billion to $128.4 billion. Viewed by market players, foreign banks still dominated the interbank foreign currency market with quite large transaction volumes.

This shift from the swap to the spot market suggested more speculative behavioral patterns. This is perhaps due to the scarcity of swap funds, particularly for medium- and long-terms (3 months and above). Also, hedging has become more costly as indicated by the high level of swap premiums. The scarcity of hedging instruments was mainly caused by the underdeveloped local derivatives market.

Of the total of $286.1 billion in interbank foreign currency transactions during 2001, $160.3 billion constituted dollar purchases and $125.8 billion

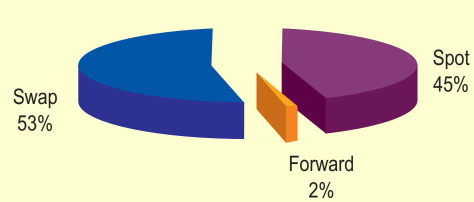


Chart 3.11
Composition of Foreign Exchange Transaction

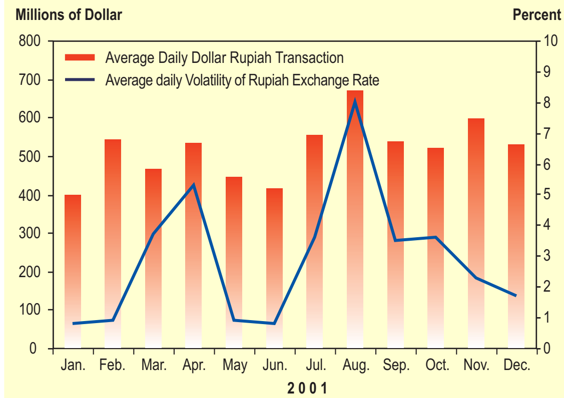


Chart 3.12
Spot Transactions and Volatility of Exchange Rate

constituted dollar sales, which implies a net overbought position of $34.5 billion in interbank foreign currency transactions. In other words, during the review period, banks tended to be in a long dollar position. The net overbought position mainly originated in transactions with counterparts abroad, which were net overbought; transactions with domestic counterparts were net oversold. Viewed by type of transaction, the net overbought position mainly originated in swap transactions.

The volume of interbank foreign currency transactions had a pattern that was similar to the exchange rate's volatility (Chart 3.12). The largest transaction volume occurred in August 2001 when the daily average reached $668 million. This high transaction volume was accompanied by high rupiah exchange rate volatility, with daily average reaching 8.0%, the highest level during the review period.

POLICIES

To cope with large fluctuations in the rupiah exchange rate, as mentioned earlier, during the reporting year Bank Indonesia adopted several monetary policy measures by optimizing all available instruments. These efforts were strengthened by enhancing several regulations; by supervising big player banks in the foreign currency market; and by monitoring foreign currency transactions. It is recognized that the various measures adopted by Bank Indonesia have not had optimum results, owing to the large influence of non-economic factors and to the complexity of macro and micro economic problems influencing the exchange rate (which were not fully under Bank Indonesia's control).

In the framework of absorbing rupiah excess liquidity (which has the potential to bring pressure on the rupiah exchange rate) in 2001, Bank Indonesia implemented monetary policy through open market operations (OMOs), supported by foreign currency sterilization. The foreign currency sterilization was also aimed at adding liquidity to the domestic foreign currency market. Amid strong demand for foreign currency—which was often spurred by socio-political turbulence—this sterilization was successful in restraining the rupiah exchange rate from sharper depreciation.

Furthermore, this sterilization policy continued to be implemented consistently and at a measured pace. This policy was adopted when implementation was tuned to market conditions and sufficient foreign currency reserves were maintained at Bank Indonesia. Consistency was very important in the implementation of this policy in order to send signals to the public concerning Bank Indonesia's commitment to maintaining exchange rate stability.

On 12 January 2001, Bank Indonesia has also issued regulation number 3/3/2001, which stipulates limitations on rupiah transactions by non-residents.[7] This policy was issued against the backdrop of non-residents' behavior that tended to use the rupiah as a tool for speculation, often creating exchange rate fluctuations. In implementation, this policy proved capable of limiting non-residents' room for undertaking rupiah transactions that were not based on real economic activities.

As was the case in previous years, Bank Indonesia continued to supervise banks that were directly and indirectly active in the foreign currency market. Direct supervision of banks-who are the main players in the foreign currency market-is very important to ensure compliance with prudential regulations, including in foreign currency transactions. Meanwhile, indirect supervision was mainly implemented by monitoring of financial reports routinely submitted by foreign currency banks and of foreign currency transactions through data from the Money Market Information Center.

Those various policy measures would have been more effective if they were supported by conducive macroeconomic fundamentals and socio-political conditions. These would re-build market confidence and reduce the demand-supply gap in the foreign currency market. Although overall economic restructuring progressed slowly, some notable progress was recorded, particularly government debt restructuring and several restructuring programs within the framework of the agreement with the IMF.

In the future, monetary policy will continue to be implemented in a consistent and measured way in order to maintain price stability and to avoid potential pressure on the exchange rate. Meanwhile, direct

7 See Box : Limitations on Rupiah Transactions and Foreign Currency Credit Extensions by Bank.

and indirect supervision of banks' foreign currency transactions will continue to be optimized. In line with measures to rehabilitate the banking sector, efforts will continue to be adopted to improve the micro structure of the foreign currency market. These include reducing market segmentation to create a more liquid and efficient foreign currency market. In this regard, in order to produce credible and realistic policies, various reviews and research will continue to be undertaken. Those efforts will be adopted, among others, through coordination with the government and routine communication with the banks in order to know the actual conditions in the foreign currency market. Research and reviews will be particularly aimed at reducing the demand-supply gap in the foreign currency market and at examining basic weaknesses in the banking system and the foreign currency market.

Meanwhile, to reduce the foreign currency demand-supply gap while developing market confidence, key economic restructuring programs (such as, debt and corporate restructurings, privatization and divestments, and revitalization of business and the banking sector) will be continued. However, these efforts would be more effective if they were supported by stable and conducive socio-political conditions. In addition, efforts to enhance legal assurance and business security would assist with the maintenance of exchange rate stability.

box

Understanding Rupiah Exchange Rate Dynamics Through the Structural Micro-Market Model Approach[1]

Since the freely floating exchange rate system was adopted in mid-1997, the rupiah exchange rate has often experienced very wide fluctuations. These fluctuations have even been larger than those of other countries, especially major world currencies such as the euro and Japanese yen, which are traded actively and speculatively on a global scale. It cannot be denied that negative sentiment towards various uncertainties in Indonesia was the main factor that spurred the start of rupiah exchange rate fluctuations. However, it is suspected that these fluctuations would be smaller, if the rupiah were traded in a more liquid and efficient foreign currency market.

A financial market can be called liquid and efficient when the buy-sell (bid-offer) spread, which basically represents the cost of transacting efficiently, is relatively thin. With a thin spread, very large transactions can be executed quickly with minimal impact on price fluctuations. In liquid market conditions, exchange rate sensitivity towards changes in the volume of transactions is relatively small, and will not create excessive changes in the exchange rate (Upper, 2000).

As mentioned, the cost of the foreign currency transaction is implicitly reflected in the buy-sell spread. The larger the spread, the more expensive the cost for transacting in the market. By contrast, the business principle for market players, particularly speculators, is the following: when the cost rises as a result of a wider spread, market players require larger swings in the exchange rate to make a speculative profit (Diagram 1).

Exchange rate swings will be larger when information does not disseminate evenly in the market (or information asymmetry occurs), and this is generally influenced by the microstructure of the market. Consequently, there is a close interrelationship between market microstructure, spreads, transaction volumes, and exchange rate volatility. Several market microstructure models review this interrelation, for example, "the mixture distribution hypothesis" model (Tauchen and Pitt, 1993).

The relationship between volatility, volume, and spread in the foreign currency rupiah market has

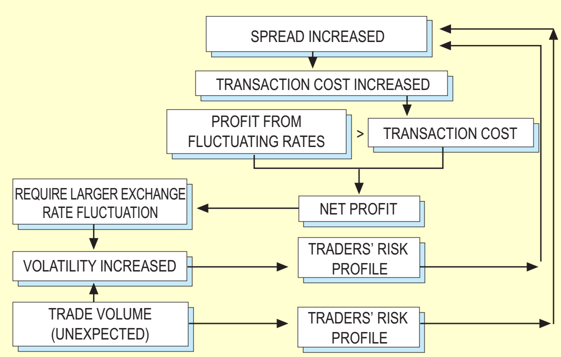


Diagram 1

1 Studies on Exchange Rate Dynamics through Information Asymetric Model and Survey, Directorate of Economic Research and Monetary Policy, Bank Indonesia 2001.

been estimated using "the mixture distribution hypothesis" (MDH) model, using data from January 1998 through May 2001. In this model, decomposition was performed between the transaction volume that can be expected and the transaction volume that cannot be expected, according to the different impact each has on the spread (Cornell, 1978). Expected volume is estimated using the ARMA (Auto Regressive Moving Average) approach. The spread is assumed to be a declining function of volume because economies of scale result in a more efficient trading process and heightened competition among traders. Consequently, the expected volume is assumed to have a negative correlation with the spread (Easley O'Hara, 1992). By contrast, the unexpected volume or a change of the unexpected volume reflects contemporaneous volatility through the MDH model, which implies a positive relationship with the spread. Meanwhile, volatility is estimated using the GARCH (General Autoregressive Conditional Heteroscedasticity) methodology.

In the rupiah-foreign exchange market, the change in unexpected volume has a positive correlation with volatility. A rise in unexpected volume by 1.0% will result in 0.3% rise in volatility. The high sensitivity of volatility towards unexpected volume shows that the foreign currency market in Indonesia is very shallow. Volatility is also significantly influenced by the spread. A rise in the spread of 1.0% will result in a 0.2% rise in volatility. The result of this estimation indicates that as the spread becomes wider or the foreign currency market becomes more illiquid, exchange rate volatility rises. As the spread widens, market players with speculative motives require larger exchange rate changes—up or down—in order to obtain profit and to cover the cost created by the wider spread.

A comparison of spread ratios towards midpoint exchange rates of several Asian countries from January 1998 to May 2001 shows that the transaction cost of rupiah trading is much higher than trading in other currencies, such as the Thai baht and the Philippines peso. This paints a picture of a rupiah exchange rate that is being traded in illiquid market conditions, and therefore fluctuates easily and very sharply. The large spread is particularly influenced by an inefficient foreign currency market that is segmented and plagued by uncertainty and persistently depressed sentiment. When market players become more uncertain as to the future direction of the exchange rate, they tend to become more risk-averse and widen the spread. This is seen from the significant influence of volatility on spread; a 1.0% rise in volatility causes the spread to widen by 0.06%.

To cope with these conditions, several structural measures would be helpful to improve the rupiah foreign exchange market so that a liquid and efficient market can be created. These include reducing market segmentation (so that the price formation is representative of all players' market strength) and raising foreign currency supply to increase market depth. In addition, conducive local conditions are needed to reduce various uncertainties and risks. Reducing uncertainties could improve market price formation, by narrowing of the buy-sell spread. These means would boost the efficiency of the foreign currency market and avoid excessive fluctuations.

box

Limitations On Rupiah Transactions and Foreign Currency Credit Extensions By Banks

As is well-known, the rupiah exchange rate has generally been under severe pressure since mid-1997, accompanied by wide fluctuations. Available data indicate that the pressures on the rupiah exchange rate were partly due to non-residents' use of rupiah for speculative activities in off-shore money markets. This was reflected in rising balances of rupiah vostro accounts owned by non-residents in domestic banks when depreciation pressures were increasing and exchange rate volatility was high (Charts 1 and 2). Another factor that contributed to exchange rate volatility was negative foreign sentiment towards Indonesia, which reduced capital inflows.

In order to reduce pressure on the rupiah, on 12 January 2001, Bank Indonesia issued regulation number 3/3/2001, which limits rupiah transactions and foreign currency credit extensions by banks. It covers two items, namely:

1. Prohibition on rupiah transfers by banks in Indonesia to non-residents, particularly for the rupiah transfers without underlying transactions that support Indonesia's economic activities.
2. Limitations on derivative transactions by lowering the limit on foreign currency sales from domestic banks to non-residents from $5 million to $3 million, for non-underlying transactions.

The main objective of this regulation is to reduce rupiah internationalization, by limiting rupiah outflows. The issuance of Bank Indonesia Regulation No. 3/3/2001 is expected to limit the supply of rupiah from residents to non-residents, which has the

Chart 1
Daily Average Changes in Vostro Account

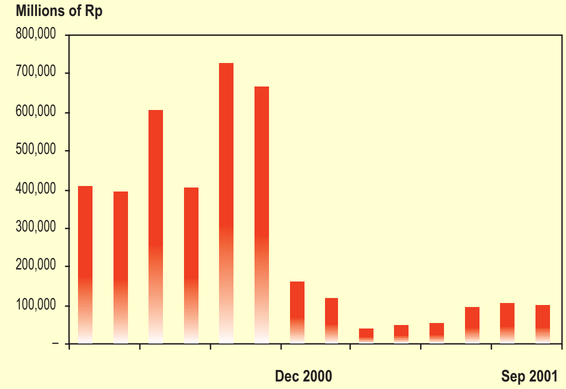


Chart 2
Developments in Vostro Account Balance

potential of being used for speculation. Hence, it will contain fluctuations in the exchange rate.

The implications of Bank Indonesia Regulation No. 3/3/2001 are as follows:

1. A drastic reduction in transactions from offshore markets (non-residents) that are made not on the basis of real transactions. These have been reflected in lower daily balances in vostro accounts, from Rp531.6 billion before the regulation was issued, to around Rp88.6 billion after the regulation was issued.
2. Shifting of most transactions that were previously undertaken in the offshore foreign currency-rupiah market to the domestic market, as reflected by rising swap and forward transactions that mostly came from foreign banks (Chart 3). At the same time, spot transactions undertaken by government and local banks also rose. The average daily value of spot transactions rose from $438 million prior to the issuance of the regulation to $511 million.
3. Shifting of foreign currency-rupiah transactions from offshore banks to domestic banks so that it will minimize opportunities for non-residents to undertake speculative transactions. This is in line with Bank Indonesia's prudential regulations for banks, such as the stipulation on the Net Foreign Currency Position, monitoring of foreign currency-rupiah market through data from the Money Market Information Center, Foreign Currency Flows, and other stipulations.
4. Average rupiah volatility after the regulation became effective, remained high. However, this volatility stemmed from two incidents that were due to changes in the political situation. The first case of high volatility was particularly the result of sharp rupiah exchange rate depreciation when the political climate became heated in advance of the national leadership transition. The other period of high volatility occurred when the rupiah exchange rate strengthened sharply after the transition of national leadership in mid-2001 (Chart 4). Excluding these two periods, exchange rate volatility tended to be lower than in 2000 (that is, before the regulation became effective), when the exchange rate was persistently depreciated.

Overall, Bank Indonesia Regulation No. 3/3/2001 has been able to reduce rupiah transactions

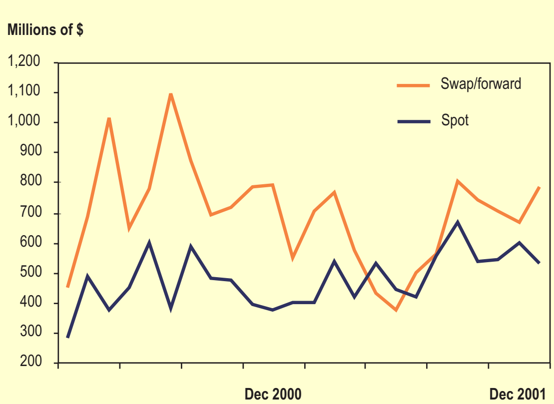


Chart 3
Daily Average Dollar-Rupiah Transaction

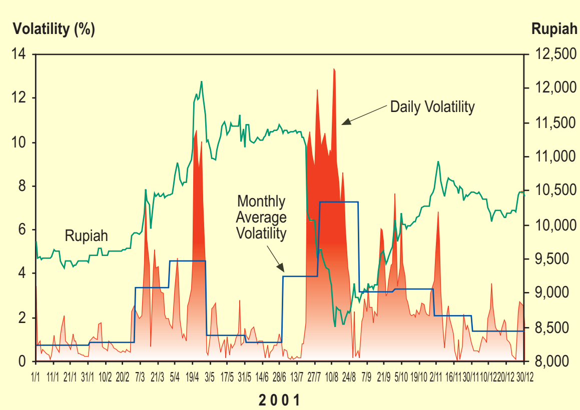


Chart 4
Volatility of Rp/$

undertaken by non-residents. However, rupiah exchange rate fluctuations in 2001 could not be avoided due to high uncertainty in domestic social, political and security conditions.

Efforts to enhance this regulation need to be continued so that speculation by non-residents can be reduced without hampering foreign capital inflows, which is needed to promote domestic investment.

chapter 4 INFLATION

chapter 4

INFLATION

At the beginning of 2001, Bank Indonesia expected that overall economic and financial conditions would improve in 2001. Economic growth was estimated to reach 4.5%–5.5%, while the exchange rate was expected to strengthen to an average of Rp7,750 – Rp8,250 per dollar. Based on these assumptions, Bank Indonesia set the Consumer Price Index (CPI) inflation target, excluding the impact of government prices and incomes policies, at 4.0%–6.0%. The impact of government policies on prices and incomes was estimated to add another 2.0%–2.5% to this target. Overall inflationary pressures in 2001 were expected to stem from the impact of government prices and incomes policies; an increase in aggregate demand; and inflationary expectations, especially as concerns the impact of government prices and incomes policies.

However, economic growth and exchange rate movements were not in line with initial assumptions, which resulted in stronger inflationary pressures than expected at the beginning of the year. These inflationary pressures originated in government prices and incomes policies; a weaker exchange rate; deteriorating inflationary expectations related to the weaker exchange rate and government policies; and limited production of foodstuffs. By contrast, aggregate demand did not add any meaningful inflationary pressures.

Bank Indonesia has undertaken various efforts to achieve the inflation target, by optimizing the available monetary instruments and by issuing new regulations in the exchange rate and foreign currency areas. To dampen the influence of the weaker exchange rate on inflation and to achieve the base money target set at the beginning of the year, Bank Indonesia absorbed excess liquidity through its open market operations. In support, Bank Indonesia intensively undertook foreign currency sterilization and limited rupiah transactions by non-residents. Furthermore, to hold down inflationary expectations, Bank Indonesia set a low inflation target at the beginning of the year.

However, these various efforts have not optimally reduced the pressures for exchange rate depreciation and fluctuations, considering these pressures were mainly caused by factors that were not fully under Bank Indonesia's control. Among those factors are : continuing high demand for foreign currency that was not matched by sufficient supply in the domestic market; negative sentiment of market players towards weaknesses in the implementation of certain economic restructuring programs; various non-economic factors; weaknesses in the micro structure of domestic financial markets; and bank intermediation that has not fully recovered. These factors trapped economic liquidity in the financial markets, which tended to be used for speculation in foreign currencies.

Strong inflationary pressure from the cost side, high inflationary expectations, and various

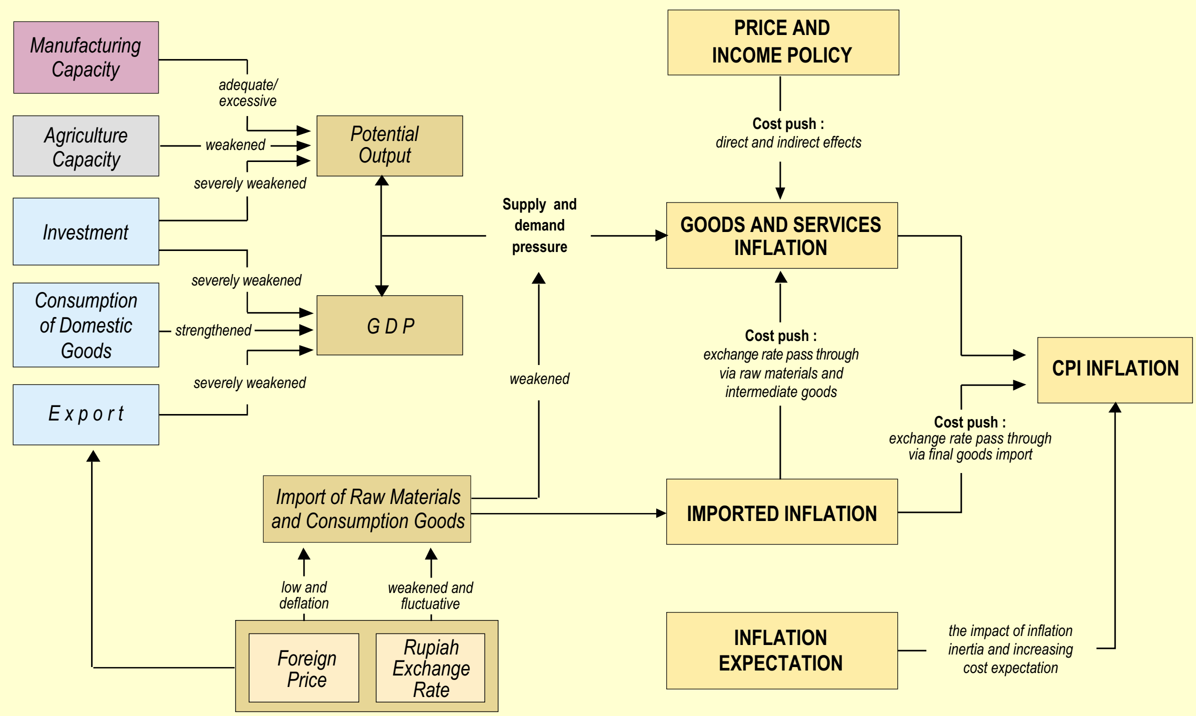


Diagram 4.1
Factors Affecting Inflation in 2001

problems faced by Bank Indonesia in controlling inflation, pushed up CPI inflation in 2001 to 12.55%. The inflationary pressures from the cost side were related to government prices and incomes policies, which are estimated to have accounted for inflation of 3.83%. The government policies included price hikes for various goods and services, such as fuel, transportation, electricity, clean water and cigarettes, as well as private sector minimum wages and salaries of civil servants. Excluding the impact of these policies, CPI inflation in 2001 is estimated to have reached 8.72%, well above the target of 4.0% - 6.0%. This was mainly due to rising producer costs stemming from the weaker exchange rate and deteriorating inflationary expectations.

CPI INFLATION

Inflation in 2001 accelerated, reached 12.55% compared to 9.35% recorded in the previous year. On a monthly basis, prices rose in 11 months of 2001,

Table 4.1
CPI Inflation Contribution in 2001 by Category

Category	Inflation	Contribution
Foodstuff	12.03	3.17
Housing	13.59	3.07
Prepared Food, Soft Drink, and Cigarettes	14.48	2.65
Transportation and Communication	14.16	1.56
Education, Recreation, dan Sport	11.90	0.93
Clothing	8.14	0.73
Health	8.92	0.44
Consumer Price Index	**12.55**	**12.55**

Source : BPS-Statistics Indonesia (processed)

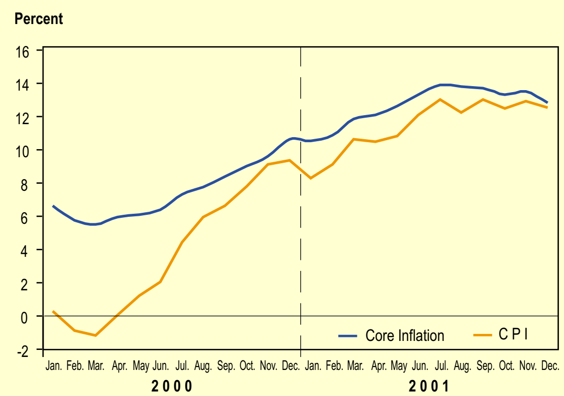


Chart 4.1
CPI and Core Inflation (y-o-y)

excepting only August, which recorded deflation. The highest monthly inflation, 2.12%, occurred in July. The largest contributor to CPI inflation was foodstuffs which accounted for 3.17%, while housing contributed 3.07%, and the processed-food, beverages, and cigarette category contributed 2.65%. The health services category made the smallest contribution, which is 0.44% (Table 4.1).

By sub-category of goods, the main contributors to CPI inflation were: housing; transportation; processed food; cigarettes, tobacco, and alcoholic beverages; grains, tubers and related products; and fuel, lighting, and water.

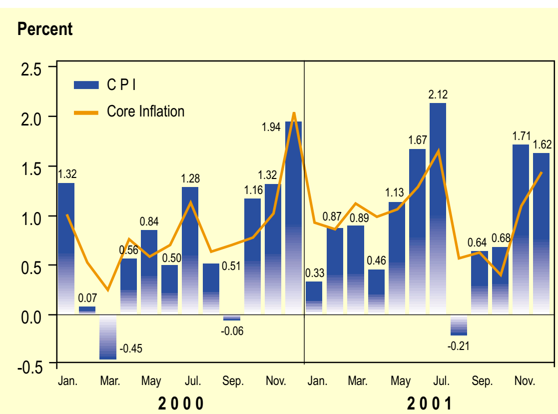
The strong inflationary pressures were reflected in the development of indicators that reflected the trend and persistency of inflation during the past two years. One of those indicators was core inflation calculated using the asymmetric trimming approach.[1] On this basis, core inflation (y-o-y) was on an upward trend and persistently above CPI

1 Core inflation calculated using the asymmetric trimming method is not the same as Bank Indonesia's inflation target. Several ways of calculating core inflation are described in the Box"Determination of Bank Indonesia's Inflation Target".

Table 4.2
CPI Inflation Contribution in 2001 by Sub-Category

Sub-Categery	Inflation	Contribution
Housing Cost	11.98	1.59
Transportation	17.24	1.50
Prepared Food	11.38	1.27
Tobacco and Alcoholic Beverages	32.89	1.23
Cereal, Cassava and Their Products	16.89	1.06
Fuel, Electricity and Water	28.41	1.04
Education Cost	17.38	0.71
Meats and its product	9.87	0.38
Fruits	13.75	0.32
Houshold operation	10.00	0.30
Vegetables	11.38	0.28
Fats and Oils	19.55	0.27
Clothing : Personal Effects	12.22	0.27
Fresh Fish	7.42	0.26
Beauty Treatment and Cosmetic	8.50	0.24
Spices	10.98	0.22
Eggs, Milk dan Their Products	9.64	0.20
Health Services and Drugs	9.12	0.20
Clothing : for Men	7.45	0.18
Clothing : for Women	6.46	0.18
Sport and Recreation	6.09	0.18
Non-alcoholic Beverages	4.50	0.15
Houshold Equipment	5.14	0.14
Clothing : for Children	6.86	0.11
Preserved Fish	9.58	0.08
Beans and Nuts	4.86	0.06
Transport Equipment and Support	7.56	0.06
Education Equipment	5.50	0.05
Other Foods Items	9.49	0.01
Communication and Delivering	0.21	0.00
Consumer Price Index	**12.55**	**12.55**

Source : BPS - Statistics Indonesia (processed)



Source : BPS-Statistics Indonesia

Chart 4.2
CPI and Core Inflation (m-t-m)

inflation (Chart 4.1). This was also the case for monthly movements in core inflation, which had been trending upwards since 2000 (Chart 4.2).

INFLUENCE OF GOVERNMENT PRICES AND INCOMES POLICIES

Government policies added to inflationary pressures in 2001. These policies included: the prices and tariffs of a number of goods and services (such as fuel, electricity, clean water, and cigarettes); the minimum wage policy for the private sector labor force; and salaries of civil servants. Taken together, these added 3.83% to CPI inflation on annual basis (Table 4.3). This is somewhat larger than the estimate at the beginning of the year of 2.0%–2.5%. This difference was due, among others, to larger increases in several areas than had been expected at the beginning of the year. In addition, certain government plans were not fully anticipated at the beginning of the year, when the initial inflation estimate was developed. Therefore, there was limited information at the beginning of the year concerning the magnitude of price and tariff increases and the stages in their implementation.

In 2001 the government's raised fuel prices for transportation, set fuel prices for industry to 50% of market prices, and increase transportation tariffs. These prices increased are estimated to add 1.78% to inflation. The impacts were in June and July after the hikes in fuel prices became effective in June 2001. The impact in June consisted of the direct impact on gasoline, pumped gasoline, and diesel fuel in the CPI basket, as well as the indirect impact on operational costs of businesses, including transportation costs. Meanwhile, the impact in July constituted the indirect impact through increased production costs.

Hikes in electricity tariffs in July and October are estimated to add 0.56% to inflation in August and December. Another pricing policy that had a sizable influence on 2001 CPI inflation was the increase in the minimum retail selling prices for cigarettes. This policy was aimed at rising government revenue through cigarette excise tax (which are calculated based on the minimum retail selling prices) and it

Table 4.3
The Impact of Government Prices and Income Policies in 2001

Price Increase		Impact on Monthly Inflation
Fuel and Transportation		1.78
Cigarettes Minimum Retail Price		0.73
Electricity Tariff		0.56
Clean Water Tariff		0.05
Provincial Minimum Wages		0.17
Civil Servants Salary		0.20
Luxury Tax		0.01
Expected impact of government policy to CPI inflation in 2001	cumulative m-t-m	**3.50**
	y-o-y	**3.83**

Source : BPS - Statistics Indonesia (processed)

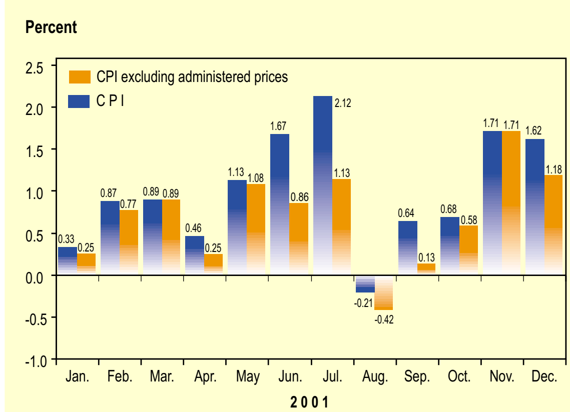


Chart 4.3
Consumer Price Index

Table 4.4
Government Prices and Incomes Policies in 2001

Month	Remarks	Percent Increase	
		Initial Assumption	Realization
January	Provincial Minimum Wages	15%	15%
February	Luxury tax for 41 categories excl. motor vehicle	not available	10% – 15%
March	Clean water tariff	20%	18,77% – 42,47%
April	Excise tax/cigarettes retail selling price (1st stage)	5% in each stage	5% (1st stage)
June	Fuel tax	20%	30%
	City transportation tariff	not available	28,57% (only Jakarta)
July	Inter-City Inter-Province Bus Tariff	not available	36%
	Excise tax/cigarettes retail selling price (2nd stage)	5% in each stage	6% (2nd stage)
	Electricity Tariff (1st stage)	not available	29,2%
September	Civil servant salary	30%	11,2%
October	Electricity Tariff (2nd stage)	not available	12,4%
December	Excise tax/cigarettes retail selling price (3rd stage)	5% in each stage	3% (3rd stage)

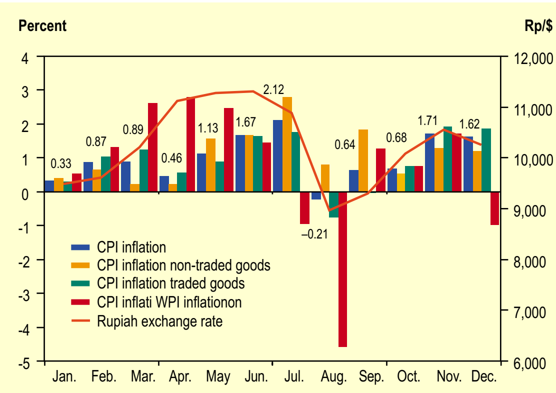
Source : Various

added 0.73% to CPI inflation. Moreover, the government's incomes policy (in the form of provincial minimum wages and salaries of civil servants) is estimated to add another 0.37%. Another policy with an impact on prices was the February increase in the sales tax on luxury goods, which is estimated to add inflation of only 0.01%.

IMPACT OF THE WEAKER RUPIAH EXCHANGE RATE

The rupiah exchange rate, which had been expected to strengthen during 2001 up to an average of Rp8,000 per dollar, actually weakened to an average of Rp10,255 per dollar, despite some strengthening early in the second half of 2001. This development pushed up CPI inflation due to increases in the costs of imported raw materials and semi-processed goods, which are substantial components of domestic goods.[2] In addition, the weaker exchange rate pushed up the cost of imported consumption goods, which are included in the CPI basket.

Movements in monthly CPI inflation were in line with movements in the rupiah exchange rate. The rupiah weakened at the beginning of the year and was at its lowest level from April through June, in line with high CPI inflation, particularly from May through July (Chart 4.4). Similarly, exchange rate movements were reflected in the wholesale price inflation and the traded-goods component of CPI inflation, which indicates the



Source : BPS-Statistics Indonesia, Bank Indonesia, Bloomberg

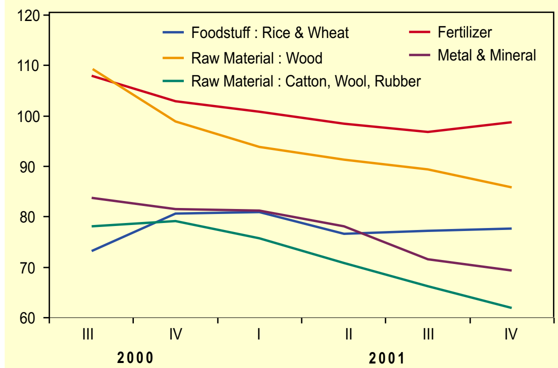
Chart 4.4
Rupiah Exchange Rate & Inflation (m-t-m)

2 Based on a 2001 survey of price formation in the manufacturing and retail sectors, imported raw materials represent some 30-40% of the total cost of downstream industries that produce goods in the CPI basket.

development of imported goods prices and production cost. In turn, the exchange rate depreciation also added to inflation in non-traded goods.

The strong influence of the exchange rate on inflation was in line with Bank Indonesia's research on monetary policy transmission from the exchange rate to inflation. This research showed that the influence of the exchange rate on inflation has became very strong since the floating exchange rate regime came into effect. By contrast, during the pre-crisis period, the influence of the exchange rate on inflation was considerably less because the exchange rate was stable and easy to predict. In addition, the survey on price formation mechanism in the manufacturing and retail sectors in 2001 indicates that the main factor boosting prices was the exchange rate depreciation. Lags in this process were quite short, within a week or less and up to one month.

In fact, the strengthening of the rupiah exchange rate in July and August had caused prices to decline. However, the magnitude of the impact from an appreciation does not appear symmetric with a depreciation. The appreciation of rupiah by 4.0% in July and 21.3% in August, only prompted monthly deflation of 0.24% in August. This condition indicated the existence of downward rigidity in prices, despite significant cost declines stemming from a strengthening exchange rate. Indications of asymmetrical price movements were in line with research on monetary policy transmission via the exchange rate channel and in the survey on price formation in the manufacturing and retail sectors *(Box: Survey of Price Formation in the Manufacturing and Retail Sectors)*. In addition, information from that survey indicated that asymmetrical pricing behavior



Source : World Banks

Chart 4.5
International Commodity Price index

was more common at the retail level than the producer level. This is supported by the fact that CPI deflation was far smaller than deflation of the wholesale price index in the month of August.

Furthermore, declining international commodity prices had a deflationary impact on imported goods prices. As depicted in Chart 4.5, international commodity prices trended downwards for wood, cotton, wool, rubber, fertilizer, as well as metal and materials commodities. However, these price declines were more than fully offset by the exchange rate depreciation, which caused prices of imported goods to rise.

IMPACT OF INFLATIONARY EXPECTATIONS

High CPI inflation was also related to the inflationary expectations of producers, traders, and consumers. On the producer side, inflationary expectations tended to rise during 2001 as indicated by the business survey (Chart 4.6). High inflationary expectations were mainly determined by high inflation in 2000, which had reached 9.35%. Based on the 2001

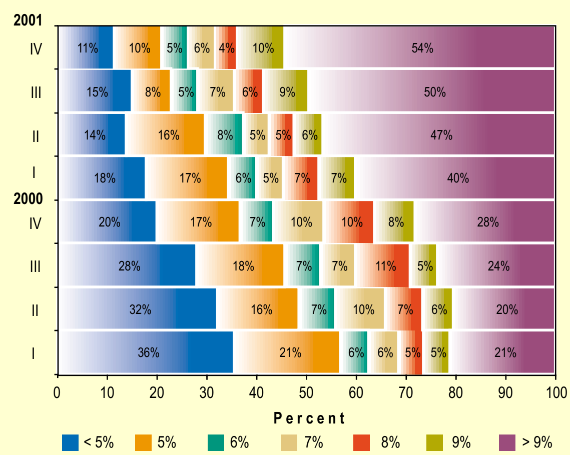


Chart 4.6
Inflation Expectation by Producer

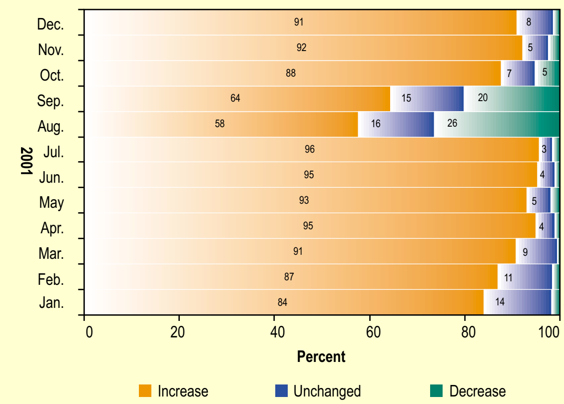


Chart 4.8
Consumer Expectation on Inflation 6-12 Month Ahead (% Respondent)

survey on price formation in manufacturing and retail sales, the inflationary expectations of producers and retail traders originated mainly in the development of current and previous year's annual inflation (Chart 4.7). This adaptive mechanism for the formation of inflationary expectations was in line with the results of Bank Indonesia's research on monetary policy transmission through the inflationary expectations channel.

Meanwhile, the consumer survey also showed a rise in consumers' expectation toward inflation (Chart 4.8). In general, consumer expectations were influenced by expectations on administered price increases and on exchange rate depreciation. This was seen in the movement of consumer expectations on price increases in 6 – 12 months ahead as well as the expectations for

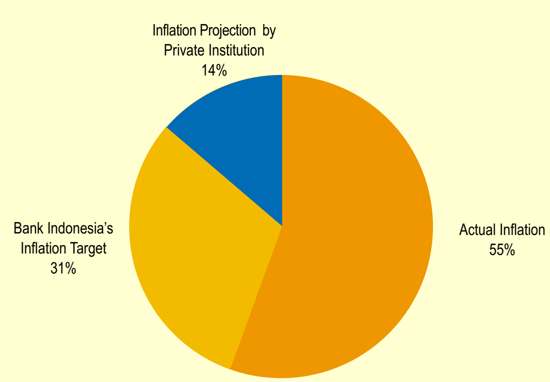


Chart 4.7
References Employed to Construct Producers' Inflation Expectation (% Respondent)

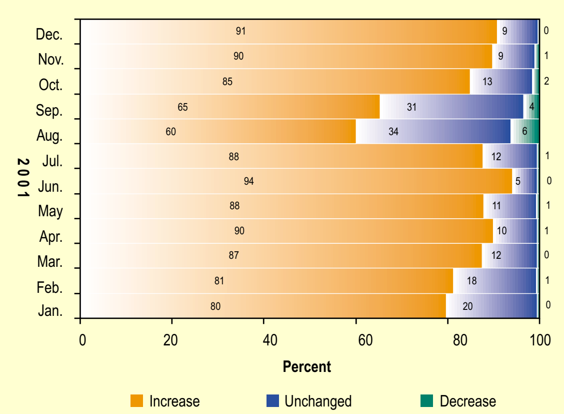


Chart 4.9
Consumer Expectation on Transportation/Communication Cost 6-12 Months Ahead (% Respondent)

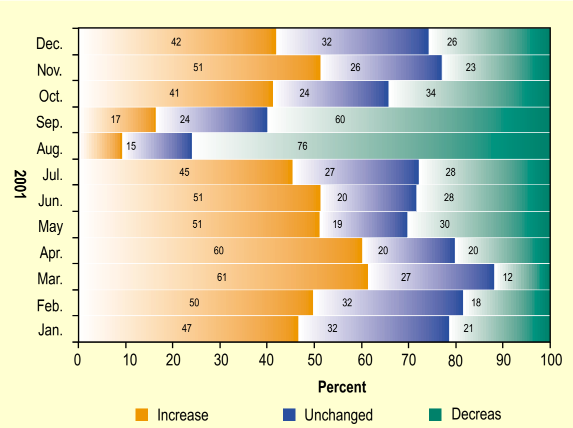


Chart 4.10
Consumer Expectation on Rupiah Exchange Rate 6-12 Month Ahead (% Respondent)

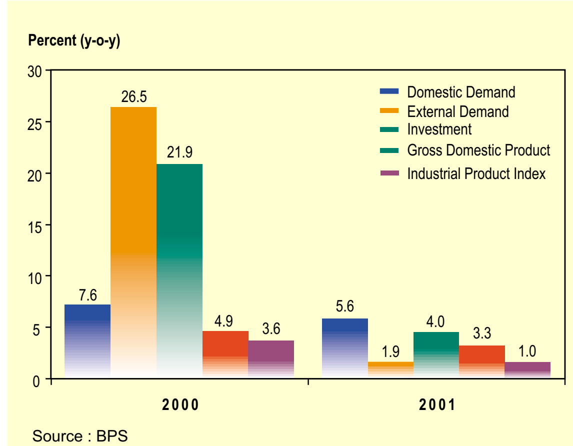


Chart 4.11
GDP Growth

increases in transportation and communication costs (Chart 4.9) and for the exchange rate in the next 6-12 months. (Chart 4.10).

IMPACT OF DEMAND AND SUPPLY CONDITIONS

The impact of demand and supply conditions on consumer inflation could be seen in the two main sectors that produce consumption goods in the CPI basket, namely manufacturing and agriculture. In the manufacturing sector, inflationary pressures due to demand and supply conditions remained low. This was in line with slow economic growth and high excess capacity in manufacturing. By contrast inflationary pressures arose due to imbalances in demand and supply conditions existed in the agriculture sector. However, that inflationary pressure was not spurred by increasing demand, but rather by declining production of foodstuffs. Limited supplies of foodstuffs, which could not even match continuing low demand, had an appreciable influence on consumer inflation, partly because foodstuffs have a large weight in the CPI basket.

Aggregate demand weakened for both domestic demand (consumption and investment) and external demand (Chart 4.11). GDP growth declined in agriculture, construction, and manufacturing, and in the index of industrial production. In the mean time, expansion of economic capacity slowed as reflected in declining investment growth.

Excess capacity remained in the manufacturing sector. Based on the survey of manufacturing, capacity utilization in that sector was stable yet at a low rate, in the range of 39% –51%, far lower than the highest rate reached in 2000 of 68% (Chart 4.12). Low rates of capacity utilization were also supported by the survey on price formation in the manufacturing and retail sectors (Chart 4.13).

By sector, capacity utilization in the processed food, beverage, and tobacco industry (whose products were the largest contributors to inflation in 2001) was on the upward trend during 2001. However, even by the end of 2001, the rate of capacity utilization in this sector was still below 40%, far below the highest level, 76%, in 2000 (Chart 4.14).

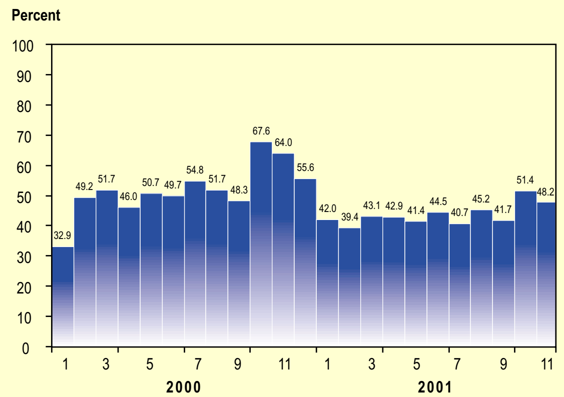


Chart 4.12
Capacity Utilization Rate in Manufacturing Industry

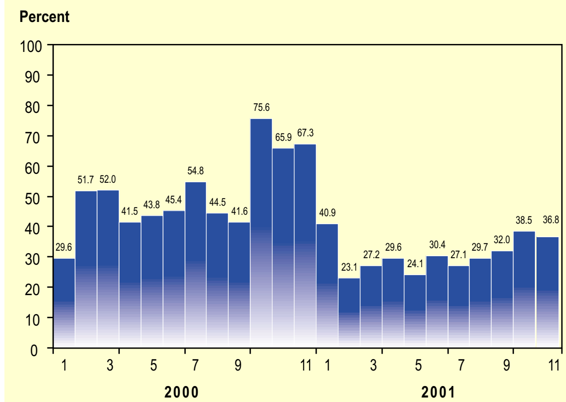


Chart 4.14
Capacity Utilization Rate in Food, Beverages, and Tobacco Industry

This indicated that the impact of demand and supply conditions has not exerted inflationary pressures in the processed-food, beverage, and tobacco category. This was also the case for capacity utilization of textile products, which tended to rise slightly, but is still below previous year's 75% level (Chart 4.15). The high and increasing rates capacity utilization were in the non-metal quarrying goods industry, which produces construction materials that are categorized as housing costs in the CPI basket (Chart 4.16). This condition is estimated to have boosted prices of construction materials. Nevertheless, high inflation in housing costs originated more in higher housing rentals and workers' wages rather than the price of construction materials.

Low capacity utilization rates in manufacturing should not put any pressure on consumer inflation. However, there were constraints related to

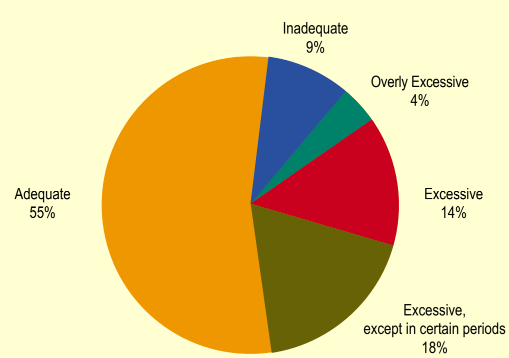


Chart 4.13
Availibility of Manufacturing Production Capacity (% Respondent)

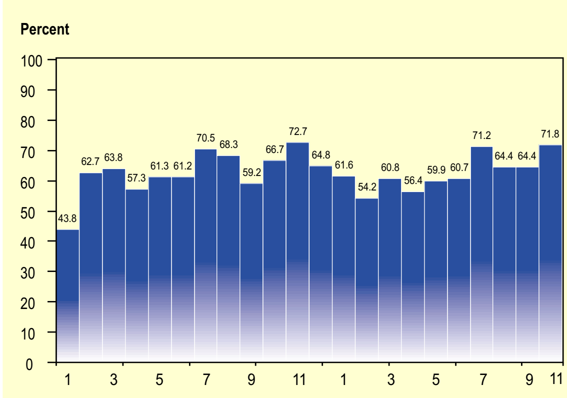


Chart 4.15
Capacity Utilization Rate in Textile, Garment & Leather Goods

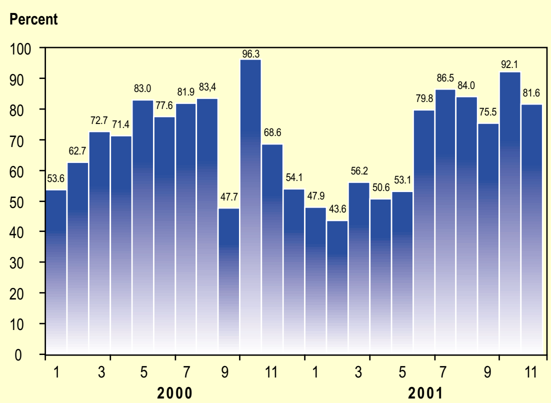


Chart 4.16
Capacity Utilization Rate in Non-metal Mining Industry

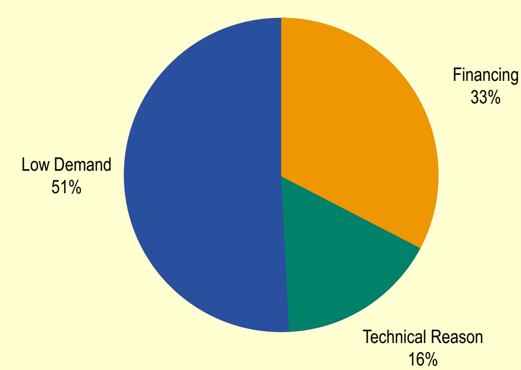
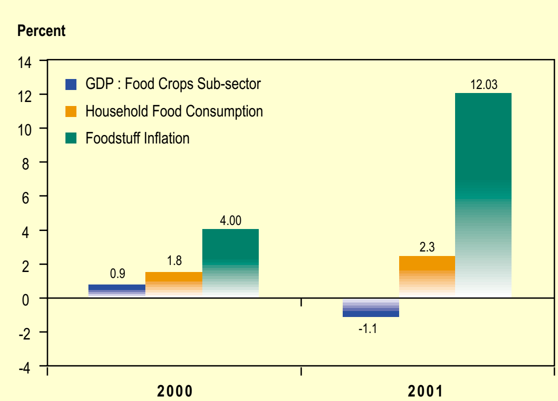


Chart 4.17
Constraints in Utilizing the Idle Capacity (% Respondent)

working capital financing, that prevented manufacturers from using this excess capacity. Hence, the burden in utilizing idle capacity lead to the emergence of some price pressure as proved by survey on price formation. The survey concludes that 33% of the total respondent faced financial problem in utilizing idle capacities. However, the main cause of idle capacity was low demand as indicated by 51% of the total survey respondents. In addition, there were also some technical production problems (Chart 4.17). These conditions suggest that although capacity utilization in manufacturing faced some constraints, these were not meaningful sources of inflationary pressure in 2001 because demand remained weak. However, if the financing constraint in this industry is not overcome, it could become a source of inflationary pressure in with regard to rising demand.

Price pressures resulting from an imbalance between demand and supply are estimated to have occurred in production of foodstuffs. Household spending on foodstuffs rose only moderately (by 1.8% and 2.3% in 2000 and 2001, respectively), but the production of foodstuff sub-sector of agriculture contracted by 1.1% in 2001 (Chart 4.18). This imbalance between demand and supply prompted high inflation of foodstuffs, especially grains and tubers and related products.

Seasonal demand pressure approaching Idul Fitri, Christmas and New Year holidays also had a significant influence on inflation. This can be seen in the high (monthly) CPI inflation in November, when



Source : BPS - Statistic Indonesia

Chart 4.18
Supply and Demand for Food Category

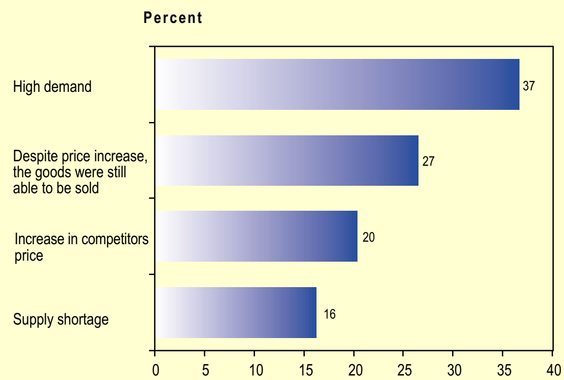


Chart 4.19
Factors Affecting Inflation
in the Forthcoming Religious Festivities & New Year

the exchange rate was stable at around Rp10,560 per US dollar and there was no shortage of goods. Referring to the survey on price formation in the manufacturing and retail sectors, high inflation during this holiday period was spurred more by rising demand than limited or disrupted supplies of goods. Also, high inflation in this period was influenced by public consumption behavior, which tended to be insensitive to price increases (Chart 4.19). This survey also showed that the action to raise prices in the face of strong seasonal demand was undertaken more by the traders than by manufacturers.

box

Survey on Price Formation in the Manufacturing and Retail Sectors

As mandated by Act 23 of 1999, Bank Indonesia's objective is to achieve and maintain stability in the value of the rupiah. In implementation, Bank Indonesia is responsible for holding inflation to a level that is relatively low and stable. Efforts to control inflation need a realistic outlook for inflation and an estimate of the impact of monetary policy in influencing price changes. In order to accurately estimate inflation, realistically set the inflation target, and appropriately formulate policy responses, Bank Indonesia needs to identify factors that determine price formation and to calculate the ability of monetary policy to control inflation. Price formation policy by producers and traders is mainly determined by their inflationary expectations and the interaction of changes in demand and supply costs. However, price formation can be asymmetric as between rises and declines in cost and demand. Meanwhile, the ability of monetary policy to control inflation is determined by the channels and lags in monetary policy transmission and by pricing behavior.

Against this backdrop, Bank Indonesia needed to obtain a picture of price formation behavior of consumption goods that are included in the CPI basket. Accordingly, a survey was conducted of producers of manufacturing goods and retail traders from July to September 2001. Survey respondents were determined using the Purposive Sample method[1], consisting of 200 companies in the manufacturing sector that produced consumption goods included in the CPI basket and 220 units of retail businesses that were respondents to Bank Indonesia's retail sales survey.

Results of that survey indicated that CPI increases at present time stemmed more from cost (cost-push inflation) rather than demand pressures (demand-pull inflation). Pressure from the cost side particularly came from exchange rate depreciation and the influence of government policies in raising import duties on raw materials and production equipment, fuel prices, electricity tariffs, and minimum wages.

With regard to cost changes, the survey indicated that producers and sellers tended to be more responsive to cost increases than to cost declines. This behavior causes prices to rise easily when costs increase but drop slowly when there are cost declines. This characteristic was reflected among others in prices at the retail sector, where prices remain unchanged for about 2.9 months during the year before the survey was conducted. This asymmetrical pricing behavior was more common in the retail sector than the manufacturing sector. In the manufacturing sector, on average, price levels remained unchanged for as long as 4.6 months. This price level retention period is shorter than in several advanced countries, where survey indicated up to 6 to 15 months.

1 Purposive sampling constitutes a method of taking samples by choosing respondents based on certain purposes.

Price behavior that tends to rise easily was also reflected by the quite short time lag between the occurrence of cost changes and the effectiveness of price changes, which was four weeksin the manufacturing sector and less than one week in the retail sector. Similarly, the influence of the exchange rate on inflation through prices of imported consumption goods occurred within a less than one-week period, while the impact through the costs of imported raw materials took around five weeks. In addition, the response to cost changes with regard to higher fuel prices and electricity tariffs led to higher prices of consumption goods within one month.

Concerning inflationary expectations, most respondents (55%) indicated that their outlook for inflation was mainly determined by post experience, rather than by Bank Indonesia's target (31% of respondents) or inflation projections issued by private institutions (14%). This result indicates that adaptive expectations characterize the behavior of producers and traders in their price setting.

Furthermore, both manufacturers and retailers do not believe that demand pressures are the main factor causing price changes in 2001, except on special occasions, such as Idul Fitri, Christmas, and New Year. In general, manufacturers and retailers respond to demand increases by raising their production and inventories. Very few companies say they respond by raising prices. The case was the same the other way around. When there was a drop in demand, companies tended to respond by reducing production or their stocks of goods. The survey indicated that demand changes (both increases and decreases) had more impact on levels of production than on prices. In other words, even when demand changes, prices tend to remain fixed.

Pricing behavior in response to demand changes indicated the existence of excess capacity amid weak demand. The majority of manufacturing respondents estimated that capacity utilization was currently in the range of 61%–80%, with an average of 65.8%. That level was considered by the majority of respondents (54%) as being sufficient to match demand. Meanwhile, 18% of the respondents considered their capacity to be excessive or even overly excessive, and 19% of respondents considered their capacity to be excessive, except at certain times. Furthermore, only 9% of respondents reported insufficient capacity.

With specific reference to the period of Idul Fitri, Christmas, and New Year, price formation behavior was very much influenced by rising demand that is price inelastic. These conditions tended to be particularly utilized by traders as an opportunity to raise prices, despite no supply constraints. The survey recorded as many as 74% of retail traders and 43% of manufacturers were taking advantage of this opportunity.

These pricing characteristics have implications for Bank Indonesia's policy in setting inflation targets and monetary policy. These characteristics include: prices that are influenced more by costs than demand; prices that tend to decline only with difficulty; prices that tend to rise easily due to cost pressures; and prices that tend not to rise easily due to demand pressure. As long as the rupiah exchange rate remains under pressure and the government increases administered goods prices, Bank Indonesia cannot set a very low inflation target and achieve it in a very short time span. On the contrary, Bank Indonesia needs to set a realistic inflation target that is achievable in line with the capacity of monetary policy. Considering the price formation behavior, weak demand conditions and realistic inflation target setting, tighter monetary policy is not expected to be able to effectively reduce inflationary pressures. On the contrary, monetary policy needs to be directed towards providing room for interest rates to decline, in order to signal the banking sector and real sector business players to increase economic activity. However, monetary policy must be supported by efforts to revive the banking sector's intermediation function.

chapter 5 MONETARY DEVELOPMENTS

chapter 5

MONETARY DEVELOPMENTS

At the beginning of 2001, when there was considerable optimism towards sustainability of the ongoing economic recovery, Bank Indonesia determined that 2000's relatively high inflation rate needed to be lowered, as a prerequisite for achieving sustainable long-term economic growth. Accordingly, the inflation target (excluding the impact of government prices and incomes policies) was set at 4.0% - 6.0%. Underlying this target were assumptions that economic growth would be at 4.5% - 5.5% and that the exchange rate would be in the range of Rp7,750 – Rp8,250 per dollar. Partly on this basis, Bank Indonesia set its base money target at 11.0% - 12.0% by the end of 2001, down from 22.3% at the end of 2000.

This monetary policy target, which had a tight bias, was the basis to pursue base money during 2001 in line with the target. In order to achieve its base money target, Bank Indonesia continuously made efforts to absorb excess liquidity in the banking sector, thereby reducing the potential for pressure on the exchange rate and inflation. These policies were implemented mainly using open market operations (OMOs) with Sertifikat Bank Indonesia/ SBIs (Bank Indonesia Certificates) and rupiah intervention. Efforts to control base money were also supported by intervention operations in the foreign currency market, which were directed at absorbing base money expansion originating in government rupiah spending that was financed from foreign borrowing. These measures were meant to ensure that efforts to achieve the base money target would not create excessive increases in interest rates. The foreign currency intervention policy also added to the supply of foreign currency in order to reduce depreciation pressures and the volatility of the rupiah exchange rate.

During implementation, monetary control faced several constraints that caused base money control to be less than optimal, particularly after May 2001. It is indicated by, frequently on test dates,[1] base money exceeded its target.[2] This was due to continuously rising public demand for currency, which is the main component of base money. The rising demand for currency was related to a significant expansion in the roles of the small- and medium-scale businesses and the informal sector, which still deal mainly in cash. In addition, heated social and political conditions prompted the public to hold currency in excess of their normal needs for precautionary motives through mid-2001. Also, the demand for currency rose in line with rising transaction needs stemming from higher prices brought on by government prices and incomes policies in June 2001. In such conditions, base money demand

1 The 'test date' for base money is measured as the average daily position from the 16th of the given month up to the 15th of the following month.

2 The base money target is based on assumptions concerning inflation, GDP growth, time deposit interest rates, and the exchange rate. It is determined in the Letter of Intent (LoI).

became less responsive to interest rate changes, meaning that relatively large increases in interest rates would have been needed to absorb more base money.

Efforts to control monetary conditions faced additional difficulties because bank intermediation had not fully recovered, magnifying the amount of excess liquidity to be absorbed by Bank Indonesia. In addition, the monetary transmission process weakend, as time deposit interest rates became less responsive to SBI interest rates.

This combination of strong demand for currency and weakened monetary transmission links due to limited restoration of bank intermediation have made it more difficult to absorb excess base money. Despite various measures to absorb liquidity (including through SBI auctions, rupiah intervention, interest rate increases, and foreign currency intervention) base money often moved usually above its target. In such conditions, increases in SBI rates to absorb more base money would have been ineffective. In coping with this condition, especially since the third quarter of 2001, Bank Indonesia tended to absorb excess liquidity from the banking system without excessive rises in SBI rates. In addition, when excess liquidity could not be absorbed through SBI auctions, Bank Indonesia used rupiah intervention.

Early in the year, base money, which had expanded very rapidly at the end of 2000, was under control and it stayed within its indicative target through April 2001. However, due to the various constraints mentioned above, base money began to accelerate and was outside its indicative target beginning May 2001. Through December 2001, base money expanded by 15.4%;[3] on average, it increased by 18.2% during 2001. By way of comparison, the target (set at the beginning of the year) for end-2001 was 11.0% - 12.0%.

Bank Indonesia's efforts to control the expansion of base money have caused SBI rates to rise. During 2001, the interest rate on 1-month SBIs rose by 309 basis points (bp) to 17.62% and the interest rate of 3-month SBIs rose by 332 bp to 17.63%. Also, to make room for time deposits rates to rise in line with changes in SBI rates, Bank Indonesia raised the margin of the deposit guarantee interest rate. This was done twice, in January and in August 2001, by 100 bp on each occasion, until it reached a margin of 400 bp above the time deposit interest rate of banks that were members of JIBOR.[4] This policy was successful in pushing up the (weighted average) time deposit nominal interest rate. In real terms, time deposit rates also rose. However, the new level is still far below pre-crisis levels, and even more so considering the current, high level of risk premiums.

In line with the rise of time deposit interest rates, total saving deposits also rose in comparison with the year before. The rise is believed to be related to the shifting of funds out of placements that were more short-term, such as saving deposits and demand deposits. By the end of 2001 this development has

3 This growth was calculated based on the December 2000 test date for base money, excluding the seasonal influence of Idul Fitri, whose timing shifts every year.

4 The margin of deposit interest rates was raised from 200 bps to 300 bps based on Circular Letter number 3/1/DPNP dated 5 January 2001 and from 300 bps to 400 bps based on Circular Letter number 3/19/DPNP dated 14 August 2001.

caused broad money supply (M2) to expand faster than narrow money (M1).

BASE MONEY

In general, control of base money during 2001 faced various quite serious challenges, which caused test date base money to be above its indicative target for most of the year. During the first four months of the reporting year, test date base money was still within its indicative target, reaching its lowest position of Rp101.9 trillion in February. However, beginning in May 2001, base money rose rapidly, exceeding its indicative target, except in November (Chart 5.1). Test date base money rose to Rp124.7 trillion in December, over its indicative target of Rp122.9 trillion. On average, annual base money expanded by 18.2% during 2001, a bit lower than the previous year's 18.6%.

At the end of 2001, base money reached Rp127.8 trillion, up Rp2.2 trillion compared from the previous year's Rp125.6 trillion. Base money peaked at Rp134.1 trillion during the run-up to Idul Fitri, and it dropped significantly after the holidays ended. This rise was mainly accounted for by the currency component, which during 2001 experienced an average annual growth of 20.1 %, considerably above base money average growth in the same period (Chart 5.2). Meanwhile, other factors, such as banks' positive balances and private sector demand deposits, did not change during the reporting year. Relatively stable

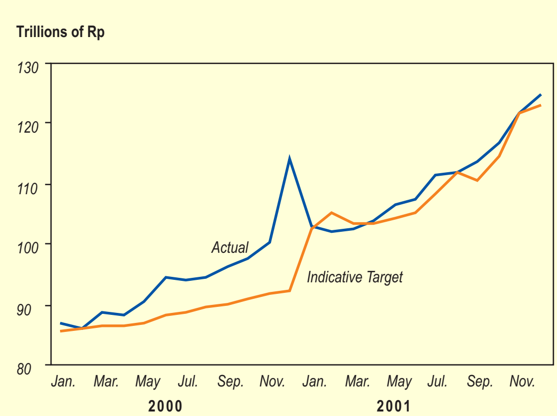


Chart 5.1
Base Money : Actual and Indicative Target

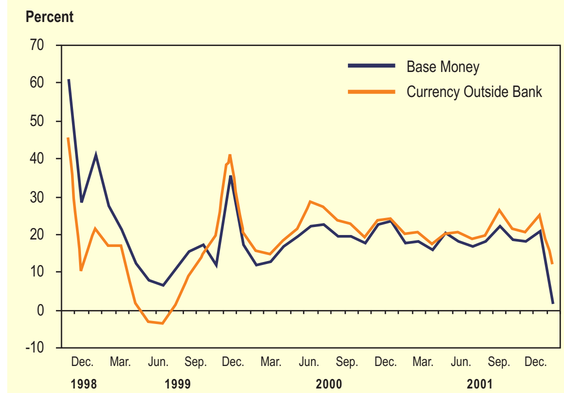


Chart 5.2
Currency and Base Money Growth

Table 5.1
Base Money and Its Affecting factors

Item	2000	2001				Annual Change
		I	II	III	IV	
	Trillions of Rupiah					
Base Money	**125.6**	**103.3**	**110.6**	**115.2**	**127.8**	**2.2**
Bank notes and coins outside BI	89.7	69.9	76.9	80.8	91.3	1.6
– public	72.4	60.1	66.2	69.0	76.5	4.1
– bank	17.3	9.8	10.7	11.8	14.8	–2.5
Banks demand deposits at BI	33.9	30.9	30.9	31.6	34.8	0.9
Private sector demand deposits	2.0	2.4	2.9	2.8	1.7	–0.3
Factors Affecting	**125.6**	**103.3**	**110.6**	**115.2**	**127.8**	**2.2**
Net International Reserve (NIR)	124.5	124.3	128.0	127.8	128.1	3.6
Net Domestic Asset (NDA)	1.1	–21.0	–17.4	–12.6	–0.3	–1.4
- Net claims on central goverment	133.7	134.4	125.6	135.5	160.8	27.0
- Liquidity support	37.3	36.7	37.1	37.1	37.1	–0.2
- Liquidity credit	15.9	15.6	15.3	15.2	15.1	–0.8
- Other claims	1.5	1.3	1.7	1.9	1.9	0.3
- Money market operation	–78.9	–90.0	–85.6	–86.0	–102.6	–23.7
- Net other items (NOI)	–108.4	–119.2	–111.5	–116.2	–112.4	–4.0

positive balances, which were the result of low excess reserves, suggested that efforts to absorb banking system liquidity have been conducted well.

During 2001, currency rose by Rp4.1 trillion, reaching Rp76.5 trillion by year-end compared with the previous year's Rp72.4 trillion (Table 5.1). Currency reached its highpoint, Rp85.8 trillion, during the approach of Idul Fitri. This rise was largely seasonal, and it dropped with the end of festivities.

The rapid increase in currency was related to the significant rise in activities of the small- and medium-scale business sector and the informal sector, which tend to use relatively large amounts of currency in their transactions. The higher demand for currency also stemmed from heated socio-political conditions in Indonesia up to mid-2001, which boosted precautionary motives for holding cash. Currency demand rose further, in line with rising needs for money for transaction purposes due to higher prices of goods spurred by government prices and incomes policies at the end of June 2001. This condition was seen in a change in the demand for currency, around July 2001 (Chart 5.3).

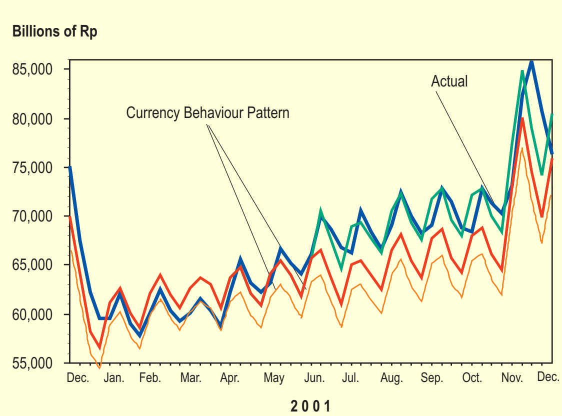


Chart 5.3
Cyclical Currency Behaviour

Rising demand for currency, which was prompted by higher prices and precautionary needs, was also supported by the "Public Motives in Holding Currency" survey conducted in 5 large cities in Indonesia (Chart 5.4). Based on that survey, the main motive prompting the public to demand more currency was price hikes of basic goods (21.6%). The other important motives were the wider types of goods and services that the public wanted to purchase (20.9%), which reflected rising real incomes, and precautionary motives (13.4%) occasioned by uncertain domestic political and security conditions. Remaining factors, such as the weaker exchange rate, interest rates on savings, larger currency denominations, and speculative objectives were relatively low (only 12.2%).

The rise in base money was mainly prompted by the expansionary impact of government rupiah accounts exceeding the contractionary influence of OMOs and foreign currency intervention. Net expansion of government rupiah accounts reached Rp41.1 trillion, used mainly for payments of salaries, general allocation funds, and revenue sharing funds of Rp81.3 trillion, bond coupons of Rp58.2 trillion, subsidies of Rp32.6

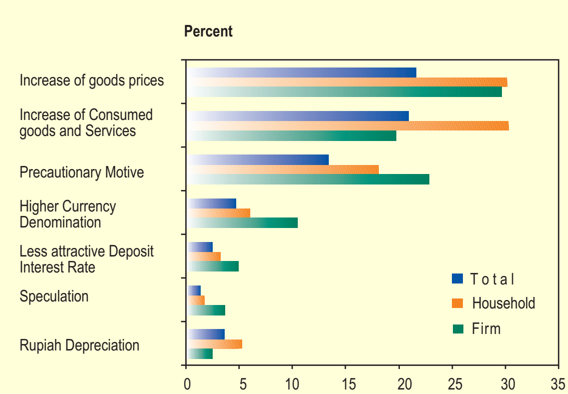


Chart 5.4
Motives for Holding Currency

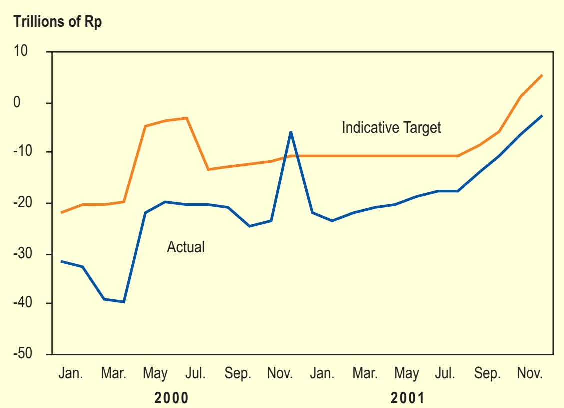


Chart 5.5
Net Domestic Assets

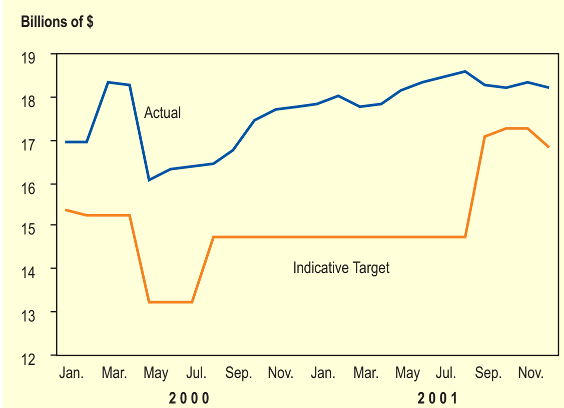


Chart 5.6
Net International Reserves

trillion, and project financing of Rp27.4 trillion. This government spending exceeded government revenues, which mainly originated in tax revenues of Rp127.5 trillion and sales of assets and privatizations of Rp31.4 trillion. Part of the rupiah account expansion was financed by government foreign currency revenues and withdrawals of government savings at Bank Indonesia. Government foreign currency revenue mainly originated from oil and gas receipts, which reached Rp62.4 trillion, larger than net payments on government offshore loans of Rp37.4 trillion.

The net contraction from OMOs was Rp23.7 trillion during 2001, which mainly came from rupiah intervention of Rp28.0 trillion, particularly in December, when banks' precautionary motives were high with the approach of Idul Fitri and year end. On the other hand, SBI auctions during the same period provided an expansionary effect of Rp4.3 trillion.

In line with the expansionary components of base money, Net Domestic Assets (NDA) during 2001 were on a rising trend, and turned positive for a while, well above the indicative target during the Idul Fitri. After Idul Fitri, NDA slowly dropped until it reached a test date position of negative Rp2.7 trillion by year-end, lower than its indicative target of Rp5.3 trillion (Chart 5.5). Meanwhile, Net International Reserves (NIR) rose by $0.5 billion, reaching $18.3 billion or equal to Rp128.1 trillion[5] at the end of 2001. This rise in NIR mainly came from oil and gas revenues of $5.3 billion, as well as offshore loans and proceeds from foreign currency management of $4.2 billion. This foreign currency revenue was larger than foreign currency spending, which was mainly used for payment on offshore loans and foreign currency intervention in the amount of $9.6 billion. Despite an adjustment that raised the NIR target floor by $1.9 billion to $17.6 billion in September, NIR was still above its indicative floor during 2001 (Chart 5.6).

OPEN MARKET OPERATIONS

As indicated earlier, efforts to control base money during 2001 depended on OMOs, mainly SBI auctions and rupiah intervention. To support control

5 Conversion of NIR from dollar to rupiah in base money factor was calculated using the exchange rate that has been determined by the IMF of Rp7,000.

of base money, the interest rate on rupiah intervention was raised 8 times during 2001 by a total of 425 bp, from 10.8% in 2000 to 15.13%. Overall, OMOs' position rose from Rp78.9 trillion at the end of 2000 to Rp102.6 trillion. This rise was mainly due to higher rupiah intervention, from Rp28.1 trillion to Rp46.9 trillion during the same period. Meanwhile, the SBI position actually declined by Rp4.3 trillion to Rp55.7 trillion.

During the reporting year, OMOs were generally successful in absorbing excess banking system liquidity as reflected in relatively limited amounts of excess reserves held by the banking system. Efforts in this regard were mainly conducted through SBI auctions; rupiah intervention was used only for fine-tuning. However, in line with Bank Indonesia's intention to not push interest rates too high, efforts since September have emphasized rupiah intervention. This was reflected in smaller placements of SBIs compared with the amounts of maturing SBIs and in rising rupiah intervention (Chart 5.7).

Based on ownership, by the end of 2001 national private banks still dominated SBI ownership with a share of 44.6%, followed by the state banks

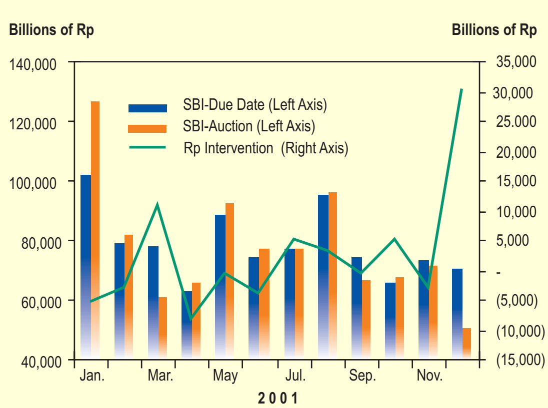


Chart 5.7
SBI Due Date, SBI Auction, and Rupiah Intervention

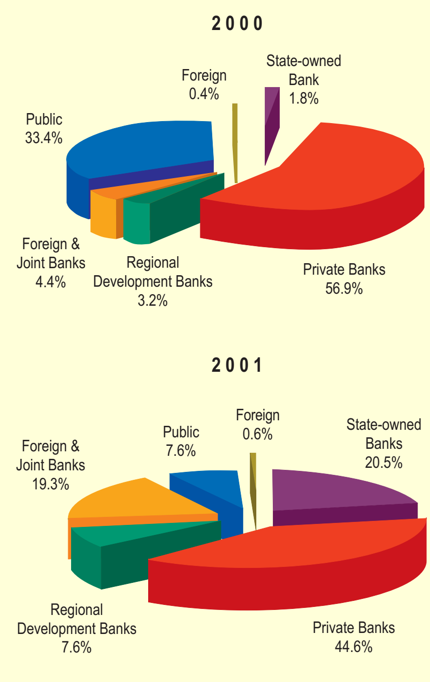


Chart 5.8
SBI Held by Banks and the Public

with 20.5%, the foreign and joint banks with 19.3%, and the regional development banks (BPD) with 7.6% (Chart 5.8). Compared with end-2000, the shares of foreign and joint banks and BPDs rose during 2001. BPDs' larger share was in line with the rise in BPDs' importance to regional governments in the light of decentralization. By contrast, SBI ownership by the public dropped during 2001, from 33.4% to only 7.6% of total SBIs. This was related to the attractive rise in banks' time deposits interest rates during 2001, relative to SBI rates offered by brokers.

Outstanding amounts of Sertifikat Wadiah Bank Indonesia (SWBIs) did not experience any meaningful change during 2001. They only moved within the range of Rp206 billion–Rp304 billion. SWBIs, which began to be issued in February 2000, are certificates issued by Bank Indonesia under sharia principles. Despite this relatively stable position, the SWBI bonus rose from 8.72% at the end of 2000 to 12.43% in line with rising rates on Bank Indonesia's other instruments. The SWBI bonus is calculated on the basis of indicative returns in the sharia interbank money market or mudharabah deposits of the previous month.

INTERBANK MONEY MARKET

During 2001, activity in the rupiah interbank money market increased significantly. The average interest rate rose by 410 bp from 10.46% to 14.56%, while the transaction volume expanded by 39.9% (Table 5.2). These increases occurred in both the morning and afternoon clearings. In the morning interbank money market, the average interest rate rose by 425 bp from 10.67% in 2000 to 14.92%; average transaction volume rose by 61.0%. Similar developments occurred in the afternoon interbank money market where the average interest rate rose by 424 bp to 18.33%.

The rise in transaction volume in the interbank money market during 2001 was indicative of the high short-term liquidity needs of the banking system during 2001. This was particularly the case for foreign and joint banks since Bank Indonesia regulation number 3/3/2001 became effective on 12 January 2001 (concerning Limitations on Rupiah Transactions to Non-Residents and Reduction of The Maximum Limit of Forward Transactions). This condition indicates that bank liquidity management more dependent upon short-term placements, including SBIs and government bonds. Meanwhile, higher interbank interest rates were partly due to rising short-term liquidity needs of banks and Bank Indonesia's efforts to dampen exchange rate volatility by raising interest rates on rupiah intervention.

In line with rising activity in the rupiah interbank market, the average volume of the foreign currency interbank market also rose during 2001, by $12.2 million compared with a year earlier to an average $167.4 million per day. Although the average volume of the foreign currency interbank money market rose in the second half of 2001, it declined again late in the year. This may be the result of a number of upper-tier banks undertaking funds

Table 5.2
Interest Rate and Volume on Daily Interbank Money Market Transactions

Period	Interest Rate (%)				Volume			
	Morning	Afternoon	Overall		Morning	Afternoon	Overall	
			Rupiah	Foreign Currency			Rp (Billions of Rp)	Foreign Currency (Millions of $)
Quarter I - 2000	9.74	9.32	9.50	5.66	1,003.4	708.2	1,712.0	135.5
Quarter II - 2000	10.19	9.87	10.03	6.25	961.5	945.5	1,906.9	149.0
Quarter III - 2000	11.16	10.62	10.89	6.44	1,196.6	1,289.3	2,485.9	177.6
Quarter IV - 2000	11.64	11.21	11.43	6.45	1,340.0	1,470.0	2,810.0	158.9
Average in 2000	**10.67**	**10.25**	**10.46**	**6.20**	**1,125.4**	**1,103.2**	**2,288.0**	**155.3**
Quarter I - 2001	12.76	12.64	12.71	5.49	1,812.0	1,318.0	3,130.0	204.6
Quarter II - 2001	14.72	14.10	14.45	4.06	1,816.0	1,288.0	3,104.0	200.1
Quarter III - 2001	16.14	15.49	15.15	3.34	1,792.0	1,278.0	3,070.0	162.8
Quarter IV - 2001	16.06	15.75	15.93	2.17	1,830.0	1,337.0	3,167.0	102.1
Average in 2001	**14.92**	**14.50**	**14.56**	**3.76**	**1,812.0**	**1,305.0**	**3,118.0**	**167.4**

placement abroad (See Chapter 3 – The Exchange Rate). Volume in the foreign currency interbank money market was dominated by the state, foreign, and joint banks. Meanwhile, the average foreign currency interbank interest rate declined during the review period, by 244 bp to 3.76%. The decline was largely due to a downward trend in offshore interest rates, particularly the Fed Funds rate.

During the reporting year, groups making placements in the rupiah interbank money market were the national foreign exchange banks, the state-owned banks, and the national non-foreign exchange banks (Chart 5.9). This indicated that these three groups of banks have become more liquid. Meanwhile, the foreign and joint banks undertook more borrowings in both the rupiah and foreign currency interbank money markets. Net borrowing by the foreign and joint banks serve three purposes: to meet liquidity needs; to arbitrage the difference between borrowing in the interbank and placements in SBIs; and to fulfill the hedging needs of multinational companies for their rupiah obligations.

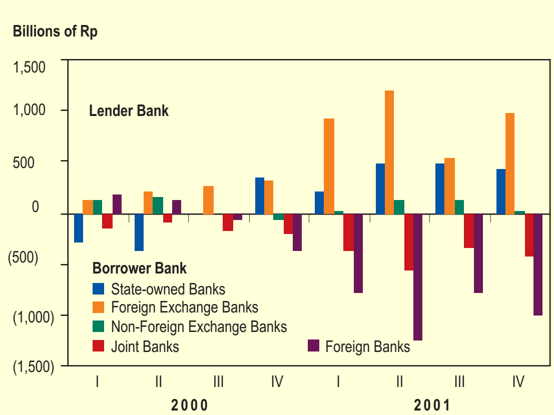


Chart 5.9
Net Lender & Borrower in Interbank Money Market by Group of Banks

INTEREST RATES

In line with efforts to absorb excess liquidity for the purpose of achieving base money target, SBI interest rates rose during 2001. The interest rate on 1-month SBIs rose by 309 bp, reaching 17.62% at the end of December 2001; the 3-month rate rose 332 bp to 17.63%. This rise in SBI rates mainly occurred prior to August 2001. From September through year-end, the rates on 1- and 3-month SBIs were stable in the range of 17.58% – 17.63%. As mentioned earlier (see Open Market Operations), overnight rates on rupiah intervention also increased, mainly in the first half of the reporting year; during the second half of the year, they were steady at 15.13% (Chart 5.10).

Although nominal SBI interest rates rose, real SBI interest rates were lower than in the previous year. At the end of 2001, the real rate on 1-month SBI was 5.07%, down 11 bp from the end of the previous year.

The rise in nominal interest rates on SBIs did not influence time deposit rates in any significant way. This was due to continuing high liquidity in the

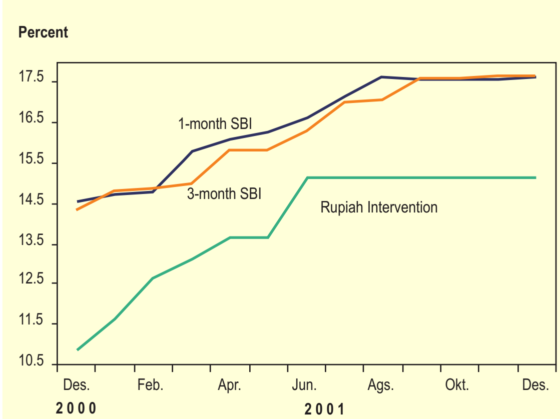


Chart 5.10
SBI and Rp Intervention Rates

banking system as the result of incomplete restoration of the banks' intermediation function. With relatively small amounts of new lending, banks made profits by operating on the spread between SBI and time deposits rates. In order to move time deposits rates in the same direction as SBI rates, Bank Indonesia has changed the margin of the interest rate guarantee twice during 2001, in January and August. On each occasion, it was widened by 100 bp over the time deposits rate of banks that were members of JIBOR. Also, that effort was supported by a policy to change the determination of the guarantee rate from once a week to once a month.

Widening the maximum guaranteed interest rate spread prompted banks to raise their time deposit interest rates during 2001. Compared with the position at the end of 2000, nominal and real time deposit interest rates have risen by 411 bp and 91 bp to 16.07% and 3.52%, respectively (Chart 5.11). This development suggested that efforts to improve the interest rate structure through use of the guarantee spread were quite effective in pulling time deposit rates upward (Chart 5.12).

Other bank interest rates, such as the interest rates on 3-month time deposits, working capital credits, and investment credits also rose during 2001. The interest rate on 3-month time deposits rose by 400 bp to 17.24%; the rate on working capital credit rose by 154 bp to 19.19%; and the rate on investment credit rose by 104 bp to 17.90%, all compared with their positions at the end of December 2000 (Chart 5.13).

Table 5.3
Interest Rate 1)

Item	1999	2000	2001
	In percent		
SBI			
1-month	11.9	14.5	17.6
Interbank Money Market			
O/N	112.1	11.4	15.66
Time Deposit			
1-month	12.2	12.0	16.07
3-month	12.9	13.2	17.24
6-month	14.3	13.2	16.18
12-month	22.4	12.2	15.48
24-month	18.4	14.3	18.05
Credit			
Working Capital	20.7	17.7	19.19
Investment	17.9	16.9	17.90

1) Weighted Average in December

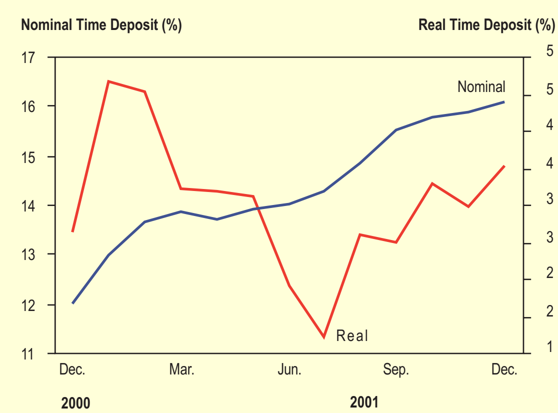


Chart 5.11
1-month Time Deposit Interest Rates

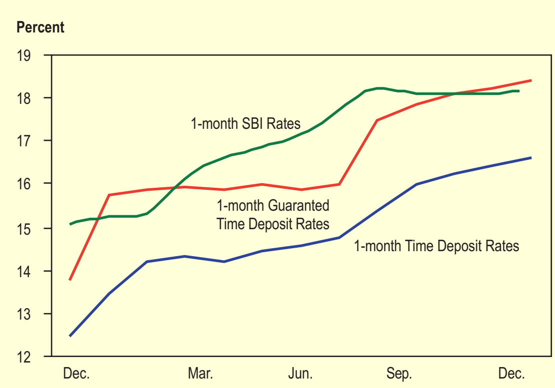


Chart 5.12
SBI and Time Deposit Interest Rates

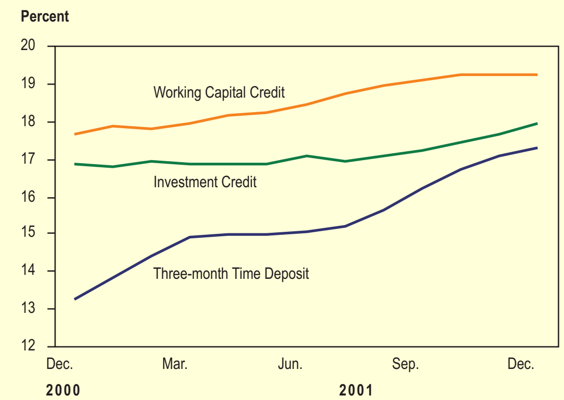


Chart 5.13
Long-term Interest Rates

MONEY SUPPLY

During 2001, narrow money (M1) rose by 9.6%, reaching Rp177.7 trillion by year-end. This rise was mainly due to an expansion in demand deposits of 12.9%; currency, as mentioned above, rose by 5.5%. Viewed by ownership, the growth of demand deposits particularly occurred in regional governments' demand deposits which soared 138.9% (Chart 5.14). This was due to the implementation of certain aspects of fiscal decentralization policy, which began in January 2001, especially general allocation funds and natural resource revenue-sharing transfers. By the end of the year, the regional government current account declined due to payments for on going projects.

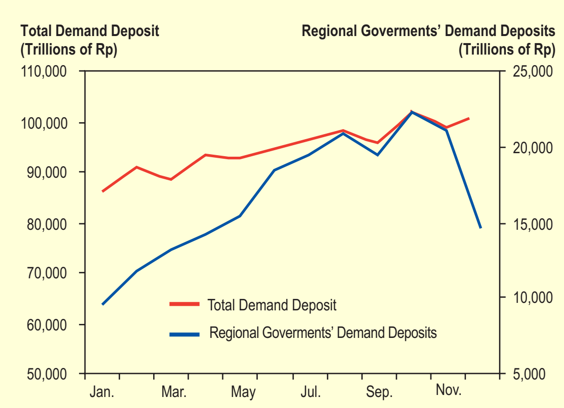


Chart 5.14
Regional Governments' Demand Deposits

During the same period, quasi money rose by 13.9%, reaching Rp666.3 trillion. Viewed by its components, this was mainly accounted for by rupiah quasi money in the form of time deposits that rose by 16.7% to Rp340.9 trillion and savings that rose by 11.8%, reaching Rp170.6 trillion. The higher growth of time deposits compared with saving deposits and demand deposits reflected the shifting of public preference into fund placements of longer-term savings (Chart 5.15). This was related to the rise of time deposit interest rates during the year (Chart 5.16) and improving expectations over future economic prospects. This was markedly different than in 2000,

Table 5.4
Money Supply and Its Affecting Factors

Item	1999	2000	2001	Change 2000-2001
	Outstanding			
	Trillions of Rupiah			
M2	**646.2**	**747.0**	**844.1**	**97.0**
M1	**124.6**	**162.2**	**177.7**	**15.5**
– Currency	58.4	72.4	76.3	4.0
– Demand Deposits	66.3	89.8	101.4	11.5
Quasi Money	**521.6**	**584.8**	**666.3**	**81.5**
– Time and saving deposits in Rupiah	408.6	444.7	511.6	66.9
– Deposits in foreign currency	113.0	140.2	154.8	14.6
Factors Affecting M2	**646.2**	**747.0**	**844.1**	**97.0**
Net Foreign Assets	129.1	210.7	234.0	23.2
– Bank Indonesia	109.3	201.2	192.6	-8.6
– Commercial banks	19.8	9.5	41.4	31.9
Net claims on central government	397.3	520.3	529.7	9.4
Net claims to IBRA	0.0	0.0	0.0	0.0
Claims to business sector	252.6	294.9	329.2	34.2
– Credit in rupiah	140.5	152.5	202.6	50.1
– Credit in foreign currency	84.6	116.5	105.0	-11.5
– Other claims	27.4	25.9	21.6	-4.4
Others (net)	-132.7	-278.9	-248.8	30.2

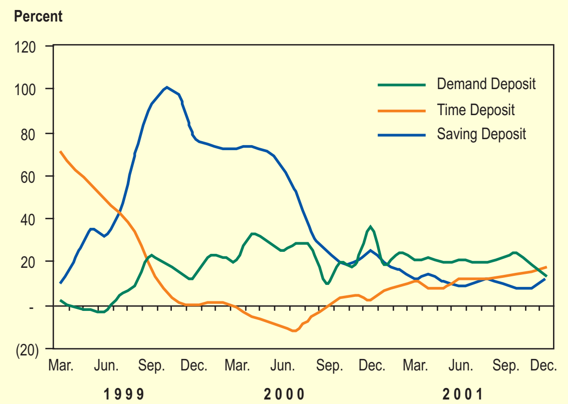


Chart 5.15
Growth of Saving Deposits, Demand Deposits and Time Deposits

when time deposits expanded by only 2.1%, while savings and current account (giro) only grew by 24.4% and 35.5%, respectively.

Meanwhile during 2001, foreign currency deposits rose by 10.4%, reaching Rp154.8 trillion by the end of the year. However, this rise was mainly due to the weakening rupiah exchange rate. If valued in dollars, foreign currency deposits only rose by $270.5 million which is equivalent to Rp2.6 trillion, reaching Rp142.8 trillion by end-2001.

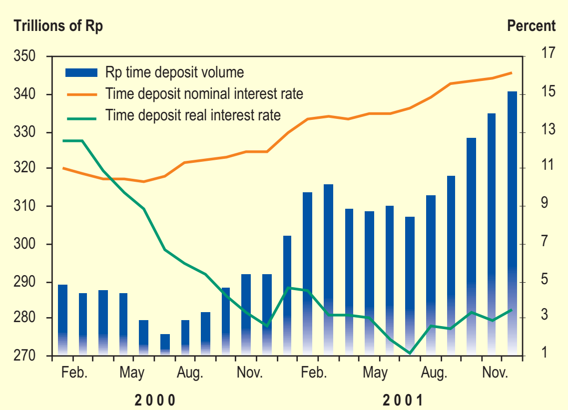


Chart 5.16
Interest Rates and Outstanding Time Deposits

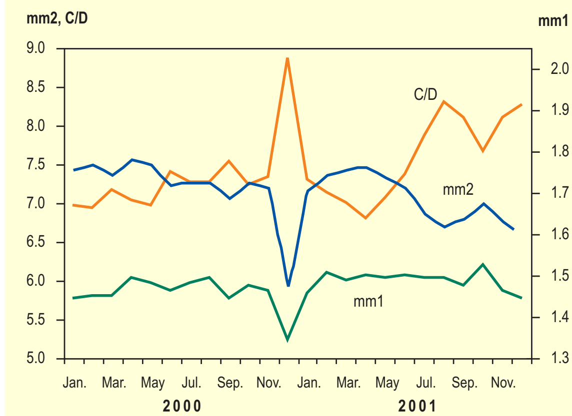


Chart 5.17
Money Multiplier and Ratio C/D

Based on these developments of M1 and quasi money, broad money (M2) expanded by 13.0% during 2001, to Rp844.1 trillion. On average in 2001, M2 grew by 14.7%. This M2 growth was lower than the average growth of M1 during 2001 (19.8%), due to the rapid expansion of currency. This was reflected in a rise in the currency to deposits ratio (Chart 5.17), and in a decline in M2 money multiplier (mm2), to 6.7 by the end of 2001. This was well below the pre-crisis average of 8.0.

Based on the factors that affect M2, expansion during the reporting year was mainly accounted for by net domestic assets (NDA), which increased by Rp73.8 trillion. NDA expansion originated in net claims on business sector (CBS; up Rp34.2 trillion) and net claims on government (NCG; up Rp9.4 trillion).

CBS expansion was due to a rise in rupiah credit of Rp50.1 trillion. By contrast, foreign currency credit and other claims declined by Rp11.5 trillion and Rp4.4 trillion, respectively. The rise in rupiah credit included, among others, credit repurchase by banks from IBRA. Looking at the type of credit, rupiah credit was mainly directed to finance working capital credit for industry and trade sectors, as well as consumption credit. The decline in foreign currency credit was mainly due to the transfer of foreign currency credits by national private banks to IBRA in exchange for hedge bonds and write-offs of foreign currency credits held by the state banks.

NCG expansion was mainly accounted for by NCG expansion from Bank Indonesia in the amount of Rp27.0 trillion; commercial banks' NCG contracted by Rp17.7 trillion. Bank Indonesia's expansion in NCG was, among others, due to general allocation funds, coupon payments on government bonds, payments on foreign debts, term payments on projects, and fuel subsidies (see the discussion of base money). Meanwhile, NCG contraction in commercial banks mainly stemmed from a decline in banks' claims on the government in the form of bonds of Rp22.0 trillion (the payment of government bonds as banks' obligations to IBRA) and from a decline in the market value of government bonds.

Meanwhile, Net Foreign Assets (NFA) rose by Rp23.2 trillion, mainly due to a rise of Rp31.9 trillion in NFA at commercial banks. The rise in NFA at commercial banks mostly stemmed from a decline of Rp24.3 trillion in banks' obligation to non-residents, among others, in the forms of demand deposits and call money of Rp12.4 trillion and Rp7.0 trillion, respectively.

CAPITAL MARKETS

The performance of the stock market in 2001 was marked by fluctuations in the Jakarta Composite Stock Index around a downward trend. The composite index closed the year at 392.0, down 24.285 points (5.83%) compared with the end of 2000 (Chart 5.18). This decline was influenced by both economic and non-economic factors. The main economic factors were: the weakening exchange rate; rising SBI rates; the downgrading of Indonesia's investment rating from "stable" to "negative", according to Moody's at the beginning of March 2001; and weak regional bourses due to uncertainty concerning Japanese and US economic prospects. The main non-economic factor was rising market worry over security and political stability during 2001. Other factors putting further pressure on the composite index were: the 11 September 2001 WTC tragedy, which was followed by anti-US demonstrations in a number of large cities; and downgradings of Indonesia's sovereign credit rating by S&P from CCC+ to CCC and its debt outlook from "stable" to "negative" in week II of November 2001. However, in February and August 2001, the index strengthened for a while, spurred by a decline in US interest rates orchestrated by the Fed, the success of the special session of the People's Consultative Assembly, and the smooth transition of

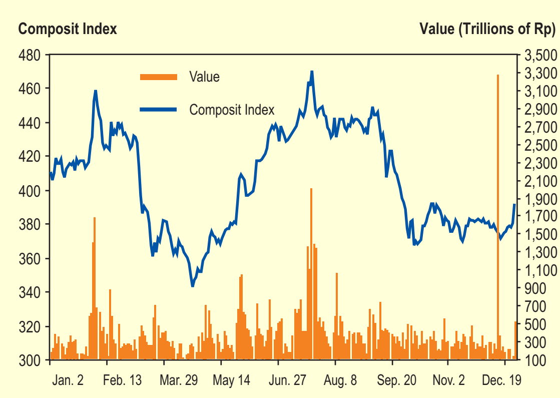


Chart 5.18
Jakarta Composite Stock Index and Market Capitalization

national leadership. These conditions also prompted a rise in the consumer confidence index from 94.1 to 112.3.

Weakness in the composite index in 2001 was also related to declining foreign investors' interest in the Indonesian capital markets. There was a decline in the value of foreign investors' transaction from Rp24.7 trillion (20.1% of total trading) last year to Rp14.6 trillion (9.9%) in 2001. In line with the weakening composite index, market capitalization value declined by 7.8% from Rp259.6 trillion at the end of 2000 to Rp239.3 trillion. Meanwhile, the number of listed companies rose from 347 (with a value of Rp226.1 trillion) to 379 (with a value of Rp231.3 trillion).

In order to improve capital market performance, the government took several steps in 2001. These included a change in the organizational structure of the Capital Market Supervisory Board (Bapepam) and the issuance of permits for a maximum 99% ownership of shares of joint venture companies before public offer to foreign security companies. In order to widen access to the bourse, in November 2001 the government developed a remote, high technology trading system. This effort was also supported by policies concerning the discontinuation of the "immediate market" for efficiency purposes through market simplification. However, the government also imposed a tax on revenue from bonds traded, amounting to 0.03% of the transaction value. This policy was contradictory with the objective of developing the capital market as one of the alternative sources of financing for business.

Unlike the composite index movements, the shares index under the sharia principle (Jakarta Islamic Index) rose from 57.9 at the end of 2000 to 61.4 by end-2001. This index is calculated using the share prices of 30 companies, whose activities are based on Islamic sharia principles.

Meanwhile, in the corporate bond market, the number of issuers rose from 91 (with a value of issuance of Rp28.8 trillion) to 94 (with a value of issuance of Rp31.7 trillion) by end-2001. However, trading in corporate bonds declined in 2001, although trading index rose by 24.9% from 433.8 last year to 541.5 in 2001. The total volume of corporate bond transactions was recorded at Rp1.1 trillion, which is a decline of 87.3% from Rp8.8 trillion in 2000, with trading frequency of 403, down from 2,497 in 2000. The decline in bond trading activities was caused by a shift in investors' investment portfolio interests due

Table 5.5
Volume of Government Bonds Traded in Secondary Market[1)]

	Variable Rate	Fixed Rate	Total
February	6,000	0	6,000
May	61,730	25,650	87,380
June	1,587,188	7,000,000	8,587,188
July	85,740	0	85,740
August	2,788,381	1,053,235	3,841,616
September	2,284,318	418,676	2,702,994
October	797,475	-	797,475
November	5,370,127	2,278,500	7,648,627
December	3,227,200	921,600	4,148,800
2000	**16,208,159**	**11,697,661**	**27,905,820**
January	4,508,000	7,929,500	12,437,500
February	3,357,113	1,064,500	4,421,613
March	1,466,197	1,439,654	2,905,851
April	7,104,770	1,844,500	8,949,270
May	1,387,590	1,518,186	2,905,776
June	2,873,130	5,337,291	8,210,421
July	2,739,751	1,572,920	4,312,671
August	1,701,927	1,578,000	3,279,927
September	1,393,822	2,004,409	3,398,231
October	565,010	2,824,720	3,389,730
November	3,551,644	3,116,753	6,668,397
December	1,779,713	3,563,011	5,342,724
2001	**32,428,667**	**33,793,444**	**66,222,111**
	48,636,826	**45,491,105**	**94,127,931**

1) Millions of Rupiah

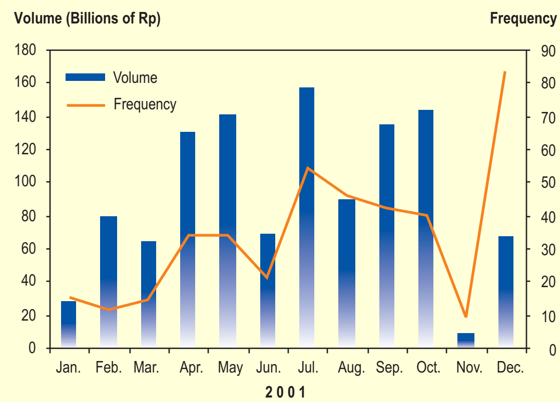


Chart 5.19
Volume of Government Bonds Traded in Secondary Market

to: continuing weak economic conditions; imposition of the transactions tax; the declining value of the rupiah; high inflationary pressures; and rising SBI discount rates.

Developments concerning the trading of government bonds were more encouraging. The volume of government bonds traded in the secondary market in 2001 rose to Rp66.2 trillion from only Rp27.9 trillion in the previous year (Table 5.5). This was in line with rising liquidity needs of several banks that held recapitalization bonds. In order to boost trading in government bonds, the ceiling on government bonds that can be included in the trading portfolio was raised from 25% on 8 December 2000 to 100% on 31 July 2001. Of total government bond trading, fixed rate bonds accounted for Rp33.8 trillion in trading, a bit more than variable rate bonds (Rp32.4 trillion). This was related to investors' motives of seeking higher revenue, as a result of the large discount rate, which reached 35%–50%. Since February 2000, total government bond trading transactions in the secondary market reached Rp94.1 trillion, covering Rp48.6 and Rp45.5 trillion of variable and fixed rate bonds, respectively.

chapter 6 BALANCE OF PAYMENTS

chapter 6

BALANCE OF PAYMENTS

During the year 2001, Indonesia's balance of payments deteriorated appreciably. The current account surplus narrowed due to weaker exports and the deficit on capital account widened. The decline in export performance was related to conditions abroad and inside the country. On the external side, exports declined substantially because of lower prices for main commodities and because of lower world economic growth in export destination countries, which was worsened by the impact of the WTC tragedy on 11 September 2001, particularly for non-oil/gas exports. Export decline was also constrained by the imposition of additional requirements on Indonesia's exports, such as environment-friendly and consumer rights requirements. On the internal side, the decline in exports stemmed from disruptions to production and distribution, which were caused by vigorous labor action, security disturbances, and incomplete restoration in banks' intermediation function. In line with low investment and declining exports, imports also declined, particularly imports of capital goods and raw materials. This decline in imports was also due to the rupiah exchange rate, which depreciated and fluctuated sharply. Meanwhile, the deficit on the services account narrowed due to lower interest payments on offshore debts and declining payments for import-related transportation services.

The wider deficit on capital account mainly stemmed from a deficit on government capital flows, following surpluses of recent years. The deficit on government capital flows was caused by a sharp decline in drawdowns of government offshore debts as a consequence of creditors' requirements not

Table 6.1
Indonesia's Balance of Payments

Item	1999	2000	2001*
	Billions of $		
A. Current Account	**5.8**	**8.0**	**5.0**
1. Merchandise	20.6	25.0	21.6
a. Export f.o.b	51.2	65.4	58.7
Non-oil and gas	41.0	50.3	45.8
Oil and gas	10.3	15.1	12.9
Oil	5.7	8.0	7.2
LNG	4.2	6.8	5.4
LPG	0.4	0.4	0.4
b. Import f.o.b	–30.6	–40.4	–37.0
Non-oil and gas	–26.6	–34.4	–31.4
Oil and gas	–4.0	–6.0	–5.6
Oil	–3.7	–5.8	–5.3
Gas	–0.3	–0.2	–0.3
2. Services	–14.9	–17.1	–16.7
a. Non-oil and gas	–11.7	–12.5	–12.4
b. Oil and gas	–3.2	–4.6	–4.3
Oil	–1.5	–2.2	–2.2
Gas	–1.7	–2.4	–2.1
B. Capital Account	**-4.6**	**–6.8**	**–8.9**
1. Oficial capital movements (net)	5.4	3.2	–0.3
a. Inflows	7.9	5.0	3.3
b. Debt repayment 1)	–2.6	–1.8	–3.6
2. Private capital movement	–9.9	–10.0	–8.6
a. Direct investment (net)	–2.7	–4.6	–5.9
b. Others (net)	–7.2	–5.4	–2.7
C. Total (A+B)	**1.2**	**1.2**	**–3.9**
D. Net Errors and Omissions	**2.1**	**3.8**	**2.6**
E. Monetary Movement 2)	**–3.3**	**–5.0**	**1.4**
Notes:			1.
Gross Foreign Assets (GFA) 3)	27.1	29.4	28.0
equivalent to non-oil and gas imports. and official foreign debt repayments (months)	6.7	6.0	6.1
2. Current account (%)	4.1	5.3	3.4

1) Taking into account the rescheduling & payment to IMF
2) Minus (–) = Surplus, vice versa
3) Since 2000, based on IRFCL concept, replacing GFA concept

having been fulfilled. The deficit on private capital flows narrowed due to lower repayments of private offshore debts.

Indonesia's overall balance of payments was in a deficit of $1.4 billion, causing international reserves at the end of 2001 to slip to $28.0 billion or equal to 6.1 months worth of imports plus government debt payments (Table 6.1).

To cope with the various problems in international trade and capital flows, the government has taken several policy measures. In the export area, the policies were, among others, a reduction in export taxes for several commodities and enhancement of the management system for textile quotas. In line with these policies, export-oriented producers, with support from the government, held several export product exhibitions abroad and in Indonesia. Concerning imports, the government has, among others, eased the import of certain goods in order to facilitate production activities. In the capital flows area, the government has issued an amendment to the stipulation concerning ownership of shares by foreign investors, which permits acquisition of certain domestic companies that have not reached the commercial stage of production.

CURRENT ACCOUNT

During 2001, the current account is estimated to be in a surplus of $5.0 billion or 3.4% of GDP, down from the previous year's surplus of $8.0 billion or 5.3% of GDP (Chart 6.1). This decline in the current account surplus was mainly accounted for by a narrower surplus on merchandise trade. The narrower surplus on trade occurred on both oil and gas and non-oil/ gas accounts; they narrowed by $1.8 billion and $1.6 billion, to $7.3 billion and $14.4 billion, respectively (Chart 6.2). As was the case in the previous years, the services account continued in deficit. In the reporting period, the services account deficit was recorded at $16.7 billion, smaller than the previous year's deficit of $17.1 billion.

In a bid to improve export performance, during the reporting year, the government undertook various policies. Effective 9 February 2001, the export tax on palm oil and crude palm oil was reduced from 5% to

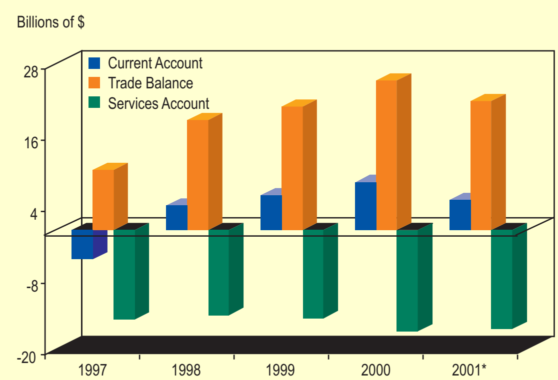


Chart 6.1
Current Account, Trade Balance, and Services Acccount

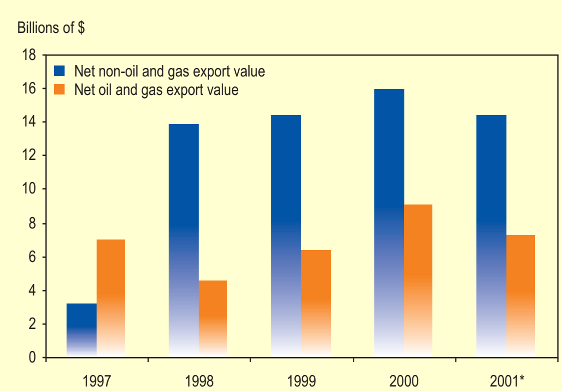


Chart 6.2
Oil and Gas and Non-oil/Gas Export Value (Net)

3%.[1] Also the export tax on crude olein, refined bleached deodorized palm oil, and refined bleached deodorized palm olein was reduced from 2% to 1%. In addition and in a bid to boost exports of textiles and textile products to countries that impose quotas, the government has enhanced the quota management system. These changes make the system more transparent so that quotas can be utilized more efficiently and to increase business certainty for the textile business.[2] Moreover, to promote Indonesia's exports, members of trade missions or exhibitions who represent the government of the Republic of Indonesia, are exempted from the requirement to pay the exit tax (foreign fiscal payment).[3]

Meanwhile, in order to ease the import of goods for domestic production, the government has allowed imports of used machinery and equipment.[4] Furthermore, in order to boost development of the domestic machinery industry, reduction of import duties to 5% is applied on imports of raw materials/ additive materials and parts/components for machinery and rotating motor assemblies.[5]

1 Minister of Finance Decree Number 66/KMK.017/2001 dated 9 February 2001 concerning Determination of Export Tax Tariffs for Palm Oil, Crude Palm Oil, and by-products.

2 Minister of Industry and Trade Decree Number 311/MPP/Kep/10/ 2001 dated 30 October 2001 concerning Stipulation on Export Quotas on Textiles and Textile Products.

3 Government Regulation Number 41 of 2001 dated 28 May 2001 concerning Amendment to Government Regulation number 42 of 2000 concerning Payment of Personal Income Tax Prior to Departure Abroad.

4 Minister of Industry and Trade Decree Number 172/MPP/Kep/5/ 2001 dated 17 May 2001 concerning Imports of Used Machineries and Used Machinery Equipments.

5. Minister of Finance Decree Number 190/KMK.01 dated 16 April 2001 concerning reduction of Import Duties on Imports of Raw materials/ Additives and Parts/Components For Machinery and Rotating Motor Assemblies.

Exports

Conditions in the global economy had a major influence on Indonesia's exports in 2001. The slowdown in the world economy and lower prices for primary commodities (oil and gas and non-oil/gas) in the international market pushed exports down. Total exports in 2001 fell by 10.3% to $58.7 billion. The value of non-oil/gas exports during the reporting year dropped by 9.0% to $45.8 billion; the value of oil and gas exports fell by 14.6% to $12.9 billion (Chart 6.3). Despite these declines, Indonesia's exports, particularly of industrial commodities, was somewhat stronger than those of other Asian countries such as Taiwan, Singapore, Malaysia, and South Korea.

The composition of non-oil/gas exports continued to be dominated by industrial goods which reached 80% of the total; mining and agriculture accounted for 11% and 9%, respectively (Chart 6.4). The contributions of these sectors were little changed from the year before.

In 2001, total exports of industrial goods dropped by 9.7% from the previous year to $36.7

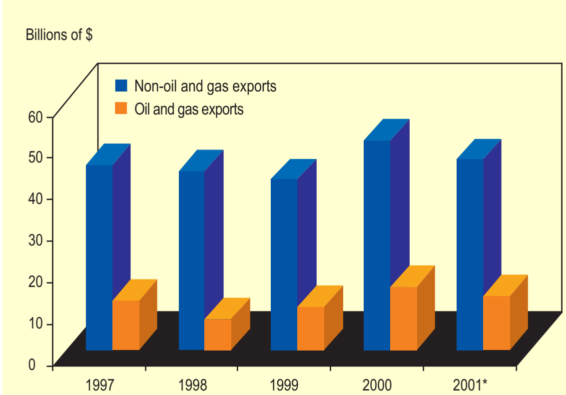


Chart 6.3
Oil and Gas and Non-oil and Gas Value

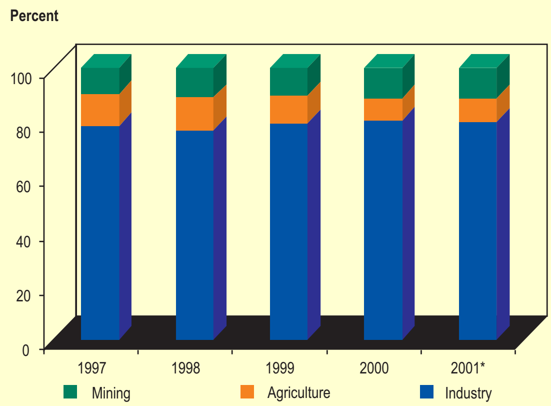


Chart 6.4
Share of Non-oil and Gas Exports

billion (Table 6.2). A drop occurred in several of the main commodities, such as textiles and textile products (-3.7%), wood products (-8.9%), palm oil (-14.9%), paper (-18.8%), as well as machinery and mechanical equipments (-23.5%). In relation to rising demand from countries within the ASEAN region, exports of cement rose by 25.3%.

Table 6.2
Industrial Goods Exports

Item	2000 Growth (%)	2001* Growth (%)	2001* Value (Millions of $)	2001* Share of Growth (%)
Textile & textile products	16.3	-3.7	7,047	15.4
– Garments	17.9	-0.7	4,038	8.8
Handicrafts	-3.6	6.0	581	1.3
Wood and wood products	-0.7	-8.9	4,094	8.9
– Plywood	-11.6	-7.1	1,854	4.0
Rattan products	16.1	-3.6	285	0.6
Palm oil	-7.6	-14.9	1,076	2.3
Copra oil-cake	31.9	-33.8	41	0.1
Chemical products	23.1	3.5	2,338	5.1
Metal products	12.9	-1.7	1,197	2.6
Electrical appliances	89.2	1.3	6,446	14.1
Cement	-1.8	25.3	176	0.4
Paper	15.2	-18.8	2,473	5.4
Rubber product	17.5	-1.7	432	0.9
Glass and glassware	25.1	-14.3	299	0.7
Footwear	6.7	-5.4	1,533	3.3
Plastics products	41.4	-14.1	1,045	2.3
Machinery and Mechanical	104.2	-23.5	2,894	6.3
Others	9.4	-23.8	4,731	10.3
Total	**24.3**	**-9.7**	**36,688**	**80.1**

In the mining sector, exports reached $5.1 billion or down 8.1% compared with the year before. Declines occurred in almost all commodities, especially tin (-5.0%), nickel (-19.0%), and aluminum (-20.5%). On the other hand exports of coal rose by 1.6%.

Agricultural exports dropped by 3.3% to $4.0 billion. Several main commodities declined, including coffee and pepper by 44.6% and 57.0%, respectively. The drop in coffee mainly stemmed from failures in world coffee retention, which caused the selling price to drop.

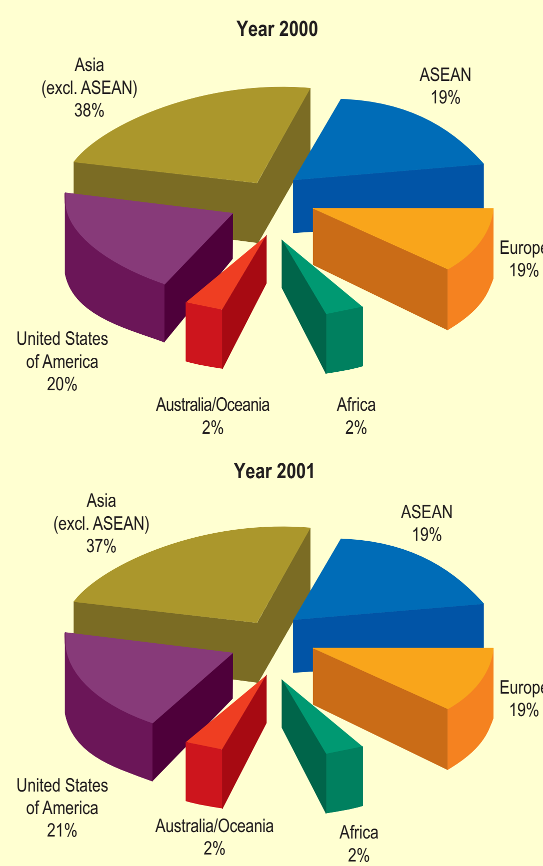


Chart 6.5
Share of Non-oil Gas Exports by Country of Destination

Based on export destination, the shares of exports to countries in the American region reached 21%, Asian (outside ASEAN) 37%, ASEAN and Europe 19% each, as well as Africa and Australia 2% each (Chart 6.5). These shares were little changed from 2000. Specifically, the share of Indonesia's exports to the US was 18%, up somewhat from the previous year. The share of exports to Japan was 16%, virtually unchanged from the previous year.

The drop in oil and gas exports stemmed from lower international prices. During the reporting year, the average price of oil dropped quite sharply to $24.0 per barrel, compared with $28.2 per barrel in 2000. This price drop reflected the continuing impact of production quota increases by OPEC member countries at the end of 2000. Despite declines in OPEC members' production since the beginning of 2001, other factors pushed down prices, including: the re-entry of Iraq into the market with the approval of the United Nations in the framework of oil for food; and rising production by non-OPEC countries. Meanwhile, the prices of LNG and LPG exports also dropped to $4.0 per MMBTU and $282.7 per Mton from the previous year's $4.8 per MMBTU and $291.8 per Mton, respectively. Measured in value terms, oil, LNG, and LPG exports dropped by 9.9%, 20.7%, and 1.1%, respectively. On the volume side, oil and LPG exports rose by 3.3% and 2.9%, while LNG exports dropped 4.5%.

Imports

In line with weaker domestic investment and the drop in exports during the reporting year, imports fell in 2001. Total import value (cif) dropped by 7.8% due to the drop in non-oil/gas imports and oil and gas imports (cif) of 8.0% and 6.6%, respectively.

Table 6.3
Non-oil and Gas Imports by Category of Goods

Item	Value (Millions of $)		Growth (%)		Share of Growth (%)	
	2000	2001*	2000	2001*	2000	2001*
Consumptions goods	2,619	2,708	74.2	3.4	6.8	7.9
Auxiliary goods	26,741	24,481	23.2	-8.5	72.9	71.7
Capital goods	7,727	6,936	33.6	-10.2	20.3	20.3

By category of goods, the decline in non-oil/gas imports stemmed from capital goods and raw materials which fell by 10.2% and 8.5%, respectively; while imports of consumption goods increased slightly, by 3.4% (Table 6.3). Despite quite a large drop in value, the share of raw materials in total non-oil/gas imports remained larger than the other two categories of goods.

The drop in imports of raw materials and capital goods by type of commodity can be seen in Table 6.4 and Table 6.5. Meanwhile, the drop in capital good imports mainly occurred in the locomotive, ship & airplane group and the optical & measuring equipment category of 26.6% and 33.8%, respectively.

Table 6.4
Imports of Raw Material Goods

Item	2000	2001*	2001*	
	Growth (%)		Value (Millions of $)	Share of Growth (%)
Food and beverages manly for industry	8.9	1.2	1,242	3.6
Processed food and beverages	-8.8	-2.5	960	2.8
Primary raw materials	-21.1	-15.0	3,004	8.8
Processed raw materials	34.9	-7.4	15,247	44.7
Primary fuel and lubricants	-13.4	-10.1	15	0.0
Proccessed fuel and lubricants	53.1	28.8	188	0.6
Spare parts and accessories for capital goods	12.3	3.3	1,931	5.7
Spare parts and accessories for transportation equipment	139.3	-24.2	1,894	5.6
Total	**23.2**	**-8.5**	**24,481**	**71.7**

Tabel 6.5
Imports of Capital Goods

Item	2000	2001*	2001*	
	Growth (%)		Value (Millions of $)	Share of Growth (%)
Tractors & agriculture equipments	144.1	-54.0	22	0.1
Handicraft and accessories	-95.8	27.2	0	0.0
Container & storage box	-21.3	29.4	67	0.2
Machinery	23.3	-1.0	4.253	12.5
Generator & electronics	26.8	-0.2	703	2.1
Locomotive, ship, & aircraft	50.8	-26.6	1.325	3.9
Craftsmanship tools	30.5	-1.5	43	0.1
Optical & meansurement devices	57.0	-33.8	427	1.3
Passenger cars	797.4	-28.8	96	0.3
Total	**33.6**	**-10.2**	**6.936**	**20.3**

Viewed by country of origin, Indonesia's imports of non-oil/gas goods mainly came from countries in the Asian and American regions, with a share of around 70% of total non-oil/gas imports

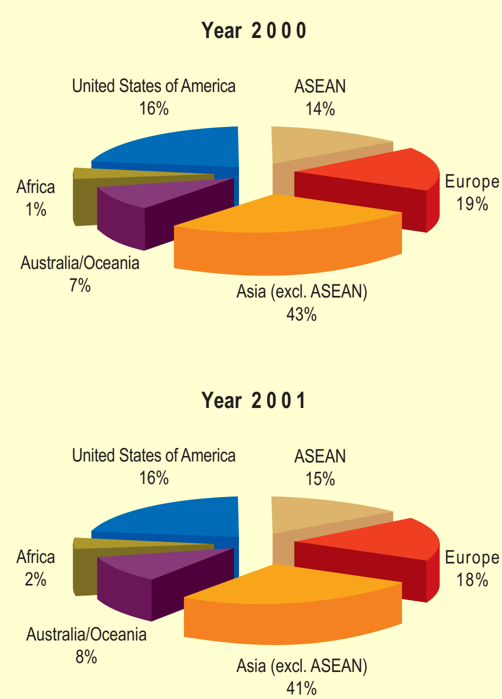


Chart 6.6
Share of Non-oil and Gas Imports by Country of Origin

(Chart 6.6). Compared with the previous year, the share of imports from these countries changed only a little. Specifically, imports from the US and Singapore in 2001 came to 12% and 8%, respectively, unchanged from the year before. Meanwhile, the share of imports from Japan declined to 17%.

Services

During reporting year, the services account remained in deficit, although narrower than in 2000. The deficit amounted to $16.7 billion, $380 million less than 2000. The narrower deficit stemmed from declines in oil and gas services of $241 million and in non-oil/gas services of $139 million. The narrower deficit for the oil and gas services sector was accounted for by freight and non-freight services, whose deficit shrank to $0.5 billion and $3.8 billion, respectively, due in part to lower oil and gas imports. In the non-oil/gas sector, the deficit in freight services dropped to $2.7 billion as a result of the decline in non-oil/gas import activities. Meanwhile, the deficit on non-freight services was $9.7 billion, down slightly from $9.8 billion in the previous year. This was mainly related to lower private offshore debts and a decline in international interest rates.

On the revenue side of non-oil/gas services, the largest source of foreign currency still came from the tourism sector, followed by transfers of Indonesian workers' incomes. Net foreign currency revenue from the tourism sector was recorded at $5.0 billion, slightly higher than that in the previous year. Meanwhile, the number of foreign tourists visiting Indonesia during 2001 reached 5.0 million people. The number was little changed from 2000, and it was a lower than government target (set at the beginning of 2001) of

5.4 million people. As was the case in the previous year, Denpasar, Medan, Batam, and Jakarta remained the main arrival gateways for international tourism.

CAPITAL ACCOUNT

During 2001, the deficit on capital account widened due to the balance on official capital swinging into deficit, following surpluses in the last four years. Private capital flows remained in deficit.

In 2001 government capital flows recorded a deficit of $0.3 billion, after a surplus of $3.2 billion in the previous year. The deficit was due to low drawdowns of program and project loans from the ADB, IBRD, and JBIC. During the reporting year, program loans recorded $0.5 billion, down sharply by $0.9 billion in 2000. Meanwhile, project loans are estimated to rise a bit to $2.5 billion, originating in non-ODA loans of $0.2 billion.

The main constraint on drawdowns was requirements set by donors that could not be met. These concerned government policies, regulations and laws, such as the anti-money laundering law, the law concerning electricity, and regulations in the water resources area. Another factor adding to the deficit was the first repayment of loans from the IMF.

The deficit on private capital flows was $8.6 billion, $1.4 billion narrower than the year before. This narrower deficit was due to a decline in payments for private offshore debts, particularly in the direct foreign investment sector, from $7.5 billion in 2000 to $5.2 billion in 2001. Net outflows of portfolio investment declined from $1.9 billion to $1.4 billion. With these developments, net capital flows recorded a deficit of $8.9 billion or up 31.7% relative to the deficit in the prior year.

Table 6.6
Indonesia's Outstanding Foreign Debt

Item	1999	2000	2001			
			Mar	Jun	Sept	Dec*
	Millions of $					
Government	75,862	74,916	71,980	72,496	75,185	71,403
Private	72,235	66,777	66,335	66,405	62,594	59,841
Bank	10,836	7,718	7,848	7,684	6,564	6,537
Non-bank	58,243	56,888	56,409	56,845	54,446	51,666
- Foreign Investment	29,805	30,264	29,445	28,731	27,888	26,381
- Domestic Investment	28,438	26,624	26,964	28,114	26,558	25,285
Securities	3,156	2,171	2,078	1,876	1,584	1,638
Total	148,097	141,693	138,316	138,901	137,778	131,244

In a bid to give incentives to foreign investors, the government issued a regulation that enables foreign investors to acquire certain domestic companies that are not yet at the commercial stage of production.[6] This regulation is expected to attract more interest from foreign investors.

Meanwhile, Indonesia's total offshore debt at the end of 2001 dropped 7.4%, to $131.2 billion relative to the end of 2000 (Table 6.6), reflecting a drop in both private and government foreign debts. The drop in private foreign debts was due to payments on loans coming due. The drop in government foreign debts was due to loans coming due and to the depreciation of the Japanese Yen against the US dollar. The impact of the depreciation of the Japanese Yen on government foreign debt was quite substantial, considering the share of government debts denominated in Japanese Yen reached around 33% of total government foreign debts.

The share of government foreign debts reached 54% of total foreign debts, while the shares

6 Government Regulation Number 83 of 2001 dated 19 December 2001 concerning Amendment to Government Regulation number 20 of 1994 concerning Share Ownership in Companies Established Under the Foreign Direct Investment Scheme.

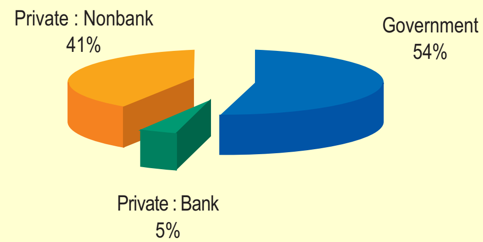


Chart 6.7
Foreign Debt

of private non-bank debts (including marketable securities) and private banks debts were recorded at 41% and 5%, respectively (Chart 6.7). Although government foreign debts are larger than private foreign debts, the repayment terms are easier, in terms of the interest rate and maturity period.

During 2001, government foreign debt dropped by $3.5 billion. Of the total of government foreign debt, $29.1 billion constituted multilateral debts, $22.7 billion constituted bilateral debts, $14.9 billion was in the form of export credit facilities, $439.2 million was leasing debts, $2.3 billion was commercial debts, and $2.0 billion was in the form of marketable securities owned by foreign investors.

Private foreign debt at the end of the reporting year stood at $59.8 billion, down 10.5% from the end of the previous year. Of total private debt, $6.5 billion comprised private bank debts, $51.7 billion comprised private non-bank debts, and $1.6 billion was in the form of marketable securities owned by foreign investors.

Viewed from the timing of repayments, short-term foreign debts falling due through December 2002 are estimated at $25.2 billion or 19.2% of Indonesia's total foreign debts (Table 6.7). That amount comprised government and private debts, including banks, of $7.6 billion and $17.5 billion, respectively; the remainder, amounting to $106.1 billion, comprised debts with more than one-year before maturity. Of the total of private short-term debts of $17.5 billion, $1.2 billion or 6.9% comprised bank debts and $16.3 billion or 93.1% comprised private non-bank debts. Private non-bank short-term debts of up to one year (original) maturity, reached $6.6 billion or 40% of the total; $9.8

Tabel 6.7
Foreign Debt by Maturity as of December 2001*

No	Maturity	Government[1]	Private								Total
			Bank	Nonbank						Total Private	
				Foreign Investment	Non-Bank Financial Ins't	Domestic Invest-ment	SOEs	Private[4] Enter-prises	Total Nonbank		
		Millions of $									
1	**Total Short-Term**	**7,609.6**	**1,211.3**	**6,955.0**	**532.0**	**4,125.0**	**828.0**	**3,898.6**	**16,338.6**	**17,549.9**	**25,159.5**
	- Original Maturity[2]	49.6	84.3	2,098.7	199.0	1,655.7	115.3	2,490.6	6,559.3	6,643.6	6,693.2
	- Remaining Maturity	7,560.0	1,127.0	4,856.3	333.0	2,469.3	712.7	1,408.0	9,779.3	10,906.3	18,466.3
2	**Medium & Long term[3]**	**63,793.4**	**5,325.4**	**19,426.2**	**387.2**	**9,322.9**	**3,546.7**	**4,282.3**	**36,965.3**	**42,290.7**	**106,084.0**
	Total	**71,403.0**	**6,536.7**	**26,381.2**	**919.2**	**13,447.9**	**4,374.7**	**8,180.9**	**53,303.9**	**59,840.6**	**131,243.6**

1) Figures after Paris Club II and London Club
2) Up to one year
3) More than one year
4) Including domestic securities

billion or 60% comprised short-term debts that originated in long-term debts falling due through December 2002 (remaining maturity).

Based on economic sectors being financed, manufacturing was the largest economic sector being financed by foreign debts, reaching $30.8 billion or 23.5% of total foreign debts. The second largest was the financial, leasing, and corporate services sector, reaching $26.5 billion or 20.2% of total foreign debts. Following that was the electricity, gas, and clean water sector, amounting to $13.5 billion or around 10.3% of total foreign debts. Compared with the year before, the largest economic sector financed by foreign debts shifted from the financial, leasing, and corporate services sector to the manufacturing sector.

Viewed by creditor country, Japan constituted the largest creditor with total outstanding loans reaching $41.3 billion or 31.5% of total foreign debts. The US came second with total outstanding loans reaching $13.3 billion or 10.1%, followed by Germany, the Netherlands, and Britain with total outstanding loans of $7.6 billion (5.8%), $7.4 billion (5.6%), and $4.2 billion (3.2%), respectively. Meanwhile, international institutions such as the IBRD, IMF, and ADB constituted the largest institutional lenders with total outstanding loans reaching $11.5 billion (8.8%), $9.1 billion (6.9%), and $7.3 billion (5.6%), respectively.

Of total foreign debts of $131.2 billion, $85.5 billion or 65.2% was recorded in US dollars; $26.5 billion or 20.2% in Japanese Yen; $9.3 billion or 7.1% in SDRs; $7.1 billion or 5.4% in Euros; $1.2 billion or 0.9% in pounds sterling; and the remainder in several other foreign currencies.

With regard to debt restructuring, the reporting period was marked by rising uncertainty over the government foreign debt restructuring process. This concerned slow settlement of the Paris Club phase II debt rescheduling (1 April 2001 up to 31 March 2002) of $2.7 billion due to delays in the agreement over the Letter of Intent between the IMF and the government of the Republic of Indonesia. One of the reasons for the delay was shortfalls vis-à-vis the target for the privatization of state-owned enterprises, asset recoveries by IBRA, and the amendment by Parliament of the law concerning the central bank.

In the banking sector, out of total restructured debts through the Offer I and II of the Interbank Debt Exchange Program of $6.3 billion (consisting of Exchange Offer I of $3 billion and Exchange Offer II of $3.3 billion), $2.9 billion has been repaid by banks through payments, in accordance with determined schedules (repayments), as well as prepayments and buybacks. Up to 2001, repayments of Exchange Offer I and II amounted to $2.1 billion, prepayments amounted to $457.0 million, and buybacks amounted to $346.2 million. Outstanding principal on Exchange Offer I and II amounted to $284.4 million and $3.1 billion, respectively, totaling $3.4 billion.

Meanwhile, the settlement process of private foreign debt restructuring generally proceeded slowly. Up to the end of the review year, only 68 corporations reported to Bank Indonesia as having completed restructuring of their foreign debts with a total value of around $4.1 billion. Compared with the total of delinquent corporate foreign debts of around $30 billion (estimated by the Jakarta Initiative), the amount of restructured foreign debt was small, at only around 13.7%. In general, the slow restructuring process was caused by technical factors, such as the lengthy time spent negotiating terms and conditions. There were disagreements over terms and conditions offered by the creditors and the conditions of companies' cash flow, as well as difficulties in accommodating the various interests of the many parties involved in the restructuring process, particularly in the case of syndicated loans. This slow restructuring process was also influenced by exchange rate fluctuations, which were difficult to predict, and which complicated projections of companies' cash flow.

Various unsettled basic problems in the external sector caused various debt indicators (criteria commonly used by the World Bank) to deteriorate during 2001 (Table 6.8). The ratio of debt payments to exports was 39.4%; the ratios of total debt to exports and GDP were 194.5% and 90.3%, respectively. These were indicative of the continuing heavy burden of foreign debts and the on-going dependency of Indonesia's economy on offshore sources of financing.

Tabble 6.8
Foreign Debt Indicators

Indicator	1997	1998	1999	2000	2001*	World Bank Criteria
	Percent					
DSR	44.5	57.9	56.8	41.1	39.4	20.0
Outstanding debt/ Exports	207.3	261.8	252.1	191.0	194.5	130–220
Outstanding debt/ GDP	62.2	146.3	105.0	92.8	90.3	50–80

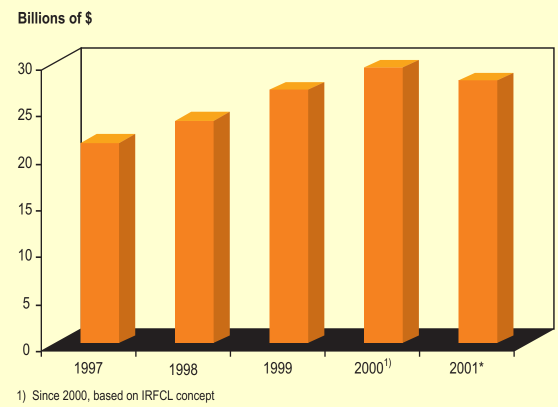


Chart 6.8
International Reserves

INTERNATIONAL RESERVES

In light of the overall balance of payments deficit of $1.4 billion, total official international reserves at the end of 2001 slipped to $28.0 billion or equivalent to 6.1 months of imports plus government foreign debt payments (Chart 6.8).

chapter 7 GOVERNMENT FINANCE

chapter 7

GOVERNMENT FINANCE

Government finance came under heavy pressure during the first few months of 2001. There were three main causal factors. First, a worsening macroeconomic environment, particularly the weaker exchange rate and higher interest rates on Sertifikat Bank Indonesia/SBIs (Bank Indonesia Certificates). Second, the postponement or limited implementation of several fiscal policies, such as the imposition of value added tax on several strategic commodities and price hikes of all fuel products, on average, by 20%. And third, the delay or cancellation of drawdowns of program loans for supporting development financing.

These unfavorable developments threatened the 2001 state budget, partly by swelling the budget deficit. To cope with this possibility, the government made several adjustments by revising the budget through the Policy on the 2001 State Budget Adjustment Package. Several basic assumptions used in development of the 2001 state budget, such as economic growth, the rupiah exchange rate, and the interest rate on 3-month SBIs were updated to more realistic estimates (Table 7.1). In addition, the government made various policy adjustments to government revenues and expenditures, as well as budget financing. With these adjustments, the deficit target remained consistent with medium and long-term economic policies (the National Development Program/ Propenas and the Long-term Economic Development Guidelines/GBHN), and the deficit was contained to the original 3.7% of GDP.

Proposals for adjustments in government revenues included : (a) a rise in the rate of value added tax from 10% to 12.5%; (b) a canvassing program for payers of value added tax, aimed at retail traders with turnover above Rp360 million per year; (c) higher retail prices of tobacco products; (d) efforts to achieve a 50% pay out on dividends of state-owned enterprises for fiscal year 2000 and (e) settlement of delinquent loans of regional governments that had budget surpluses from regional balancing funds.

On the expenditure side, the proposals included : (a) reduction of personnel expenditures by accelerating the process of transferring central government personnel to regional governments; (b) lowering fuel subsidies by fuel price hikes; (c) reduction of electricity subsidies by raising basic electricity tariffs; (d) rationalization and focusing of budget

Table 7.1
Basic Assumptions for the 2001 State Budget

Assumption	2000	2 0 0 1		
	Budget 1)	Budget	Budget R)	Budget P)
Nominal GDP (trillions of rupiah)	988.3	1,425.0	1,468.1	1,476.2
Economic growth (%)	4.9	5.0	3.5	3.5
Inflation rate (%)	8.33	7.20	9.30	11.90
Crude oil price ($/barel)	29.2	24.0	24.0	24.6
Oil production (millions of barrels/day)	1.4	1.5	1.5	1.3
Exchange rate (Rp/$)	8,774	7,800	9,600	10,219
Average 3 months SBI rates (%)	12.70	11.50	15.00	16.40

1) State budget (unaudited), period of April 1 to December 31, 2000
R) State budget (revised)
P) State budget (provisional realization)
Source : Ministry of Finance

allocation for development expenditures; and (e) keeping the allocation of regional balancing funds, originating frrom revenue sharing and general allocation funds in accordance with the original plan.

On the financing side, policy adjustments covered the issuance of government bonds (which the regional governments with surplus balancing funds would buy), and the optimization of drawings from the pipeline of program loans.

Despite these revisions, budgetary implementation still faced difficult challenges, particularly on financing and expenditure, as reflected in the estimated realization figures for the 2001 revised state budget.[1] On budget financing, offshore loans withdrawals are estimated to be 24.5% below target, while on the expenditure side, payments for fuel subsidies are estimated to be 27% above target. The low drawings on offshore loans was mainly attributed to delays in release of loans by aid donors. These delays were due to unfulfilled policy actions that were prerequisites for drawings on the program loans, as well as the short time available for project implementation following revision of the budget. Meanwhile, high spending on fuel subsidies—despite the government having raised fuel prices by an average of 30%— were mainly the result of: i) higher total fuel consumption than originally estimated, and ii) adjustment for under-payments of subsidies in 2000, in accordance with the results of an audit conducted by the Finance and Development Supervisory Agency (BPKP).

These problems in expenditure and financing had a significant effect on government liquidity management during 2001. Shortfalls in drawdowns of offshore loans forced cutbacks in development spending, while the high allocations for fuel subsidies limited the availability of rupiah counterpart funds for projects financed from offshore loans.

Outside these problem areas, it should be noted that the government succeeded in realizing its target for several important accounts in the state budget. On the revenue side, tax revenues met their target and the tax ratio rose appreciably compared with the previous year, from 11.7% to 12.5% of GDP. On the financing side, sales of assets under the bank restructuring program (asset recovery) even exceeded their target, despite various challenges in implementation. On the expenditure side, the government fulfilled its responsibilities concerning non-discretionary expenditures, such as personnel expenditure, interest payments, subsidies, and regional balancing funds.

Overall, government revenues and expenditures exceeded their targets by similar percentages, namely 4.8% and 4.2%. Consequently, the deficit on government financial operations in 2001 is estimated at Rp54.7 trillion or 3.7% of GDP, virtually identical to the planned deficit of Rp54.3 trillion (3.7% of GDP) in the 2001 revised state budget.

In relation to aggregate demand, government spending rose in comparison with last year, from 10.8% to 11.9% of GDP. This rise was mainly contributed by the transfers of funds to regional governments in the form of regional balancing funds. Most (65%) of government spending was in the form of consumption expenditure; the remainder was investment spending. Meanwhile, transfers to the

1 Approved by enactment of Law number 1 of 2002 dated 7 January 2002.

Table 7.2
Government Revenues and Grants 2001*

Item	2000[1)]		2001				
			Budget[2)]		Realization[3)]		
	Trillions of Rp	% of GDP	Trillions of Rp	% of GDP	Trillions of Rp	% of Budget[R]	% of GDP
A. Goverment Revenues and Grants	**204.9**	**20.7**	**286.0**	**19.5**	**299.9**	**104.8**	**20.3**
I. Domestic Revenues	**204.9**	**20.7**	**286.0**	**19.5**	**299.8**	**104.8**	**20.3**
1. Tax Revenues	**115.8**	**11.7**	**185.3**	**12.6**	**184.7**	**99.7**	**12.5**
a. Domestic Taxes	**108.8**	**11.0**	**174.3**	**11.9**	**174.2**	**100.0**	**11.8**
i. Income tax	57.1	5.8	95.0	6.5	92.8	97.7	6.3
1. Oil and gas	18.7	1.9	25.7	1.8	23.1	89.8	1.6
2. Non-oil and gas	38.4	3.9	69.2	4.7	69.7	100.6	4.7
ii. Value added tax	35.0	3.5	53.5	3.6	55.8	104.5	3.8
iii. Land tax and building	3.5	0.4	5.1	0.3	4.8	94.2	0.3
iv. Duty on land and building transfer (BPHTB)	0.9	0.1	1.2	0.1	1.5	124.6	0.1
v. Excise duties	11.3	1.1	17.6	1.2	17.6	100.1	1.2
vi. Other taxes	0.9	0.1	1.9	0.1	1.7	86.2	0.1
b. International Trade Taxes	**7.0**	**0.7**	**11.0**	**0.7**	**10.5**	**95.8**	**0.7**
i. Import duties	6.7	0.7	10.4	0.7	9.8	94.5	0.7
ii. Export tax	0.3	0.0	0.6	0.0	0.7	118.6	0.0
2. Non-tax Revenues	**89.2**	**9.0**	**100.7**	**6.9**	**115.1**	**114.3**	**7.8**
a. Natural Resource Revenues	**76.0**	**7.7**	**79.4**	**5.4**	**86.7**	**109.1**	**5.9**
i. Oil	51.0	5.2	57.9	3.9	60.0	103.8	4.1
ii. Gas	15.7	1.6	17.4	1.2	21.8	125.8	1.5
iii. Mining	0.6	0.1	0.9	0.1	1.6	175.3	0.1
iv. Forestry	8.8	0.9	3.0	0.2	3.0	100.0	0.2
v. Fishery	0.0	0.0	0.3	0.0	0.1	50.0	0.0
b. Profit Transfer from SOEs	**3.9**	**0.4**	**9.0**	**0.6**	**10.4**	**116.0**	**0.7**
c. Other non-tax revenues	**9.3**	**0.9**	**12.3**	**0.8**	**18.0**	**146.4**	**1.2**
II. Grants	**-**	**-**	**-**	**-**	**0.0**	**-**	**0.0**

1) State budget (unaudited), period of April 1 to December 31, 2000
2) State budget (revised)
3) State budget (provisional realization)
Source : Ministry of Finance and Bank Indonesia (processed)

private sector rose quite sharply from 6.4% to 10.0% of GDP owing to payments of subsidies and interest on domestic loans.

In relation to monetary developments, government financial operations contributed to a net expansion of the money supply amounting to the equivalent of 3.8% of GDP in 2001, up from last year's 3.3% of GDP. As financing, there were net foreign inflows equivalent to 3.3% of GDP, down from last year's 4.7% of GDP. Hence, during 2001 there was negative financing amounting to Rp7.6 trillion or the equivalent of 0.5% of GDP.[2]

GOVERNMENT REVENUES AND GRANTS

The realization of government revenues and grants is estimated to reach Rp299.9 trillion or 4.8% above the target set in the revised state budget (Table 7.2). This total is equivalent to 20.3% of GDP, a bit lower compared with year 2000 when it reached 20.7%. The largest source (61.6%) of total revenues continued to be tax revenues of Rp184.7 trillion. With this achievement, the tax ratio reached 12.5% of GDP

2 The negative overall balance equal to is, the difference between total expenditures and total revenues.

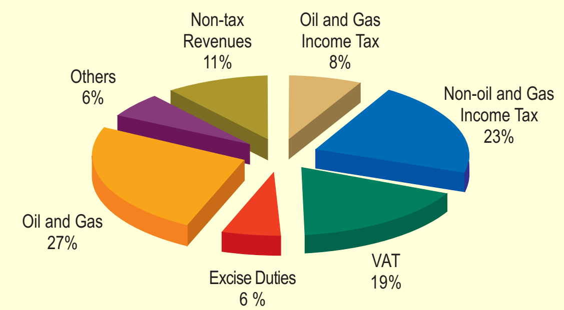


Chart 7.1
Composition of Government Revenues

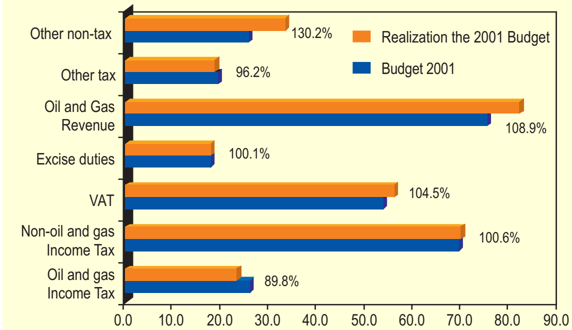


Chart 7.2
Realization of Revenues Target

or almost the same as its budget target of 12.6% of GDP. Collection of tax revenues was fuelled by non-oil/gas tax revenues; oil and gas taxes were below target. The main non-oil/gas tax revenues were income tax and value added tax. For their part, non-tax revenues contributed Rp115.1 trillion or 14.3% above their target, most of which stemmed from oil and gas revenues.

On an individual component basis, the largest sources of government revenues was non-oil/gas income tax and the value added tax, which contributed Rp69.7 trillion (23.2% of the total, or 4.7% of GDP) and Rp55.8 trillion (18.6% of the total or 3.8% of GDP), respectively. The contributions of these components to total government revenues during 2001 were higher than in 2000 when contributions were only 18.8% (3.9% of GDP) and 17.1% (3.5% of GDP), respectively. These higher revenues were mainly accounted for by an increase in the tax rate on interest earned from time/saving deposits and SBI holdings from 15% to 20%, broadening the income tax base and a stronger collection effort; revocation of certain exemptions from value added tax and tax on luxury goods; and optimization of the taxpayer canvassing program, particularly on retail traders whose turnover was above Rp360 million per year.

Among non-tax revenues, the largest portion (27.3%) accrued from the oil and gas sector, in total Rp81.9 trillion, which is equivalent to 5.6% of GDP. This contribution was lower than in 2000 (when it was 32.5% of the total, or 6.8% of GDP), owing to a drop in average production of crude oil, from 1.5 million barrels to 1.3 million barrels per day. However, despite this drop in production, oil and gas revenue in 2001 exceeded their target, due to a weaker exchange rate and receipt of back payments for oil revenues from part of 2000.

Several other revenue accounts—which were generally quite small-were well below target, including import duties and other taxes. Low revenues from import duties was partly due to lower import tariffs, particularly for commodities related to the international agreement based on Law Number 10 of 1995 Concerning Customs. The low revenue from other taxes was attributed in part to a low number of transactions that required duty stamps.

GOVERNMENT EXPENDITURES

Realization of government expenditures, as reflected in central government expenditures and regional balancing funds, was estimated to reach Rp354.6 trillion or 4.2% above target (Table 7.3). This total was equivalent to 24.0% of GDP, up from 23.3% in 2000. Government expenditure was dominated by central government routine expenditures, which amounted to Rp232.8 trillion (65.7% of total expenditures) and equivalent to 15.8% of GDP. Meanwhile, development expenditures reached Rp39.4 trillion (11.1% of total expenditures), equivalent to 2.7% of nominal GDP. The remainder, Rp82.4 trillion (23.2% of the total, equivalent to 5.6% of nominal GDP) was used for regional balancing funds. Compared with their targets, central government routine expenditures and regional balancing funds are estimated at 107.9% and 101.1% of target, respectively. Development expenditures is estimated to reach only 91.4% of its target.

Viewed from its components, most (84.3%) of government expenditures was for non-discretionary items, such as interest payments, subsidies, regional balancing funds, and personnel expenditure with allocations of funds of 26.9%, 23.0%, 23.2%, and 11.2%, respectively. Spending on these items was 106.7%, 123.1%, 101.1%, and 103.5% of their budgeted amounts. The high spending for interest was due to the rise in SBI interest rates and the exchange rate depreciation. The high expenditure for subsidies was caused by a sharp rise in domestic fuel consumption (from 52.8 million kilolitres to 56.6 million kilolitres); the exchange rate depreciation; and adjustments for underpayments of subsidies in 2000 that amounted to Rp5.6 trillion, in accordance with the results of audit conducted by the Finance and Development Supervisory Agency (BPKP). Low development spending was the result of low drawings on government offshore loans.

In the light of fiscal decentralization from the center to the regions (regional autonomy), the government allocated almost 23.2% of its total spending for regional balancing funds. In general and despite various challenges in decentralization, implementation of regional autonomy went according to the budgetary targets. The largest allocation was for general allocation

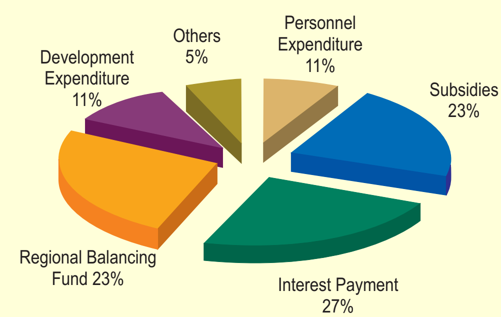


Chart 7.3
Composition of Government Expenditures

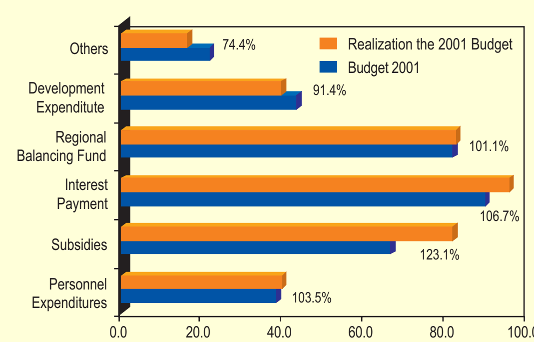


Chart 7.4
Realization of Expenditure Targets

Table 7.3
Government Expenditures 2001*

Item	2000[1)]		2001				
			Budget[2)]		Budget[3)]		
	Trillions of Rp	% of GDP	Trillions of Rp	% of GDP	Trillions of Rp	% of Budget[R]	% of GDP
B. Government Expenditures	**219.9**	**22.3**	**340.3**	**23.2**	**354.6**	**104.2**	**24.0**
I. Central Government Expenditures	**187.1**	**18.9**	**258.8**	**17.6**	**272.2**	**105.1**	**18.4**
1. Current Expenditures	**161.4**	**16.3**	**215.8**	**14.7**	**232.8**	**107.9**	**15.8**
a. Personnel Expenditures	**29.4**	**3.0**	**38.2**	**2.6**	**39.5**	**103.5**	**2.7**
i. Salaries and Pensions	24.3	2.5	31.9	2.2	33.3	104.3	2.3
ii. Rice Allowances	1.5	0.2	1.3	0.1	1.3	98.3	0.1
iii. Food Allowances	1.8	0.2	2.1	0.1	2.1	100.0	0.1
iv. Other Domestic Personnel Expenditures	1.5	0.1	1.4	0.1	1.8	133.5	0.1
v. Overseas Personnel Expenditures	0.3	0.0	1.5	0.1	1.1	69.9	0.1
b. Material Expenditures	**8.1**	**0.8**	**9.9**	**0.7**	**9.6**	**96.9**	**0.7**
i. Domestic	8.0	0.8	8.7	0.6	8.7	100.0	0.6
ii. External	0.1	0.0	1.2	0.1	0.9	74.0	0.1
c. Interest Payment	**50.1**	**5.1**	**89.6**	**6.1**	**95.5**	**106.7**	**6.5**
i. Domestic interest	31.2	3.2	61.2	4.2	66.3	108.3	4.5
ii. Foreign interest	18.8	1.9	28.4	1.9	29.3	103.1	2.0
d. Subsidies	**62.8**	**6.4**	**66.3**	**4.5**	**81.6**	**123.1**	**5.5**
i. Oil subsidies	53.6	5.4	53.8	3.7	68.4	127.2	4.6
ii. Non-oil subsidies	9.1	0.9	12.5	0.9	13.2	105.6	0.9
- Rice (BULOG)	2.2	0.2	2.4	0.2	2.7	110.6	0.2
- Electricity	3.9	0.4	4.7	0.3	4.6	97.7	0.3
- Credit Program	2.4	0.2	4.9	0.3	4.9	100.0	0.3
- Others	0.6	0.1	0.4	0.0	1.0	237.5	0.1
e. Other Current Expenditure	**11.0**	**1.1**	**11.8**	**0.8**	**6.5**	**55.5**	**0.4**
2. Development expenditures and net lending	**25.7**	**2.6**	**43.1**	**2.9**	**39.4**	**91.4**	**2.7**
a. Rupiah financing	9.4	0.9	20.6	1.4	19.7	95.6	1.3
b. Project aid	16.3	1.7	22.5	1.5	19.7	87.5	1.3
II. Regional Budget Expenditures	**32.9**	**3.3**	**81.5**	**5.5**	**82.4**	**101.1**	**5.6**
1. Balance Budget	**32.9**	**3.3**	**81.5**	**5.5**	**82.4**	**101.1**	**5.6**
a. Revenue sharing funds	4.3	0.4	20.3	1.4	21.2	104.6	1.4
b. General allocation funds	28.6	2.9	60.5	4.1	60.5	100.0	4.1
c. Special allocation funds	-	-	0.7	0.0	0.7	100.0	0.0
2. Special autonomy	**-**	**-**	**-**	**-**	**-**	**-**	**-**

1) Statel budget (unaudited), period of April 1 to December 31, 2000
2) State budget (revised)
3) State budget (provisional realization)
Source : Ministry of Finance and Bank Indonesia (processed)

funds with a share of almost 73.4% of total regional balancing funds. The general allocation funds included late payment of civil servants salary increases, which were effective around mid-2001.

DEFICIT AND FINANCING

With government revenues and expenditures exceeding their respective targets by similar percentages, the deficit on the government's financial operations in 2001 is estimated to have been contained at Rp54.7 trillion or 3.7% of GDP, as provided for in the 2001 revised state budget (Table 7.4). Most of this deficit was covered by asset recovery in the amount of Rp31.0 trillion (56.6%), net offshore financing of Rp10.5 trillion (19.3%), and privatization receipts of Rp5.0 trillion (9.1%). The remainder (Rp7.6 trillion equivalent to 0.5% of GDP) was financed by

Table 7.4
Government Financial Operation 2001*

Item	2000[1)]		2001				
			Budget[2)]		Budget[3)]		
	Trillions of Rp	% of GDP	Trillions of Rp	% of GDP	Trillions of Rp	% of Budget[R]	% of GDP
A. Government Revenues and Grants	**204.9**	**20.7**	**286.0**	**19.5**	**299.9**	**104.8**	**20.3**
I. Domestic Revenues	**204.9**	**20.7**	**286.0**	**19.5**	**299.8**	**104.8**	**20.3**
1. Tax Revenues	**115.8**	**11.7**	**185.3**	**12.6**	**184.7**	**99.7**	**12.5**
a. Domestic taxes	108.8	11.0	174.3	11.9	174.2	100.0	11.8
b. International trade taxes	7.0	0.7	11.0	0.7	10.5	95.8	0.7
2. Non-tax revenues	**89.2**	**9.0**	**100.7**	**6.9**	**115.1**	**114.3**	**7.8**
a. Natural resource	76.0	7.7	79.4	5.4	86.7	109.1	5.9
b. Profit transfer from SOEs	3.9	0.4	9.0	0.6	10.4	116.0	0.7
c. Other	9.3	0.9	12.3	0.8	18.0	146.4	1.2
II. Grants	**-**	**-**	**-**	**-**	**0.0**	**-**	**0.0**
B. Government Expenditures	**219.9**	**22.3**	**340.3**	**23.2**	**354.6**	**104.2**	**24.0**
I. Central Government Expenditures	**187.1**	**18.9**	**258.8**	**17.6**	**272.2**	**105.1**	**18.4**
1. Current Expenditure	**161.4**	**16.3**	**215.8**	**14.7**	**232.8**	**107.9**	**15.8**
a. Personnel	29.4	3.0	38.2	2.6	39.5	103.5	2.7
b. Material	8.1	0.8	9.9	0.7	9.6	96.9	0.7
c. Interest payment	50.1	5.1	89.6	6.1	95.5	106.7	6.5
d. Subsidy	62.8	6.4	66.3	4.5	81.6	123.1	5.5
e. Other	11.0	1.1	11.8	0.8	6.5	55.5	0.4
2. Development expenditure and net lending	**25.7**	**2.6**	**43.1**	**2.9**	**39.4**	**91.4**	**2.7**
a. Rupiah financing	9.4	0.9	20.6	1.4	19.7	95.6	1.3
b. Project aid	16.3	1.7	22.5	1.5	19.7	87.5	1.3
II. Regional Budget Expenditures	**32.9**	**3.3**	**81.5**	**5.5**	**82.4**	**101.1**	**5.6**
1. Balance budget	**32.9**	**3.3**	**81.5**	**5.5**	**82.4**	**101.1**	**5.6**
2. Special autonomy	**-**	**-**	**-**	**-**	**-**	**-**	**-**
C. Statistical Discrepancy	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
D. Primary Balance	**35.1**	**3.6**	**35.2**	**2.4**	**40.8**	**115.7**	**2.8**
E. Budget Surplus/(Deficit)	**(15.0)**	**(1.5)**	**(54.3)**	**(3.7)**	**(54.7)**	**100.7**	**(3.7)**
F. Financing	**15.0**	**1.5**	**54.3**	**3.7**	**54.7**	**100.7**	**3.7**
I. Domestic Financing	**5.4**	**0.6**	**34.4**	**2.3**	**44.2**	**128.5**	**3.0**
1. Domestic banks financing	**(13.5)**	**(1.4)**	**0.0**	**0.0**	**7.6**	**-**	**0.5**
2. Non-domestic banks financing	**18.9**	**1.9**	**34.4**	**2.3**	**36.6**	**106.5**	**2.5**
a. Privatization proceed	0.0	0.0	6.5	0.4	5.0	76.9	0.3
b. Recovery of Bank asset	18.9	1.9	27.0	1.8	31.0	114.7	2.1
c. Government bonds	0.0	0.0	0.9	0.1	0.7	74.2	0.0
II. Foreign Financing (Net)	**9.6**	**1.0**	**19.9**	**1.4**	**10.5**	**52.9**	**0.7**
1. Gross drawing	**17.2**	**1.7**	**40.1**	**2.7**	**30.3**	**75.5**	**2.1**
a. Program aid	0.8	0.1	16.3	1.1	10.6	65.0	0.7
b. Project aid	16.3	1.7	23.7	1.6	19.7	82.8	1.3
2. Amortization	**(7.6)**	**(0.8)**	**(20.2)**	**(1.4)**	**(19.7)**	**98.0**	**(1.3)**

1) Statel budget (unaudited), period of April 1 to December 31, 2000
2) State budget (revised)
3) State budget (provisional realization)
Source : Ministry of Finance and Bank Indonesia (processed)

more net credit to the government from the monetary system.

Viewed from achievement of targets, the asset recovery reached 114.7% of budgeted amounts; while privatization and net foreign financing were only 76.9% and 52.9%, respectively. The low realization of privatization was attributed in part to weak domestic and international markets, conflicts of interest between parties involved in privatization, continuing weak legal infrastructure, and incomplete corporate restructuring.

On external financing, there were limited drawings of both program and project aid, of 65.0% and 82.8% of budget targets, respectively. Low drawings of program loans were due to failure to meet policy conditions that had been agreed between the government and the aid donors. These included delays in the law concerning money laundering, the law concerning electricity, and amendment to law number 23 of 1999 concerning Bank Indonesia. Limited drawings of project aid were partly due to the short time available for project implementation after the revision of the state budget and to the limited availability of rupiah counterpart funds. The respective proportions of program and project loans in total drawings of offshore aid were 35% and 65%.

Impact of Government Financial Operations On Aggregate Demand, Monetary Conditions, and the Balance of Payments

Of total government spending of Rp354.6 trillion, some Rp175.5 trillion (or 49.5%, equivalent to 11.9% of GDP) directly influenced aggregate demand in the form of consumption expenditure and government investment (Table 7.5). Of the total that influenced aggregate demand, 65.1% was in the form of consumption spending and 34.9% was investment spending. Meanwhile, 41.7% of total government spending (or Rp147.8 trillion, equivalent to 10.0% of GDP) was for transfers to the private sector in the form of subsidies and interest on domestic loans.

Compared with the year before, government consumption spending was virtually unchanged at

Table 7.5
Impact of State Budget on Domestic Demand*

Item	2000[1)]		2001				
			Budget[2)]		Realization[3)]		
	Trillions of Rp	% of GDP	Trillions of Rp	% of GDP	Trillions of Rp	% of Budget[R]	% of GDP
I. Government Consumption	**76.7**	**7.8**	**117.7**	**8.0**	**114.3**	**97.1**	**7.7**
Domestic Personnel Expenditures	29.1	2.9	36.7	2.5	38.5	104.9	2.6
Domestic Material Expenditures	8.0	0.8	8.7	0.6	8.7	100.0	0.6
General Allocation Funds	28.6	2.9	60.5	4.1	60.5	100.0	4.1
Other Routine Expenditures	11.0	1.1	11.8	0.8	6.5	55.5	0.4
II. Gross Domestic Fixed Capital Formation	**29.9**	**3.0**	**64.0**	**4.4**	**61.3**	**95.7**	**4.2**
Rupiah Financing	9.4	0.9	20.6	1.4	19.7	95.6	1.3
Project Aid	16.3	1.7	22.5	1.5	19.7	87.5	1.3
Revenue Sharing and Special Allocation Funds	4.3	0.4	21.0	1.4	21.9	104.4	1.5
III. Total I + II	**106.6**	**10.8**	**181.8**	**12.4**	**175.5**	**96.6**	**11.9**
Memo Items : Transfer Payment	94.0	6.4	127.4	8.7	147.8	120.6	10.0
a. Domestic interest	31.2	2.1	61.2	4.2	66.3	108.3	4.5
b. Subsidies	62.8	4.3	66.3	4.5	81.6	12.3	5.5

1) Statel budget(unaudited), period of April 1 to December 31, 2000
2) State budget (revised)
3) State budget (provisional realization)
Source : Ministry of Finance and Bank Indonesia (processed)

Table 7.6
Rupiah Impact of Government Financial Operation*

Item	2000 1)		2001 Budget 2)		2001 Realization 3)		
	Trillions of Rp	% of GDP	Trillions of Rp	% of GDP	Trillions of Rp	% of GDP	% of Budget R
A. Revenues in Rupiah							
Taxes							
Oil and Gas	18.7	1.9	25.7	1.8	23.1	1.6	89.8
Non-oil and gas	97.1	9.8	159.5	10.9	161.6	10.9	101.3
Non-taxes	22.5	2.3	25.5	1.7	33.2	2.3	130.2
Privatization proceeds	0.0	0.0	6.5	0.4	5.0	0.3	76.9
Recovery of bank asset	18.9	1.9	27.0	1.8	31.0	2.1	114.7
Government bonds	0.0	0.0	0.9	0.1	0.7	0.0	74.2
Total Revenues	**157.2**	**15.9**	**245.2**	**16.7**	**254.6**	**17.2**	**103.8**
B. Expenditure in Rupiah							
Operational	-142.1	-14.4	-184.7	-12.6	-201.6	-13.7	109.2
Domestic Personnel	-29.1	-2.9	-36.7	-2.5	-38.5	-2.6	104.9
Subsidies	-62.8	-6.4	-66.3	-4.5	-81.6	-5.5	123.1
Domestic Interest Payment	-31.2	-3.2	-61.2	-4.2	-66.3	-4.5	108.3
Other Routine Expenditure	-19.0	-1.9	-20.5	-1.4	-15.3	-1.0	74.4
Investment	-15.1	-1.5	-28.5	-1.9	-26.6	-1.8	93.4
Regional Expenditure	-32.9	-3.3	-81.5	-5.5	-82.4	-5.6	101.1
Total Expenditures	**-190.0**	**-19.2**	**-294.6**	**-20.1**	**-310.6**	**-21.0**	**105.4**
C. Statistical Discrepancy	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
D. Rupiah Impact	**-32.8**	**-3.3**	**-49.5**	**-3.4**	**-56.0**	**-3.8**	**113.2**

1) State budget (unaudited), period of April 1 to December 31, 2000
2) State budget (revised)
3) State budget (provisional realization)
Source : Ministry of Finance and Bank Indonesia (processed)

7.7% of GDP. Government investment spending rose from 3.0% to 4.2%, due in particular to funds allocated for revenue sharing with regional governments, starting in 2001. Transfers to the private sector in the form of subsidies and interest on public debt rose quite sharply from 6.4% to 10.0% of GDP. Overall, the government sector's direct contribution to aggregate demand rose from 10.8% of GDP in 2000 to 11.9% in 2001.

On the monetary side, government financial transactions during 2001 had a net expansionary impact of Rp56.0 trillion on the money supply (Table 7.6). The largest expansions occurred in budgetary spending for the regions, subsidies, and payments of interest on domestic loans. Compared with the year before, this net rupiah expansion rose from 3.3% to 3.8% of GDP. The main factors that pushed the rise of net rupiah expansion in 2001 were the rise in allocations for the regions from 3.3% to 5.6% of GDP and payment of interest on domestic loans from 3.2% to 4.5% of GDP.

From the balance of payments side, government financial transactions are estimated to provide net foreign currency inflows equivalent to Rp48.4 trillion, or somewhat lower (by around Rp7.6 trillion) than the net rupiah expansion mentioned above (Table 7.7). On this basis, there was a remain-

Table 7.7
Foreign Exchange Impact of Government Financial Operation*

Item	2000[1)]		2001				
			APBN[2)]		Realization[3]		
	Trillions of Rp	% of GDP	Trillions of Rp	% of GDP	Trillions of Rp	% of Budget[R]	% of GDP
A. Current Account	**36.8**	**3.7**	**29.5**	**2.0**	**37.9**	**2.6**	**128.3**
Trade balance	55.9	5.7	59.4	4.0	68.2	4.6	114.8
Oil and gas export	66.7	6.7	75.2	5.1	81.9	5.5	108.9
Project aid import	-10.6	-1.1	-14.6	-1.0	-12.8	-0.9	87.5
Foreign material expenditure	-0.1	0.0	-1.2	-0.1	-0.9	-0.1	74.0
Services account	-19.1	-1.9	-29.9	-2.0	-30.3	-2.1	101.4
Foreign debt interest payment	-18.8	-1.9	-28.4	-1.9	-29.3	-2.0	103.1
Foreign personnel expenditure	-0.3	0.0	-1.5	-0.1	-1.1	-0.1	69.9
B. Net Official Capital Inflows	**9.6**	**1.0**	**19.9**	**1.4**	**10.5**	**0.7**	**52.9**
Foreign debt disbursment and grants	17.2	1.7	40.1	2.7	30.3	2.1	75.6
Foreign debt amortization	-7.6	-0.8	-20.2	-1.4	-19.7	-1.3	98.0
C. Foreign Exchange Impact (A+B)	**46.3**	**4.7**	**49.5**	**3.4**	**48.4**	**3.3**	**97.9**

1) State budget (unaudited), period of April 1 to December 31, 2000
2) State budget (revised)
3) State budget (provisional realization)
Source : Ministry of Finance and Bank Indonesia (processed)

der of Rp7.6 trillion, which was covered by withdrawals from the government's accounts in the monetary system. The main contributor of the foreign currency inflows was oil and gas exports, which reached almost 73% of government foreign currency revenues. Compared with the year before, government net foreign currency inflows dropped from 4.7% to 3.3% of GDP. The important factor that caused the drop in net foreign currency inflows was low drawings on offshore loans, which reached only 75% of planned amounts.

PROSPECTS FOR THE 2002 STATE BUDGET

During 2002, state financial policies will be directed at achieving fiscal sustainability. For this purpose, there are two strategic objectives designed into the 2002 state budget. First, efforts to reduce the size of the budget deficit, both in levels and as a ratio to GDP. And second, efforts to reduce the ratio of government debt—domestic and offshore—to GDP. Therefore, the government is preparing measures to boost government revenues, control spending, and optimize choices for financing the deficit.

Table 7.8
Basic Assumptions for the State Budget 2001 - 2002

Assumptions	2001	2002
	Budget	
Nominal GDP (trillions of rupiah)	1,468.1	1,685.4
Economic growth (%)	3.5	4.0
Inflation rate (%)	9.30	9.00
Crude oil price ($/barrel)	24.0	22.0
Oil production (millions of barrels per day)	1.5	1.3
Exchange rate (Rp/$)	9,600	9,000
Average three month SBI-rates (%)	15.00	14.00

Source : Ministry of Finance

Table 7.9
Government Revenues and Grants*

I t e m	Budget 2001[1]		Budget 2002[2]		Change
	Trillions of Rp	% of GDP	Trillions of Rp	% of GDP	% of GDP
A. Government Revenues and Grants	**286.0**	**19.5**	**301.9**	**17.9**	**-1.6**
I. Domestic Revenues	**286.0**	**19.5**	**301.9**	**17.9**	**-1.6**
1. Tax revenues	**185.3**	**12.6**	**219.6**	**13.0**	**0.4**
a. Domestic taxes	**174.3**	**11.9**	**207.0**	**12.3**	**0.4**
i. Income tax	95.0	6.5	104.5	6.2	-0.3
1. Oil and gas	25.7	1.8	15.7	0.9	-0.8
2. Non-oil and gas	69.2	4.7	88.8	5.3	0.6
ii. Value added tax	53.5	3.6	70.1	4.2	0.5
iii. Land and building tax	5.1	0.3	5.9	0.4	0.0
iv. Duty on land and building transfer (BPHTB)	1.2	0.1	2.2	0.1	0.0
v. Excise duties	17.6	1.2	22.4	1.3	0.1
vi. Other taxes	1.9	0.1	1.9	0.1	0.0
b. International trade tax	**11.0**	**0.7**	**12.6**	**0.7**	**0.0**
i. Import duties	10.4	0.7	12.2	0.7	0.0
ii. Export tax	0.6	0.0	0.3	0.0	0.0
2. Non-tax Revenues	**100.7**	**6.9**	**82.2**	**4.9**	**-2.0**
a. Natural resource revenues	**79.4**	**5.4**	**63.2**	**3.7**	**-1.7**
i. Oil	57.9	3.9	44.0	2.6	-1.3
ii. Gas	17.4	1.2	14.5	0.9	-0.3
iii. Mining	0.9	0.1	1.3	0.1	0.0
iv. Forestry	3.0	0.2	3.0	0.2	0.0
v. Fishery	0.3	0.0	0.3	0.0	0.0
b. Profit transfer from State-owned Enterprises (SOEs)	**9.0**	**0.6**	**10.4**	**0.6**	**0.0**
c. Other non-tax revenues	**12.3**	**0.8**	**8.7**	**0.5**	**-0.3**
II. Grants	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**

1) State budget, revised as per June15, 2001
2) State budget, approved on October 23, 2001
Source : Ministry of Finance (processed)

Government financial operations in 2002 are budgeted to be in a deficit of Rp42.1 trillion or 2.5% of GDP, compared with Rp54.3 trillion (3.7% of GDP) in the budget for 2001. To achieve this lower deficit, revenues will be increased, mainly by broadening the tax base, and by greater efficiency in spending through budget prioritization. On the financing side, the government will make efforts to increase sales of assets through the bank restructuring program and privatization and to use part of the receipts to reduce domestic debt (asset-for-bond swaps and cash-for-bond swap).

Total government revenue is expected to rise from Rp286 trillion to Rp301.9 trillion. However, as a percentage of GDP, it will drop from 19.5% to 17.9%, mainly due to a decline in Indonesia's crude oil price from $24 to $22 per barrel. The main source of revenue would be tax revenue of Rp219.6 trillion with a tax ratio target that rises from 12.6% of GDP in 2001 to 13.0%. To achieve this tax revenue target, the government will continue various policies concerning tax collection intensification and extensions of tax subjects/objects. That policy will be implemented for all types of taxes, which will be further detailed in operational policies for each type of tax. In addition to working as a contingency against a drop in oil and gas revenues, a gradual rise in the tax target is vital to ensuring future fiscal sustainability. By contrast,

Table 7.10
Government Expenditures*

Item	Budget 2001 1)		Budget 2002 2)		Change
	Trillions of Rp	% of GDP	Trillions of Rp	% of GDP	Trillions of Rp
B. Government Expenditures	**340.3**	**23.2**	**344.0**	**20.4**	**-2.8**
I. Central Government Expenditures	**258.8**	**17.6**	**246.0**	**14.6**	**-3.0**
1. Current Expenditures	**215.8**	**14.7**	**193.7**	**11.5**	**-3.2**
a. Personnel expenditures	**38.2**	**2.6**	**41.3**	**2.5**	**-0.2**
i. Salaries and pensions	31.9	2.2	34.0	2.0	-0.2
ii. Rice allowances	1.3	0.1	1.4	0.1	0.0
iii. Food allowances	2.1	0.1	2.8	0.2	0.0
iv. Other domestic personnel expenditures	1.4	0.1	1.5	0.1	0.0
v. Overseas personnel expenditure	1.5	0.1	1.5	0.1	0.0
b. Material expenditures	**9.9**	**0.7**	**12.9**	**0.8**	**0.1**
i. Domestic	8.7	0.6	11.7	0.7	0.1
ii. External	1.2	0.1	1.2	0.1	0.0
c. Interest Payment	**89.6**	**6.1**	**88.5**	**5.3**	**-0.9**
i. Domestic interest	61.2	4.2	59.5	3.5	-0.6
ii. Foreign interest	28.4	1.9	29.0	1.7	-0.2
d. Subsidies	**66.3**	**4.5**	**41.6**	**2.5**	**-2.0**
i. Oil subsidies	53.8	3.7	30.4	1.8	-1.9
ii. Non-oil subsidies	12.5	0.9	11.2	0.7	-0.2
- Rice (BULOG)	2.4	0.2	4.7	0.3	0.1
- Electricity	4.7	0.3	4.1	0.2	-0.1
- Credit program	4.9	0.3	2.2	0.1	-0.2
- Others	0.4	0.0	0.2	0.0	0.0
e. Other current expenditures	**11.8**	**0.8**	**9.5**	**0.6**	**-0.2**
2. Development expenditures and net lending	**43.1**	**2.9**	**52.3**	**3.1**	**0.2**
a. Rupiah financing	20.6	1.4	26.5	1.6	0.2
b. Project aid	22.5	1.5	25.8	1.5	0.0
II. Regional Budget Expenditures	**81.5**	**5.5**	**98.0**	**5.8**	**0.3**
1. Balance budget	**81.5**	**5.5**	**94.5**	**5.6**	**0.1**
a. Revenue sharing funds	20.3	1.4	24.6	1.5	0.1
b. General allocation funds	60.5	4.1	69.1	4.1	0.0
c. Special allocation funds	0.7	0.0	0.8	0.0	0.0
2. Special autonomy	**0.0**	**0.0**	**3.4**	**0.2**	**0.2**

1) State budget, revised as per June15, 2001
2) State budget, approved on October 23, 2001
Source : Ministry of Finance (processed)

non-tax revenues are estimated to drop compared with the previous year, from 6.9% to 4.9% of GDP.

On the spending side, expenditure is planned to rise to Rp344.0 trillion, which would represent 20.4% of GDP compared with 23.2% in 2001. This drop would be accounted for by the allocation for central government routine expenditures, which falls sharply from 14.7% to 11.5% of GDP.

The largest spending will be for interest on the public debt that will reach Rp88.5 trillion or equivalent to 5.3% of GDP. However, interest payments will be lower in 2002 than in 2001 in line with assumptions that SBI rates will decline; that the exchange rate will strengthen; and that the stock of domestic debt will decline through, for example, asset-for-bond swaps, cash-for-bond swaps and the use of receipts from asset sales to buy back debt.

Three other large spending categories are : (i) subsidies (2.5% of GDP), (ii) personnel expen-

Table 7.11
Government Financial Operation*

I t e m	Budget 2001[1)]		Budget 2002[2)]		Change
	Trillions of Rp	% of GDP	Trillions of Rp	% of GDP	% of GDP
A. Government Revenues and Grants	**286.0**	**19.5**	**301.9**	**17.9**	**-1.6**
I. Domestic Revenues	**286.0**	**19.5**	**301.9**	**17.9**	**-1.6**
1. Tax Revenues	**185.3**	**12.6**	**219.6**	**13.0**	**0.4**
a. Domestic tax	174.3	11.9	207.0	12.3	0.4
b. International trade taxes	11.0	0.7	12.6	0.7	0.0
2. Non tax revenues	**100.7**	**6.9**	**82.2**	**4.9**	**-2.0**
a. Natural resource revenues	79.4	5.4	63.2	3.7	-1.7
b. Profit transfer from SOEs	9.0	0.6	10.4	0.6	0.0
c. Other non-tax revenues	12.3	0.8	8.7	0.5	-0.3
II. Grants	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
B. Goverment Expenditures	**340.3**	**23.2**	**344.0**	**20.4**	**-2.8**
I. Central Government Expenditures	**258.8**	**17.6**	**246.0**	**14.6**	**-3.0**
1. Current Expenditures	**215.8**	**14.7**	**193.7**	**11.5**	**-3.2**
a. Personnel expenditures	38.2	2.6	41.3	2.5	-0.2
b. Material expenditures	9.9	0.7	12.9	0.8	0.1
c. Interest payments	89.6	6.1	88.5	5.3	-0.9
d. Subsidies	66.3	4.5	41.6	2.5	-2.0
e. Other routine expenditures	11.8	0.8	9.5	0.6	-0.2
2. Development Expenditures	**43.1**	**2.9**	**52.3**	**3.1**	**0.2**
a. Rupiah Financing	20.6	1.4	26.5	1.6	0.2
b. Project Aid	22.5	1.5	25.8	1.5	0.0
II. Regional Budget Expenditures	**81.5**	**5.5**	**98.0**	**5.8**	**0.3**
1. Balance Budget	**81.5**	**5.5**	**94.5**	**5.6**	**0.1**
2. Special Autonomy	**0.0**	**0.0**	**3.4**	**0.2**	**0.2**
C. Statistical Discrepancy	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
D. Primary Balance	**35.2**	**2.4**	**46.4**	**2.8**	**0.3**
E. Overall Balance	**-54.3**	**-3.7**	**-42.1**	**-2.5**	**1.2**
F. Financing	**54.3**	**3.7**	**42.1**	**2.5**	**-1.2**
I. Domestic Financing	**34.4**	**2.3**	**23.5**	**1.4**	**-0.9**
1. Domestic banks	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
2. Non-domestic banks	**34.4**	**2.3**	**23.5**	**1.4**	**-0.9**
a. Privatization proceeds	6.5	0.4	4.0	0.2	-0.2
b. Recovery of bank asset	27.0	1.8	19.5	1.2	-0.7
c. Government bonds	0.9	0.1	0.0	0.0	-0.1
II. Foreign Financing (Net)	**19.9**	**1.4**	**18.6**	**1.1**	**-0.3**
1. Gross drawing	**40.1**	**2.7**	**62.6**	**3.7**	**1.0**
a. Program Aid	16.3	1.1	36.8	2.2	1.1
b. Project Aid	23.7	1.6	25.8	1.5	–0.1
2. Amortization	**-20.2**	**-1.4**	**-44.0**	**-2.6**	**-1.2**
1) Targeted Privatization Proceeds	6.5	0.4	6.5	0.4	-0.1
(Includes redeemed of Government Bond)	0.0	0.0	-2.5	-0.2	-0.2
2) Recovery of Bank Asset	37.0	2.5	42.8	2.5	0.0
(Includes redeemed of Government Bond)	-10.0	-0.7	-23.3	-1.4	-0.7

1) State budget, revised as per 15 June 2001
2) State budget, approved on 23rd October 2001
Source : Ministry of Finance (processed)

ditures (2.4%), and (iii) development expenditures (3.1%). Subsidies will drop significantly from their levels of 2001, mainly due to government plans to raise domestic fuel prices by an average of 25% starting January 2002 and basic electricity tariffs by 4% - 6% each quarter. Personnel expenditure is budgeted

Table 7.12
Rupiah Impact of the 2001 and 2002 Budget*

Item	Budget 2001[1]		Budget 2002[2]		Change
	Trillions of Rp	% of GDP	Trillions of Rp	% of GDP	% of GDP
A. Revenues in Rupiah					
Taxes					
Oil and gas	25.7	1.8	15.7	0.9	-0.8
Non-oil and gas	159.5	10.9	203.9	12.1	1.2
Non-taxes	25.5	1.7	23.7	1.4	-0.3
Privatization proceeds	6.5	0.4	4.0	0.2	-0.2
Recovery of bank asset	27.0	1.8	19.5	1.2	-0.7
Government bonds	0.9	0.1	0.0	0.0	-0.1
Total revenues	**245.2**	**16.7**	**266.8**	**15.8**	**-0.9**
B. Expenditures in Rupiah					
Operational	-184.7	-12.6	-162.1	-9.6	3.0
Personnel expenditure	-36.7	-2.5	-39.8	-2.4	0.1
Subsidies	-66.3	-4.5	-41.6	-2.5	2.0
Domestic interest payments	-61.2	-4.2	-59.5	-3.5	0.6
Other routine expenditure	-20.5	-1.4	-21.2	-1.3	0.1
Investment	-28.5	-1.9	-35.5	-2.1	-0.2
Regional expenditures	-81.5	-5.5	-98.0	-5.8	-0.3
Total expenditures	**-294.6**	**-20.1**	**-295.6**	**-17.5**	**2.5**
C. Statistical Discrepancy	**0.0**	**0.0**	**0.0**	**0.0**	**0.0**
D. Rupiah Impact	**-49.5**	**-3.4**	**-28.7**	**-1.7**	**1.7**

1) State budget, revised as per 15 June 2001
2) State budget, approved on october 23, 2001
Source : Ministry of Finance (processed)

to rise in nominal terms owing in part to higher allowances for several functional positions, considering that there has been no change in those allowances for several years. Meanwhile, funds allocated for development expenditures will remain low compared with routine expenditures.

Meanwhile, the budget allocation for the regions in 2002 is estimated to reach Rp98.0 trillion (5.8% of GDP), up a bit from 2001, which was recorded at Rp81.5 trillion (5.5% of GDP). The majority of this allocation will be for general allocation funds (Rp69.1 trillion), followed by revenue sharing funds (Rp24.6 trillion), and the remainder for special allocation funds. In addition, the government has allocated funds amounting to Rp3.4 trillion for the implementation of special autonomy.

In the conditions described above, the primary balance would record a surplus of 2.8% of GDP in 2002, slightly better than in 2001. In 2002, the overall fiscal deficit is expected to amount to Rp42.1 trillion or 2.5% of GDP. Part of this deficit will be financed domestically, particularly from privatization and asset recovery; the remaining deficit would be financed from offshore sources.

The target for privatization is set at Rp6.5 trillion, of which Rp2.6 trillion would be used to buy back government bonds. Meanwhile, sales of IBRA assets are targeted at Rp42.8 trillion, of which Rp7.5 trillion would be reached in the form of asset-to-bond swaps and Rp15.8 trillion in the form of cash-to-bond swaps. On this basis, outstanding domestic debt would be reduced by some Rp25.8 trillion during 2002.

Table 7.13
Foreign Exchange Impact of the 2001 and 2002 Budget*

Item	Budget 2001[1)]		Budget 2002[2)]		Change
	Trillions of Rp	% of GDP	Trillions of Rp	% of GDP	%of GDP
A. Current Account	**29.5**	**2.0**	**10.1**	**0.6**	**-1.4**
Trade balance	59.4	4.0	40.6	2.4	-1.6
Oil and gas export	75.2	5.1	58.5	3.5	-1.7
Project aid import	-14.6	-1.0	-16.8	-1.0	0.0
Foreign material expenditure	-1.2	-0.1	-1.2	-0.1	0.0
Services account	-29.9	-2.0	-30.5	-1.8	0.2
Foreign debt interest payment	-28.4	-1.9	-29.0	-1.7	0.2
Foreign personnel expenditure	-1.5	-0.1	-1.5	-0.1	0.0
B. Net Official Capital Inflows	**19.9**	**1.4**	**18.6**	**1.1**	**-0.3**
Foreign debt disbursment and grants	40.1	2.7	62.6	3.7	1.0
Foreign debt amortization	-20.2	-1.4	-44.0	-2.6	-1.2
C. Foreign Exchange Impact (A+B)	**49.5**	**3.4**	**28.7**	**1.7**	**-1.7**

1) State budget, revised as per 15 June 2001
2) State budget, approved on t on October 23, 2001
Source : Ministry of Finance (processed)

This policy to buy back outstanding bonds is aimed at reducing government domestic debt, which is currently more burdensome than foreign debt.

Meanwhile, net foreign financing in 2002 is estimated to drop in comparison with last year, from Rp19.9 trillion to Rp18.6 trillion. This net addition to foreign debt is smaller than the total value of government bond buy backs. Consequently, total outstanding government debt would decline in 2002, which is important for fiscal sustainability.

Impact of Government Financial Operations on Monetary Conditions, the Balance of Payments, and Aggregate Demand

The various policies on government financial operations, which are quantified in the 2002 state budget, will influence the monetary side of the economy, as well as the balance of payments and aggregate demand. On the monetary side, government financial transactions in 2002 are estimated to provide a net rupiah expansion of Rp28.8 trillion (1.7% of GDP), far lower than in 2001, which amounted to Rp49.5 trillion (3.4% of GDP). The largest drop will stem from reductions in fuel and electricity subsidies. This drop in net rupiah expansion is also supported by an optimistic rise in the tax ratio from 12.6% to 13.0% in 2002. Lower net rupiah expansion on government account is expected to reduce the burden of monetary control, thereby reducing interest rates which should boost activity in the real sector. This would also feedback favorably into the government accounts and assist further with fiscal sustainability.

Concerning the balance of payments, the main sources of foreign currency inflows are oil and gas revenues and drawings on offshore loans of Rp58.5 trillion and Rp62.6 trillion, respectively.

Table 7.14
Impact of the 2001 and 2002 Budget on Domestic Demand*

Item	Budget 2001[1]		Budget 2002[2]		Change
	Trillions of Rp	% of GDP	Trillions of Rp	% of GDP	% of GDP
I. Government Consumption	**117.7**	**8.0**	**133.5**	**7.9**	**-0.1**
Domestic Personnel expenditures	36.7	2.5	39.8	2.4	-0.1
Domestic material expenditures	8.7	0.6	11.7	0.7	0.1
General allocation funds	60.5	4.1	69.1	4.1	0.0
Other routine expenditures[3]	11.8	0.8	12.9	0.8	0.0
II. Gross Domestic Fixed Capital Formation	**64.0**	**4.4**	**77.7**	**4.6**	**0.2**
Rupiah financing	20.6	1.4	26.5	1.6	0.2
Project aid	22.5	1.5	25.8	1.5	0.0
Revenue sharing and special allocation funds	21.0	1.4	25.4	1.5	0.1
III. Total I + II	**181.8**	**12.4**	**211.3**	**12.5**	**0.2**
Memo Items : Transfer Payment	127.4	8.7	101.1	6.0	-2.7
a. Domestic interest	61.2	4.2	59.5	3.5	-0.6
b. Subsidies	66.3	4.5	41.6	2.5	-2.0

1) State budget, revised as per 15 June 2001
2) State budget, approved on 23rd October 23, 2001
3) Including special autonomy and equalization funds
Source : Ministry of Finance (processed)

Meanwhile, foreign currency outflows will mainly be used to pay for interest and amortization on offshore loans, of Rp29.0 trillion and Rp44.0 trillion, respectively. On this basis, the foreign currency impact of government operations is estimated to amount to Rp28.7 trillion. This number will be used by Bank Indonesia in conducting monetary operations to sterilize the impact of government rupiah transactions on base money.

Regarding the impact on aggregate demand, the government's contribution to aggregate demand will remain limited and rise only a little, from 12.4% in 2001 to 12.5% of GDP in 2002. There would be a small increase in investment, from 4.4% to 4.6%; government consumption would be virtually unchanged. Meanwhile, government spending in the form of transfers to the private sector would drop from 8.7% to 6.0% of GDP, due to a reduction in subsidies.

box

Indonesia's Debt Problem and Options For Its Management[1]

Indonesia's debt problem currently is quite complex, burdensome, and serious. It is complex because it originates in both domestic and foreign debts borne by the government, as well as foreign debts that have to be borne by the national private sector. It is burdensome because debt has put threatening amounts of pressure on the current account of the balance of payments and the government's finances. It is serious because measures adopted to date have done little to lighten the burden.

This debt problem should make us awake and be on the alert. The size of debts that are borne by the government currently is almost the same as total GDP, rising sharply from only 25% of GDP in 1996. Meanwhile, government foreign debts as of December 2001 stood at $71.4 billion or 49.1% of GDP. With private foreign debts of $59.8 billion, overall foreign debts borne by Indonesia have reached $131.2 billion, or 90.3% of GDP in 2001.

With such high level of debts, debt service payments borne by the government as well as the national private sector swelled. In 2002, for example, the government has to reserve funds of around Rp136.4 trillion for debt servicing (principal and interest); approximately Rp73.0 trillion is allocated for foreign debts and some Rp63.4 trillion for domestic debts. Compared with government revenue projections for the same year, government debt service had reached 45.2%. Meanwhile, the private sector foreign debt service is estimated at $11.8 billion for 2002. On this basis, debt service payments on government and private foreign debts for 2002 will reach $24.2 billion. Debt service ratios (DSRs) for 2001 and 2002 are estimated at around 39.4% and 34.9%, respectively, far higher than the 20% that is considered as a safe DSR level by the World Bank.

Measurement of government financial solvency and sustainability can be undertaken with the intertemporal budget constraint approach developed by Dinh (1999).[2] Results of the analysis performed by Bank Indonesia using this approach show that government finance for the period 2001-2005 is, in general, still solvent and sustainable.

However, there are a number of critical factors that will substantially influence the solvency and sustainability of government finance during the coming years. These factors are in the fiscal and macro-economic areas. Specifically, critical factors in the fiscal area will depend very much upon the size of the government's primary balance;[3] critical factors in

1 Summarized from "Indonesia's Debts: Condition, Problems and Options For Handling", a paper prepared by the Directorate of Economic Research and Monetary Policies and Directorate of Foreign Affairs, Bank Indonesia, December 2001.

2 Hinh T. Dinh, "Fiscal Solvency and Sustainability in Economic Management", Macroeconomics In The Southern Africa Region, The World Bank, 1999.

3 The primary surplus/deficit is the surplus/deficit in government financial operation excluding interest obligations.

the macroeconomic area will determine the height of the index (passing grade) of fiscal solvency and sustainability. More important, in addition to influencing the size of the government's primary balance, critical factors in the fiscal area also determine the possibility of short-term liquidity problems for government finance in relation to servicing its extremely large debt burden obligation.

The critical fiscal factors mentioned above include success in the privatization of state-owned enterprises and sales of assets by IBRA, as well as the success of the bank recapitalization program, subsidy reductions, and implementation of regional autonomy. Meanwhile, the critical macroeconomic factors include a number of short-and medium-term macro developments: (i) the international economy, which has been highly uncertain lately; (ii) domestic social, political and security conditions, which are important determinants of consumer confidence and the investment climate; and (iii) a recovery of bank intermediation.

Solvency analysis of Indonesia's finances (the non-interest current account) support previous analysis concerning the debt burden borne by Indonesia's economy. Although Indonesia's finances are generally estimated to still be in a manageable condition during the period 2000-2004, its finances are quite worrisome. Future developments will be very much dependent on a number of critical factors. These factors, in addition to being related to the development of macroeconomic variables as just described, have a substantial direct relation with the success of our efforts to restructure government and national private foreign debts in the future short- and medium-term.

From the review above, it can be seen clearly that Indonesia's debt problem forces us to focus on at least three issues, namely: (i) short-term liquidity problems that might be faced by the government as a consequence of the high debt burden; (ii) solvency and sustainability problems in the balance of payments, government finance, and Indonesia's finance within the short- to medium-term; as well as (iii) debt restructuring within the medium- to long-term, particularly in relation to the stance and direction of government policies for managing Indonesia's debts.

First, management of the threat of short-term liquidity problems demands quick and, at the same time planned, measures. On the domestic side, the government must be able to maintain discipline in meeting its targets for revenue from privatization and asset sales by IBRA, reduction of subsidies, and implementation of regional autonomy. Further, the government should accelerate the issuance of T-Bills or other bonds, such as medium-term notes (MTN) and floating rate notes (FRN), which can be utilized to refinance government bonds that fall due in 2002. The government should also undertake the rolling-over of bonds that mature (especially those with easy interest rates and terms), as well as the exchange of credits restructured by IBRA with bonds.

On the international side, rescheduling debts through the Paris Club becomes the first and most feasible choice. Through the Paris Club, the government has twice succeeded in having bilateral debts amounting to around $10.9 billion rescheduled. Although the postponement of debt principal repayment managed to solve short-term financial difficulties, the terms and conditions obtained from the two Paris Club reschedulings have not been optimal-especially if compared with the terms and conditions received by Pakistan. Paris Club rescheduling for Pakistan agreed to exit rescheduling amounting to $12.5 billion. This scheme enables the rescheduling of payments on Official Development Assistance (ODA) loans up to 38 years (including 15 years grace period) and on non-ODA loans to 23 years (including 8 years grace period). The treatment received by Pakistan is so outstanding that the scheme is called the Islamabad Terms.

In light of the terms obtained by Pakistan, it seems that the government of Indonesia still has many opportunities to negotiate more favorable terms and conditions at Paris Club III or later. For this, better preparation is needed, which includes explicit determination of the terms and conditions that the government wants to achieve, more intensive lobbying at the IMF and World Bank, as well as political approaches to the dominant donor countries, such as the US and Japan. If necessary, the government could consider the use of lobbyists and legal advisers of international standards, who would not only act as liaison persons but who would also fight for government interests in the coming Paris Club negotiations.

Second, one of the critical elements in handling the solvency and sustainability problem within the short- to medium-term is reduction of the debt level. On the domestic side, there are several options that can be considered, for example: (i) paying off bonds by utilizing funds from privatization and assets sales by IBRA; (ii) earmarking a certain percentage of government revenue for the reduction of bond principal; (iii) using government bonds as a monetary instrument for open market operations, which is expected to indirectly raise public confidence in government bonds; (iv) accelerating the establishment of a deposit insurance institution, which would reduce government contingent liabilities concerning the guarantee program.

On the international side, amid the unpopularity of debt haircuts and debt default options within the creditor country circle and the limited ability of the government to undertake debt buybacks, the most feasible option to reduce the principals on government offshore loans—although of a magnitude that is still limited-is debt-for-nature swaps. Currently, the US and German governments have made available the debt-for-nature swap facility. In order to take advantage of this offer, flexibility in government finances and coordination between related departments are needed to follow up on the offered nature conservation project. This facility has been utilized by a number of countries such as Bolivia, Poland ($3.6 billion), Equador ($10 million), and the Philippines ($29 million).

Success in efforts to conserve Indonesia's nature, will not only be beneficial for the Indonesian people themselves, but also constitutes a positive campaign for Indonesia in the international arena. In addition, if creditor countries consider the debt-for-nature swap program successful, it is not impossible that this program could be followed by other similar programs for larger amounts. Based on the same consideration, debt-for-development swaps should also be explored immediately in order to help reduce the level of government foreign debt.

Third, management of Indonesia's debts within the medium- to long-term is especially related to the transparency of government policies in this area.

Considering that the debt problem faced by Indonesia is complex and multi-dimensional, government policies should be comprehensive, not only in relation with government debt but also with regard to private foreign debt.

In this regard, it would be helpful to establish a separate institution to handle government debt and private foreign debt in an integrated way. As would be proper for a good debt management structure, this institution should have front-, middle-, and back-office functions. This institution would also function as an initiator, coordinator, and overseer in the debt restructuring process. This institution should also be equipped with the authority to impose sanctions, including to bring non-cooperative debtors to court. Specifically for private foreign debt, this institution should also function as a hedging institution.

In order to support the policy stance above, specifically in relation to private foreign debt, a regulation is needed to avoid reoccurrence of a condition where the private sector foreign debt exposure becomes excessive and slips out of control. This regulation should include indicators concerning ‘prudential borrowing guidelines’ in qualitative and quantitative terms.

Finally, in addition to various measures that are curative, a pro-active government role is also needed to prepare comprehensive legal instruments and implement them in a credible and serious way to prevent another debt crisis in the future.

chapter 8 BANKS AND OTHER FINANCIAL INSTITUTIONS

chapter 8

BANKS AND OTHER FINANCIAL INSTITUTIONS

In general, the performance of the banking sector has improved during 2001, following completion of the bank recapitalization program in 2000. This was particularly reflected in the improving capital structure, declining non-performing loans, and rising net interest margins. Likewise, the performance of other financial institutions (such as, finance companies and the state-owned pawn company) picked-up. Despite these improvements, the banks were unable to fully restore their function as financial intermediaries and this has impeded the economic recovery. In the non-bank sector, credit was on the rise, but the total was still small in comparison with total financing from the banking sector.

Evidence of the problem of incomplete restoration of banks intermediation is shown by the banks' loan-to-deposit ratio, which has not changed much in the past two years. Factors influencing this condition include ongoing internal consolidation among the banks and slow progress in credit and corporate restructuring. Internal consolidation was related to strategic targets of the bank restructuring program, namely fulfillment of the minimum 8% capital adequacy ratio (CAR) and the 5% indicative target for non-performing loans (NPLs). Meanwhile, slow credit and corporate restructuring stemmed from several factors, such as: extended disagreements over terms and conditions between debtors and creditors; decline in the value of collateral maintained by the Indonesian Bank Restructuring Agency (IBRA); increased country risk, which has resulted in higher interest costs and hampered foreign investors from taking over offshore corporate debts; volatility of the exchange rate; and uncertainty in legal matters.

In facing these challenges, Bank Indonesia continued the bank restructuring program and encouraged banks to provide credits to the small- and medium-scale business sector and to micro-credit projects, while respecting principles of prudent credit extensions. These two sectors have an important role in the real sector and still have large potential for boosting the economic recovery.

BANKING SECTOR

During the reporting year, national banking policies continued to be directed at sustainable bank restructuring in two major parts, namely the bank rehabilitation program and the banking system resilience program. To create a sound banking sector in the face of various complex risks, Bank Indonesia focused on fulfillment the minimum 8% CAR and the 5% indicative target for NPLs by the end of 2001. In relation to the minimum capital requirement, policies included requests to banks to add more paid-up capital, to merge with other banks, and to find new strategic (domestic and foreign) investors. Banks that failed to meet the minimum capital requirement have one final alternative to follow; an exit policy. As of November 2001, 138 banks (or 95% of the total of 145 banks) had met the minimum 8% CAR target.

With regard to the indicative target for NPLs, banks have made various efforts, including: credit restructuring which were undertaken by the banks themselves or with the mediation of Bank Indonesia's Credit Restructuring Task Force; write-offs of NPL portfolios; and the extension of new credits. As of end-2001, NPLs had improved significantly to 12.1%, but this is still far above the 5% target.

With regard to banking system resilience, Bank Indonesia continued to enhance banking supervision, using the 25 Basel Core Principles for Effective Banking Supervision that are applied internationally. In addition, Bank Indonesia continued to consistently push banks to enhance the quality of bank management (that is, good governance) and to strengthen banking infrastructure by promoting the expansion of the sharia bank network and the empowerment of Bank Perkreditan Rakyat/BPR (rural credit banks). These various policies have been successful in improving the banking sector's performance during the reporting year. For example, there were increases in banks' total assets; third-party funds; extensions of new credit; credit quality; capital; and profitability. In line with bank restructuring and the government guarantee program (which has been successful in maintaining public confidence in the banking sector), third-party funds increased, which allowed for extensions of new bank credit to the business sector.

Improved bank performance has not yet boosted the overall intermediation function. This was reflected in the continuing high share of government bonds in bank assets and the share of bond interest in banks' net interest margins. Furthermore, although new credits did increase, their utilization was low compared with commitments due to the high risk still faced by the business sector.

Banking Policies

Banking policies in the reporting year were directed at two strategic targets, namely the minimum 8% capital adequacy ratio (CAR) and the 5% indicative target for non-performing loans. In addition, Bank Indonesia continued applying the following policies, namely: (i) the bank rehabilitation program through the government guarantee program for commercial banks and BPRs, monitoring of the commercial bank recapitalization program, and continued bank credit restructuring; and (ii) strengthened banking system resilience through infrastructure development, improved bank management quality (good corporate governance), enhanced banking sector regulations and strengthened banking supervision in accordance with the 25 Basel Core Principles for Effective Banking Supervision. Based on the latest assessment by the IMF in September 2000, out of the 25 Basel Core Principles (CP), Indonesia is fully compliant with two principles. The first is CP-1 concerning Preconditions for Effective Banking Supervision (which covers Objectives, Independence and Resources, Legal Framework, Enforcement Powers, and Legal Protection). The second is CP-2 concerning Permissible Activities of Banks. There are 5 other principles for which Indonesia is "largely compliant".

Bank Rehabilitation Program

Policies on bank rehabilitation during 2001 were largely directed at the government guarantee program by continuing with the establishment of deposit insurance institutions and the credit restructuring process. Implementation of the policies concerning bank rehabilitation were particularly directed at compliance with the Letter of Intent with the IMF, which stressed the minimum 8% capital adequacy ratio (CAR) and the 5% indicative target for non-performing loans, both by the end of 2001. The objective of this program was to strengthen bank capital so that banks can better withstand shocks and comply with international standards.

Guarantee Program

In order to maintain public confidence in the banking system, the government continued the guarantee program for commercial banks and Rural Banks (BPRs). Review of the possibility for phasing out the blanket guarantee program was continued so that the planned establishment of the deposit insurance institution can be realized soon.

Implementation of the guarantee program through the interbank debt exchange offer was still undertaken by Bank Indonesia. During the reporting year, payments made for principal and interest on the exchange offer amounted to USD902.3 million, which was part of the 1999 issuance of government bonds amounting to Rp53.8 trillion.

As regards the guarantee for BPRs, an operational manual on implementation procedures for the government guarantee (in the form of a Bank Indonesia regulation concerning the BPR guarantee and exit policy) was completed in the reporting year. This Bank Indonesia regulation explains, among others, that guarantees for the BPRs are, for the time being, implemented by Bank Indonesia, which acts for and on behalf of the government, until a deposit insurance institution for BPRs is established.

Commercial Bank Recapitalization Program

With completion of the recapitalization program in 2000, it is expected that bank capital will no longer be the main constraint for bank rehabilitation. Bonds owned by the recapitalized banks can be one of their sources of funds, whether by outright sale or collateralization.

In order to support recovery of bank intermediation and development of a secondary market in bonds, the government and Bank Indonesia have allowed all recapitalization bonds owned by the banks to be traded (see the Chapter on “Monetary Conditions”). However, through the end of the review period, total government bonds traded amounted to only Rp64.7 trillion (14.9% of total bonds under recapitalization); those in the trade portfolio were Rp61.2 trillion, in the collateral portfolio, Rp3.5 trillion, and in the investment portfolio, Rp370.6 trillion. Total government bonds issued under the recapitalization

Table 8.1
Goverment Bonds for Recapitalization Program
(As of December 31, 2001)

Group of Banks	Number of Banks	Bond (Trillions of Rp)			Total (Trillions of Rp)
		Fixed Rate	Variable Rate	Hedge Bond	
Banks		**163.3**	**217.8**	**40.4**	**421.4**
State-owned banks	4	123.2	112.2	28.5	263.9
Taken over banks	4	28.9	74.3	-	103.1
Recapitalized banks	7	4.0	12.5	11.9	28.4
Regional development banks	12	0.4	0.8	-	1.2
Non Recapitalized banks	-	6.7	18.0	-	24.8
Sub-registry	-	**11.3**	**1.7**	**-**	**13.0**
Ministry of Finance	**-**	**0.9**	**-**	**-**	**0.9**
Total		**175.5**	**219.5**	**40.4**	**435.3**

program for national commercial banks in the 2001 was recorded at Rp435.3 trillion (Table 8.1).

Credit Restructuring Program

Efforts related to the restructuring of banks' problem credits were undertaken by the banks themselves or with the assistance of the Debt Restructuring Task Force established by Bank Indonesia. In addition, IBRA continued to undertake restructuring of problem-credits that have been taken over from state banks and banks participating in the recapitalization program. Meanwhile, the Jakarta Initiative continued to facilitate restructuring of offshore debts owed by non-bank companies.

Up to November 2001, problem-credits (outside the IBRA framework) that had been restructured by the banks themselves or through the mediation of the Debt Restructuring Task Force (and already at the implementation stage) stood at Rp91.8 trillion spread among 21,824 debtors. In accordance with Bank Indonesia Governor's decree number 1/15/KEP.GBI/1999 dated 1 September 1999, the service period of the Debt Restructuring Task Force in Bank Indonesia was 3 years, expiring on 31 December 2001. Credits transferred to IBRA as of December 2001 amounted to Rp310.7 trillion, of which Rp19.9 trillion had entered the implementation stage and Rp12.2 trillion had been fully paid. Credits that have been restructured and fully paid through mediation of the Jakarta Initiative came to $14.2 billion.

Strengthening Banking System Resilience

Efforts to strengthen banking system resilience continued to be implemented through infrastructure development; improved quality of bank management (that is, good corporate governance); enhancement of banking sector regulations; and strengthening of banking sector supervision. As was the case in the previous year, progress was marked by: (i) improved banking sector infrastructure as reflected in the development of BPRs and sharia banking, and on-going preparations for the establishment of deposit insurance institutions; (ii) improved quality of bank management by fit and proper tests, determination of a tighter selection process for prospective new bank managers, appointment of compliance directors, and submission of results of investigations into criminal offences in the banking sector to the law-enforcement authority; and (iii) introduction of enhanced regulations and forward-looking risk-based banking supervision using the standards developed by the Bank for International Settlements (BIS).

Improvement in Banking Infrastructure

Efforts to improve banking infrastructure during the reporting year remained focused on the expansion of BPRs and sharia banks as well as preparations to replace the blanket guarantee program with a deposit insurance scheme. These changes will help to build solid banking infrastructure and to maintain public confidence in the banking sector.

Development of BPRs

During the reporting period, cooperation continued with Gesselschaft fur Technische Zusammenarbeit (GTZ) in the Promotion of Small Financial Institutions (ProFI) project as well as with the United States Agency for International Development (USAID) and the Indonesian Bankers Institute (IBI).

This cooperation was in the form of research and seminars to empower BPRs and to improve their supervision.

Another matter undertaken in relation to BPRs was the development of a BPR database program, which has been through a system test by Bank Indonesia's Directorate for Information Technology and a user acceptance test by Bank Indonesia's Database Development Team. This program has been socialized and implemented within the environment of Bank Indonesia's head office. This database program contains the principal data, health rating, monthly report, and statistics of all BPRs in Indonesia, which are all much needed in the supervision of BPRs.

In addition, a stipulation has been drafted on the fit and proper test for owners and managers of BPRs. This stipulation is expected to provide a foundation for evaluations of persons that are capable and appropriate to manage BPRs. In a continuation of the BPR restructuring program of the year before, as of December 2001, 15 BPRs had been frozen.

Development of Sharia Banks

In order to develop sharia banking, the Bureau for Sharia Banking was established at the end of May 2001. Previously, the development of sharia banking had been handled by a temporary working team. This rise in status indicated Bank Indonesia's commitment to providing alternatives to the public in choosing suitable banking services, namely conventional and sharia systems. Bank Indonesia's policy in promoting the development of sharia banking remained based on a 4-part strategy: development of a sharia bank office network; enhancement of sharia banking regulations; socialization and research; and human resource development.

The development of a sharia bank office network was mainly directed at increasing the provision of sharia bank services. The main targets were areas where there were no sharia bank offices, but where research suggests that the public desires such a presence.

The enhancement of sharia banking regulations covered a preliminary review of the blue print for the development of sharia banking, which is expected to be a reference point in expansion of the sharia banking program. The Statement of Sharia Banking Accounting Standards (PSAKS) and the technical guidelines in the form of the Indonesian Sharia Banking Accounting Guidelines (PAPSI) have entered the finalization stage. The draft PSAKS has been approved by the National Sharia Council and they are awaiting ratification by the Board of Indonesian Accounting Standards. Meanwhile, surveys and simulations on the implementation of preliminary concepts of CAR and Productive Asset Quality for sharia banks have been completed and are countinously being enhanced.

The socialization program to enhance public education on sharia banking has been conducted intensively in various regions in cooperation with the local Moslem Religious Leader Council and universities. In addition, Bank Indonesia has undertaken research on sharia banking products, services, and regulations in the form of studies on: (i) development of cash waqaf instrument; (ii) Sharia BPRs' performance in the Jakarta-Bogor-Tangerang-Bekasi (Jabotabek) area; (iii) placements for sharia commercial banks' productive assets; (iv) reserve requirements for sharia banks; and (v) a short-term funding facility for sharia commercial banks.

In the framework of developing human resources, seminars and trainings have been held with the objective of enhancing knowledge and perceptions in various areas related to sharia banking. As technical assistance for banks within the framework of guiding and developing competence and professionalism among sharia BPRs' management, in the reporting year, Bank Indonesia held up-grading training for directors and senior officers of all sharia BPRs in Indonesia.

Deposit Insurance Institution

During 2001, the Team for Preparation for the Establishment of a Deposit Insurance Institution (LPS) has completed the final draft of the Minister of Finance decree that describes the phase out of the blanket guarantee program regulated by Minister of Finance decree number 179/KMK.017/2000 of the Minister of Finance. In the near future, the draft of the decree will be submitted to the Steering Team, which would present it to the Governor of Bank Indonesia, the Minister of Finance and the heads of related departments, before becoming formally effective.

During drafting of the decree on LPS, several new subjects were discussed intensively. These subjects included a proposal to drop the use of the term "banks under rehabilitation" because the settlement process for problem banks (exit policy) will be different from what is currently applicable.

Public socialization of the plan to establish the LPS should be continued to obtain more comprehensive input for the plan. The socialization program will be continued in large cities with significant economic activity. Meanwhile, a concept for the establishment of a LPS for BPRs has been developed. This will be discussed further with the Ministry of Finance's team for LPS, especially as regards the possibility of merging the LPS for commercial banks with that for BPRs.

Enhancement of Regulations and Stengthening of Banking Supervision

In light of the development of banking products and problems, Bank Indonesia continued to enhance banking regulations and to strengthen banking supervision. This included regulations on: micro credit projects; credits for small-scale business; limitations on rupiah transactions and foreign currency credit extensions by banks; a higher percentage of government bond portfolio that can be traded by commercial banks participating in the recapitalization program; guarantees on third-party savings and the interbank money market; implementation of the "know your customer" principle; terms and conditions and implementation procedures on government guarantees on payments of BPRs' obligations; determination on the status of BPRs under special surveillance and a freeze on business activity; commercial banks' periodic reports; obligations on the provision of minimum capital; transparency in banks' financial conditions; and the determination of status and transfer of banks to IBRA. Meanwhile, banking supervision was strengthened by changing the paradigm for supervision to forward-looking, risk-based supervision. In this regard, a Master Plan for the Enhancement of Bank Supervision Effectiveness has been developed, which uses the international standard of the *25 Basel Core Principles for Effective*

Table 8.2
IMF Assesment on 25
Basel Core Principles Compliance

Degree of Compliance	Principles	Remarks
1. Compliant (2 CPs)	• CP. 1 (1)	Objectives
	• CP. 1 (2)	Independence and Resources
	• CP. 1 (3)	Legal Framework
	• CP. 1 (4)	Enforcement Powers
	• CP. 1 (5)	Legal Protection
	• CP. 2	Permissible Activities
2. Largely Compliant, and		
• Efforts to achieve fully compliance underway (2 CPs);	• CP. 21	Accounting
	• CP. 22	Remedial Measures
	• CP. 1 (6)	Information Sharing
• Efforts to achieve fully compliance not underway (4 Cps)	• CP. 5	Investment Criteria
	• CP. 24	Host Country Supervision
	• CP. 25	Supervision of Foreign Establishments

Banking Supervision. Based on an assessment by the IMF, Indonesia has fully complied with and implemented two principles, namely: CP-1 concerning Preconditions for Effective Banking Supervision, which covers Objectives, Independence and Resources, Legal Framework, Enforcement Powers, and Legal Protection; and CP-2 concerning Permissible Activities of Banks. Meanwhile, there are 5 other principles on which Indonesia has achieved the status of "largely compliant", as shown in Table 8.2.

Enhancement of Banking Regulations

During the reporting year, Bank Indonesia has issued several regulations covering: (i) the supervision system; (ii) prudential banking principles; (iii) bank liquidity; and (iv) government guarantees.

(i) Regulations issued within the scope of the supervision system included commercial banks periodic reports,[1] obligations on the provision of minimum capital for commercial banks (CAR),[2] transparency in banks' financial condition,[3] and exit policy.[4] The regulation concerning commercial banks' periodic reports requires commercial banks to give accurate, on-time, and efficient information to support monetary policy. Regulated matters include: types of reports to be submitted; time schedule and procedures for submission and correction of reports; and sanctions for non-compliance. The regulation on CAR requires banks to provide a minimum CAR of 8% to strengthen banks' capital structure in accordance with international standards so that banks will be able to compete nationally as well as internationally. The regulation concerning transparency in banks' financial condition constitutes an effort to increase banks' transparency in the framework of creating market discipline. The regulation concerning exit policy is a follow up on the minimum 8% CAR regulation with the objective of enhancing bank supervision.

(ii) Regulations issued concerning prudential banking principles included micro credit projects,[5] credit extensions for small-scale business,[6] limitations on rupiah transactions and foreign currency credit

1 Bank Indonesia Regulation Number 3/17/PBI/2001 dated 4 October 2001 concerning Commercial Banks' Periodic Reports.

2 Bank Indonesia Regulation Number 3/21/PBI/2001 dated 13 December 2001 concerning Obligation on the Provision of Minimum Capital for Commercial Banks.

3 Bank Indonesia Regulation Number 3/22/PBI/2001 dated 13 December 2001 concerning Transparency in Banks' Financial Conditions.

4 Bank Indonesia regulation number 3/25/PBI/2001 dated 24 December 2001 concerning Determination of Status and Delivery of Banks to IBRA.

5 Bank Indonesia regulation number 3/1/PBI/2001 dated 4 January 2001 concerning Micro Credit Project as subsequently amended by Bank Indonesia Regulations Number3/8/PBI/2001 dated 25 April 2001 and Number 3/16/2001 dated 3 October 2001.

6 Bank Indonesia Regulation Number 3/2/PBI/2001 dated 4 January 2001 concerning Credit Provision for Small-Scale Business.

extensions by banks,[7] and implementation of the "know your customer" principle.[8] The regulation concerning credit extensions for small-scale business essentially raises the overall maximum credit ceiling for small-scale customers from Rp350 million to Rp500 million. The regulation concerning the limitations on rupiah transactions and foreign currency credit extensions by banks was one of the ways to limit rupiah fund outflows to offshore destinations, which can be used for speculation. It also aims to promote domestic interbank transactions. The regulation concerning the "know your customer" principle is one of the efforts to implement prudential banking principles, especially in relation to risk management in bank operations and reputation. In particular, it would help prevent the banking industry from being used for criminal activity.

(iii) A regulation issued within the scope of bank liquidity covered the rise in the percentage of the government bond portfolio that can be traded by commercial banks participating in the recapitalization program.[9] This regulation is an amendment to Circular Letter number 3/6/DPM and raises the tradable percentage from 35% to 100% to anticipate the use of government bonds as collateral in interbank transactions and intraday liquidity facilities. The amendment would also assist in development of the secondary market for trading in government bonds.

(iv) Regulations issued within the scope of government guarantees included: guarantees on international trade financing;[10] guarantees on third-party savings and the interbank money market;[11] implementation guidelines for government guarantees on commercial bank payment obligations;[12] requirements and procedures on the implementation of government guarantees on BPRs' payment obligations;[13] and guarantees on inter-bank offshore loans.[14] The regulation concerning guarantees on third-party savings and the interbank money market involves a change in the notification period for the maximum guarantee interest rate from weekly to monthly. This was done in order to reduce the influence of the maximum interest rate guaranteed by the government on monetary policy. The regulation concerning the government guarantee on commercial bank payment obligations concerned responsibility for implementation of that guarantee. Upon the issuance of this regulation, IBRA previously assisted by

7 Bank Indonesia Regulation Number 3/3/PBI/2001 dated 12 January 2001 concerning Limitation on Rupiah Transactions and Foreign Currency Credit Extensions by Banks.

8 Bank Indonesia Regulation Number 3/23/PBI/2001 dated 13 December 2001 concerning Implementation of the 'Know Your Customer Priciple'

9 Bank Indonesia Circular Letter Number 3/18/DPM dated 31 July 2001 concerning Increased Percentage of Government Bond Portfolio That Can Be Traded by Commercial Banks Participating in The Recapitalization Program.

10 Bank Indonesia Regulation Number 3/20/PBI/2001 dated 29 November 2001 concerning Guarantees on International Trade Financing.

11 Bank Indonesia Regulation Number 3/5/PBI/2001 dated 22 March 2001 concerning Guarantees on Savings and the Interbank Money Market.

12 Bank Indonesia Regulation Number 3/7/PBI/2001 dated 2 April 2001 concerning the Revocation of Bank Indonesia Board of Directors decree number 32/46/KEP/DIR dated 14 May 1999 as documented in a joint decree between Bank Indonesia Board of Directors and Chairman of IBRA number 32/46/KEP/DIR and number 181/BPPN/0599 concerning Implementation Guidelines on the Extension of Government Guarantees on Commercial Bank Payment Obligations.

13 Bank Indonesia Regulation Number 3/12/PBI/2001 dated 9 July 2001 concerning Requirements and Procedures in The Implementation of Government Guarantees on BPRs' Payment Obligations

14 Bank Indonesia Regulation Number 3/14/PBI/2001 dated 20 September 2001 concerning Inter-Bank Off-Shore Loan Guarantees.

Bank Indonesia, became fully in charge of the implementation.

(v) With regard to accounting guidelines, Bank Indonesia has improved the Indonesian Banking Accounting Guidelines (PAPI), which became effective on 13 December 2001. PAPI provides further details on the Statement of Financial Accounting Standards (PSAK) number 31 (2000 revision) concerning bank accounting and several other accounting standards for the banking industry. The improved PAPI is more comprehensive as regards the basis for regulation, accounting treatments, journal illustrations, and obligatory disclosures.

Strengthening Banking Supervision

In implementation of the Master Plan for Bank Supervision (to fulfil the Basel Core Principles and enhance prudential regulations) three regulations were issued during the reporting period, namely: i) Bank Indonesia regulations concerning Transparency in Banks' Financial Condition; ii) Requirements to Provide Minimum Capital; and iii) Determination of Banks' Status and Delivery to IBRA.

In accordance with regulations, banks that do not meet the 8% CAR requirement are placed under special surveillance. During 2001, 6 banks were put under special surveillance, comprising 4 national private commercial banks under the recapitalization program and 2 A-category national private commercial banks. IBRA is planning to merge the 4 national private commercial banks under the recapitalization program with one of the taken-over banks. The merger would save those banks from closure due to their failure to meet Bank Indonesia CAR standards. For this purpose, IBRA has submitted a request to Bank Indonesia to designate the 4 national private commercial banks as "bank under rehabilitation" and this request is currently in process. The 2 A-category national private commercial banks have committed to adding capital.

Regarding establishing the Supervision Institution for the Financial Services Sector (as stated in Act 23 of 1999 concerning Bank Indonesia), the formulation of the related draft law was still in process by the end of 2001 *(Box : Supervision Institution for the Financial Services Sector).*

Improved Quality of Bank Management (good corporate governance)

Efforts to enhance the quality of bank management continued along four lines in 2001; i) implementation of the fit and proper test programs for bank owners and management; ii) interviews with potential bank owners and management (new entries); iii) appointments of compliance directors; and iv) investigations into criminal offences in the banking sector.

Implementation of Fit and Proper Tests

Fit and proper tests are undertaken to establish the integrity of owners, and the integrity and competency of members of the board of commissioners; the board of directors; and the executive officers of the banks. The tests apply to persons who are currently active in the banks; they may be undertaken periodically or as and when needed. Since the year 1999 up to 2001, the fit and proper tests have been applied to 1,149 persons (bank owners and management).

Table 8.3
The Conduct of Good Corporate Governance
July 1999 to December 2001

Description	Candidate	Passed Approved	Passed Conditional	In Process	Fail/Un-approved	Cancelled
Fit and Proper Test Interview	1,149	593	399	-	157	-
- Owner candidate	8	8	-	-	-	-
- Management candidate	775	690	-	-	85	-
Compliance Directors	248	189	-	7	34	18

Interviews with Potential Bank Owners and Management

To ensure that banks will be owned only by responsible people with good intentions and that banks will be managed professionally, interviews are held with candidates for management, including heads of bank representative offices, and potential bank owners.

There were 40 additional candidate members interviewed during the reporting year. Cumulatively from July 1999 through December 2001, 166 banks proposed 783 candidates to be interviewed, consisting of 8 owner candidates and 775 manager candidates.

Directors of Compliance

To enforce the implementation of prudential principles in bank management, up to the end of the reporting year, 162 banks proposed 248 candidate directors of compliance.

Investigation of Criminal Offences in the Banking Sector

Bank Indonesia's Special Unit for Bank Investigation (UKIP) continued to meet with the Indonesian Police and Attorney General to discuss cases of criminal offence that have occurred in several banks, in an effort to strengthen the handling of criminal offences in the banking sector. During 2001, UKIP submitted 5 cases at 4 banks to the law-enforcement authority.

In addition, UKIP conducted socialization for the public and law-enforcement officers concerning efforts to handle deviations in the banking sector.

Institutions

Development of Commercial Banks

During the reporting year, the total number of operating banks dropped by 6 to 145 banks (Table 8.4). The change was due to the closing of one foreign exchange private commercial bank and one foreign joint venture bank, as well as the merger of joint bank (Table 8.5).

Table 8.4
Number of Banks and Bank Offices

Group of Banks	Outstanding			Growth (%)		Share[1] (%)
	1999	2000	2001	2000	2001	
I. Commercial banks						
Number of banks	164	151	145	-7.9	-4.0	100.00
Number of offices [2]	7,113	6,509	6,765	-8.5	3.9	100.00
State-owned banks						
Number of banks	5	5	5	0.0	0.0	3.45
Number of offices	1,853	1,736	1,807	-6.3	4.1	26,71
Regional development banks						
Number of banks	27	26	26	-3.7	0.0	17.93
Number of offices	825	826	857	0.1	3.8	12.67
Private national forex banks						
Number of banks	47	38	38	-19.1	0.0	26.21
Number of offices	3,798	3,302	3,432	-13.1	3.9	50.73
Private national non-forex banks						
Number of banks	45	43	42	-4.4	-2.3	28.97
Number of offices	533	535	556	0.4	3.9	8.22
Joint banks						
Number of banks	30	29	24	-3.3	-17.2	16.55
Number of offices	57	57	53	0.0	-7.0	0.78
Foreign banks						
Number of banks	10	10	10	0.0	0.0	6.90
Number of offices	47	53	60	12.8	13.2	0.89
II. Rural Credit Banks	7,772	7,764	7,703	-0.10	-0.8	-
Rural credit agencies	5,345	5,345	5,345	0	0.0	-
No-rural credit agencies	2,427	2,419	2,358	-0.33	-2.5	-

1) Share to all commercial banks
2) Excluding rural unit of BRI

Table 8.5
List of Merged and Frozen Banks in 2001

Merged Banks	Frozen Banks
March 27, 2001 merged to	
Bank Sumitomo Mitsui Indonesia	**February 5, 2001 :**
1. Bank Sakura Swadarma	1. Bank Paribas - BBD Indonesia
3. Bank Sumitomo Indonesia	
	October 29, 2001 :
September 7, 2001 merged to	
Bank UFJ Indonesia	1. Unibank
1. Sanwa Bank	
2. Tokai Lippo Bank	
September 28, 2001 merged to	
Bank Mizuho Indonesia	
1. IBJ Indonesia	
2. Daichi Kangyo Bank	
3. Fuji Internasional Bank	

Despite this smaller number of banks, the total number of bank offices rose from 6,509 to 6,765. The rise occurred in all bank groups except the foreign joint venture bank group. The rise was in line with efforts to expand the provision of services.

Of the 145 existing banks, the government owned 42 banks or 28.9% of the total number. This comprised 5 state banks; 4 taken-over banks; 7 national private commercial banks under recapitalization; and 26 regional development banks (BPDs). Of the 26 BPDs, 12 are under recapitalization. The remaining banks are comprises of 69 A-category banks (47.6%) owned by the national private sector, 24 foreign joint venture banks (16.6%) owned by the national private sector and foreign parties, and 10 foreign banks (6.9%) owned by foreign parties.

Development of BPRs

During the reporting year, the total number of operating BPRs dropped by 61 to 7,703 due to revocation of business licenses. There were 81 BPRs operating under the sharia principle, up 2 from the year before. By business activity, BPRs enjoyed significant progress, as reflected in rising total assets, credit extensions, and funding (Table 8.6). These successes raised current-year profits from Rp116 billion in 2000 to Rp200 billion in the reporting year. Although BPRs do not operate in the same market segment as commercial banks, their improved performance demonstrates a high level of public confidence in BPRs and good future prospects.

Table 8.6
Business Activities of Rural Credit Banks

Item	1999	2000	2001[1)]
	Billions of Rp		
Asset	3,462	4,731	6,020
Deposits	2,038	3,082	3,906
Credit	2,452	3,619	4,496
Capital	587	705	832
Current year profit (Loss)	7	116	200

1) up to September 2001

Development of Sharia Banks

During 2001, the total number of commercial bank branch offices operating under the sharia principle rose by 11 to 130 offices, which is in line with sharia bank development policy. This total comprises 37 branch offices of Bank Muamalat Indonesia and Bank Syariah Mandiri; 12 sharia branch offices of 3 conventional commercial banks (namely, Bank IFI, Bank BNI, and Bank Jabar); as well as 81 sharia BPRs.

During the reporting period, total assets of sharia banks rose from Rp1.71 trillion (0.17% of total banking sector assets) to Rp2.6 trillion (0.24% of total assets). A rise also occurred in accumulated funds and credit extensions, of Rp1.7 trillion and Rp1.9 trillion, respectively. These developments were in line with the rise in the total number of sharia bank offices and the socialization program undertaken to enhance public education in sharia banking.

Commercial Banks' Business Activity

The various policy measures adopted in relation to bank restructuring continued to boost commercial bank performance. In aggregate, all banking performance indicators improved during 2001, as reflected in the rise in bank total assets, funds, credit extensions, credit quality, capital, and profitability (Table 8.7).

Despite these improvements, bank intermediation has not fully recovered as expected. In its assets placement, the banking sector still saw high risks in the business sector and tended to choose short-term placements alternative with low risk, such as SBIs and interbank placements. Other factors that caused limited extensions of credit included: ongoing, internal bank consolidation in relation to the minimum capital requirement by the end of 2001; and incomplete credit and corporate

Table 8.7
Banking Indicators

Indicators	1999	2000	2001
	Trillions of Rp		
Total Assets	1,006.7	1,030.5	1,099.7
Credits	277.3	320.4	358.6
Deposits	617.6	699.1	797.4
Capital	-41.2	52.3[r]	62.3
NPL - gross (%)	32.8	18.8	12.1
NPL - net (%)	7.3	5.8	3.6
Profit (Loss) before tax	-91.7	10.5	13.1
Net Interest Margin	-38.6	22.8	37.8

restructuring. Limited bank intermediation was also reflected in low credit realizations relative to commitments and in the low loan-to-deposit ratio of the national banking sector.

Total Assets

During 2001, banks' total assets rose by 6.7% to Rp1,099.7 trillion, stemming mostly from credits and marketable securities. By composition, 38.3% (Rp421.4 trillion) of assets comprised government bonds owned by recapitalized banks or purchased by non-recapitalized banks. Meanwhile, the shares of credits and SBIs were 32.6% and 6.8%, respectively. This continuing high share of government bonds stemmed from the still illiquid secondary market and limited alternatives for low-risk placement. These conditions caused banks to hold bonds, instead of selling them to obtain fresh funds. Meanwhile, credit extensions were also relatively low, although there has been a rise in nominal terms and in the share of credit compared with 2000. Effort to raise credit included purchase of IBRA's restructured credit. This effort, however, has not yet shown the expected result. Viewed by the composition of productive assets, government bonds still had the largest share (41.4%) of the total of Rp1,018.1 trillion (Chart 8.1).

Banks' operational revenues continue to rely heavily upon interest income from bonds, due to the dominance of bonds in banks' productive assets. This indicates that bank restructuring has not yet been able to significantly improve overall bank intermediation.

Viewed from the asset ownership side, the state bank group has the largest share of banks' total assets with 48.5% (Rp533.4 trillion), followed by the

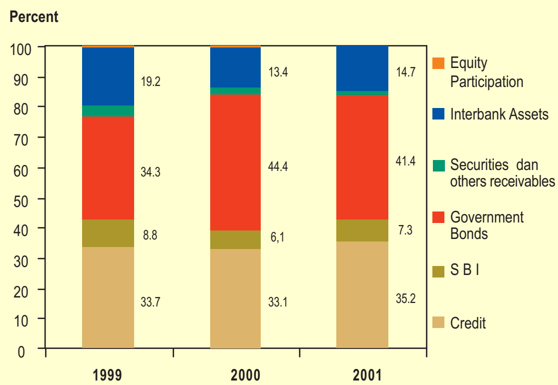


Chart 8.1
Composition of Bank Assets

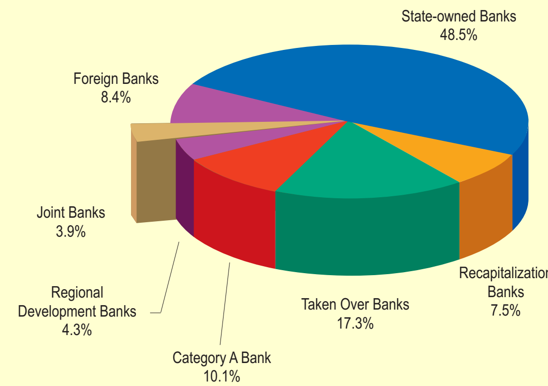


Chart 8.2
Assets by Group of Banks

taken-over bank group with 17.3% (Rp190.6 trillion). The A-category banks account for 10.1% (Rp111.1 trillion).

Funds

Third-party funds[15] mobilized by the banking sector during 2001 rose by 14.1% to Rp797.4 trillion (Table 8.8), up from 13.2% the year before. The rise in third-party funds covered all types of savings in rupiah and foreign currency; with the largest rise occurring in rupiah deposits. The main factor that prompted the rise in third-party funds was the rise in interest rates offered by banks (particularly deposit rates that approached the guarantee interest rate). Also, public confidence was sustained by the continuing government guarantee program and by bank restructuring. Rupiah third-party funds rose by 15.0%, while foreign currency third-party funds rose by 10.5%. Excluding exchange rate valuation effects, foreign currency funds rose by only 2%, and total third-party funds rose by 12.3%.

By composition, time deposits still dominated third-party funds with a share of 55.2%. The shares of current account and savings account were 23.3% and 21.5%, respectively. During 2001, current and savings accounts expanded by 15.3% and 12%, respectively, down significantly from 2000 (44.4% and 24.4%, respectively); deposits rose by 14.4%, well above last year's 0.5%, and this was largely due to

Table 8.8
Composition of Deposits

Type of Deposits	Outstanding (Trillions of Rupiah)			Growth (%)		Share (%)	
	1999	2000	2001	2000	2001	2000	2001
Demand Deposits	**111.8**	**161.5**	**186.2**	**44.4**	**15.3**	**23.1**	**23.3**
- Rupiah	68.5	103.6	120.0	51.3	15.8	64.2	64.5
- Foreign currency	43.4	57.9	66.2	33.4	14.3	35.8	35.5
Time Deposits	**382.8**	**384.7**	**439.9**	**0.5**	**14.4**	**55.0**	**55.2**
- Rupiah	301.4	296.7	344.9	-1.6	16.2	77.1	78.4
- Foreign currency	81.4	88.0	95.1	8.1	8.0	22.9	21.6
Saving Deposits	**123.0**	**152.9**	**171.3**	**24.4**	**12.0**	**21.9**	**21.5**
Total	**617.6**	**699.1**	**797.4**	**13.2**	**14.1**	**100.0**	**100.0**
- Rupiah	492.9	553.2	636.2	12.2	15.0	79.1	79.8
- Foreign currency	124.8	145.9	161.2	16.9	10.5	20.9	20.2

15 Banks' third-party funds are different from the concept discussed in the chapter on "Monetary Conditions". In the banking concept, third-party funds includes funds owned by non-residents and the government.

rupiah deposits (16.2%). The rise in deposits reflected a shift in public interest from short- to long-term placements, which reversed the preferences of 2000. The strong public interest in deposits was spurred by higher deposit interest rates offered by several banks (approaching the guarantee interest rate).

Bank Credit

During 2001, bank credit rose by 11.9% to Rp358.6 trillion (Table 8.9). This rise stemmed from rupiah credits in the amount of Rp50.6 trillion (28.4%); foreign currency credits dropped by Rp12.3 trillion (8.7%). Excluding exchange rate valuation effects, foreign currency credits dropped by 15.7% and total credit rose by only 8.8%.

Table 8.9
Composition of Bank Credits

Type of Credit	Outstanding (Trillions of Rupiah)			Growth (%)		Share (%)
	1999	2000	2001	2000	2001	2001
By Economic Sectors	**277.3**	**320.4**	**358.6**	**15.5**	**11.9**	**100.0**
Agriculture	26.1	19.9	21.3	-23.8	7.1	5.9
Mining	5.4	5.3	3.1	-1.9	-42.2	0.9
Manufacturing	97.9	109.7	118.7	12.1	8.2	33.1
Electricity	20.0	5.1	5.1	-74.5	-0.7	1.4
Construction	13.3	7.2	8.2	-45.9	14.3	2.3
Trade	45.2	46.0	49.3	1.8	7.2	13.7
Transportation	12.4	7.3	7.6	-41.1	4.1	2.1
Business Services	26.4	26.4	27.7	-	5.1	7.7
Social Services	3.3	2.9	3.6	-12.1	22.6	1.0
Others	27.3	90.6	114.1	231.9	26.0	31.8
By Category of Banks	**277.3**	**320.4**	**358.6**	**15.6**	**11.9**	**100.0**
State-owned banks	152.1	142.8	159.9	-6.1	11.9	44.6
Private national forex banks	56.5	79.4	97.6	40.5	22.9	27.2
Private national non-forex banks	5.0	10.6	10.3	112.0	-2.6	2.9
Regional development banks	13.6	11.5	17.1	-15.3	48.3	4.8
Joint banks	22.5	29.3	29.2	30.0	-0.5	8.1
Foreign banks	27.6	46.8	44.7	69.6	-4.5	12.5
By Currency	**277.3**	**320.4**	**358.6**	**15.5**	**11.9**	**100.0**
Rupiah	159.1	178.0	228.6	11.9	28.4	63.7
Foreign currency	118.2	142.4	130.1	20.5	-8.7	36.3

The rise in rupiah credits was due to new extensions of credit and resales of IBRA-restructured credits back to the banking sector. The drop in foreign currency credits was due to payoffs, write-offs, and sales of credits. During the reporting year, new bank credits amounted to Rp56.8 trillion,[16] or an average of Rp4.7 trillion per month. These new credits were mainly channeled to the industry, trade, and business services sector, by the state banks, the taken-over banks, and the A-category banks. Meanwhile, total restructured credits (either by the banks themselves or with mediation by the Debt Restructuring Task Force) through the first 11 months of 2001 were recorded at Rp91.8 trillion, up from Rp59.9 trillion in 2000. In addition (and based on IBRA's monthly report for December 2001), of the Rp310.7 trillion bank credits that have been transferred to IBRA, Rp58.2 trillion has entered the stage of the signing of Memorandums of Understanding; Rp19.9 trillion has entered the implementation of credit restructuring; and Rp12.2 trillion has been fully repaid. During 2001, no problem credits were transferred to IBRA.

Although credits rose, the bank loan-to-deposit ratio (LDR) remained virtually unchanged at 33%. Potentially, the LDR could be raised somewhat, if customers were to drawdown their credit commitments from banks. At the end of the reporting period, total undisbursed loans reached Rp70.5 trillion compared with commitments of Rp127.3 trillion. This condition suggests that the banking sector was sufficiently expansionary in credit extensions, but borrowers were not able to absorb all the available credit. This may be the result of continuing high business

16 Based on data from the Debtor Information System, supported by survey results on a number of banks.

risk in line with less conducive macroeconomic conditions, such as the unstable exchange rate, high interest rates, and unstable socio-political conditions. Another factor impeding bank intermediation is continuing internal consolidation, resulting from efforts to fulfill prudential regulations. Furthermore, credit extensions to large debtors (corporations) during the reporting year only increased slightly because most of those debtors were still under restructuring with IBRA. Based on a survey from a paper on the "Credit Crunch",[17] banks were still reluctant to extend credit to the corporate sector because the banks remain traumatized over their past experiences while developing new large scale creditors will take some time.

Quality of Bank Credit

During the reporting period, the quality of bank credit has improved in line with progress in the credit restructuring process. In nominal terms, non-performing loans (NPLs) dropped from Rp60.1 trillion in December 2000 to Rp43.4 trillion at the end of the reporting year. The gross (that is, without allowing for reserves for write-offs) NPL ratio dropped from 18.8% in December 2000 to 12.1% at the end of the reporting year (Chart 8.3). The net NPL ratio was 3.6% by the end of the reporting year. This improvement is prompted by new credit that was categorized as "current", improvement in credit quality causing "sub standard", "doubtful", and "loss", credit as well as write-offs of loss categorized credits. Although the gross NPL ratio improved, it was still above the indicative

17 Agung, Kusmiarso, Pramono, Hutapea, Prasmuko, Prastowo (2001). "Credit Crunch in Indonesia in The Aftermath of Crisis : Facts, Causes and Policy Implications". Bank Indonesia.

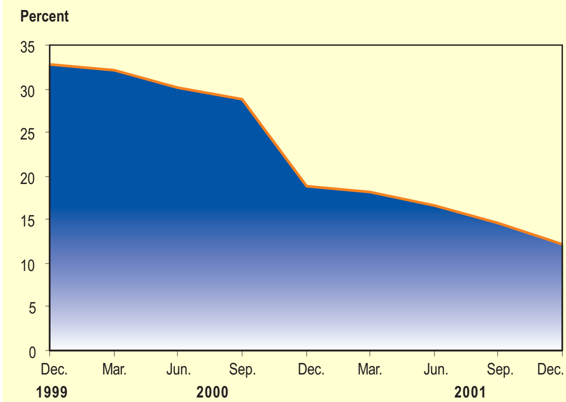


Chart 8.3
Non-Performing Loans

target of 5% set by Bank Indonesia. The continuing high NPL ratio was related to banks having given priority to achieving the 8% minimum CAR by the end of 2001. Although the target for the NPL ratio was not obligatory, its achievement would help to accelerate the recovery of bank intermediation. Along the same lines, measures to accelerate credit restructuring, to raise new credit extensions, and to transfer restructured credits from IBRA to the banking sector need to be continued. In addition, Bank Indonesia tried to accelerate credit restructuring by adjustments to the treatment of credit quality, maximum limits for credit extension, and reserves for productive asset write-offs for restructured credits.

Development of Small- and Medium-Scale Business

Throughout the reporting year, Bank Indonesia continued to boost the development of the small- and medium-scale business. This commitment took the forms of Technical Assistance for The Development of Small and Micro Business, which focuses on activities training, research, and the provision of information.

Bank Indonesia's technical assistance activities during 2001 included :

a. In the area of training, Bank Indonesia implemented training for BPR facilitators and training for small and micro business for commercial banks.
b. In the area of research, Bank Indonesia undertook a study on small-scale commodities with potential for bank financing, covering 10 commodities. This work complements the 45 Integrated Partnership Project Feasibility Models from various sectors: agriculture, industry, and services, which were researched from 1995 to 1999.
c. In the area of information provision, Bank Indonesia has entered the results of its research into the Integrated Information System for Small Business Development (SI-PUK), which can be accessed through the internet/Bank Indonesia website. This information system consists of Information System for Baseline Economic Surveys (SIB), Information System for Export-Oriented Agroindustry (SIABE), Information System for Small Business Lending (SI-LMUK), Supporting System for Investment Decisions (SPKUI), and Information System for Procedures To Obtain Credit (SI-PMK).
d. In order to encourage banks to increase their lending, particularly to small- and medium-scale business, Bank Indonesia conducted socialization in the form of seminars or workshops.

Meanwhile, another technical assistance activity still carried out by Bank Indonesia is the micro credit project, which is a joint project between the government of the Republic of Indonesia and the Asian Development Bank (ADB). With Act 23 of 1999 put into effect, Bank Indonesia should have transferred management of this micro credit project to a state-owned enterprise appointed by the government. However the funds from the ADB loan have not been fully withdrawn and the public need for credits from the micro credit project is still high. Consequently and based upon agreement between the ADB, the government, and Bank Indonesia, Bank Indonesia will continue to implement the micro credit project through the end of the loan withdrawal period, which was 30 June 2001,[18] but extended to 31 December 2001.[19]

To date, the micro credit project has covered 15 provinces, involving 24 Bank Indonesia regional offices located in various provinces in Indonesia. Meanwhile, the maximum total of credit that is given to the micro customers also has been changed a few times to adjust to national economic conditions. The latest change states that the maximum total of the first tranche given to each customer is Rp2 million with subsequent tranches of Rp5 million.[20]

During the reporting period, total credits extended by Bank Indonesia to micro business came to Rp137.4 billion, bringing total extensions of credit to micro business (from 1996 through December 2001) to Rp417.1 billion spread among 752,492 micro customers, involving BPDs, BPRs, Village Funding and Credit Institutions, and Community Self-Support Development Institutions. Based on repayments, the micro credit project was considered to be quite successful due to delinquent credits being a mere 1.2%.

18 Bank Indonesia Regulation Number 3/1/PBI/2001 dated 4 January 2001 concerning the Micro Credit Project

19 Bank Indonesia Regulation Number 3/16/PBI/2001 dated 3 October 2001 concerning amendment to Bank Indonesia Regulation Number 3/1/PBI/2001 dated 4 January 2001 concerning the Micro Credit Project.

20 Bank Indonesia Regulation Number 3/8/PBI/2001 dated 25 April 2001 concerning amendment to Bank Indonesia Regulation Number 3/1/PBI/2001 dated 4 January 2001 concerning the Micro Credit Project.

Further in relation to credit policy, Bank Indonesia has enhanced the stipulation concerning credits for small-scale business.[21] This policy is no longer an obligation, but rather it recommends credit extensions to small-scale business and it changed the ceiling to Rp500 million per customer. Realized credits to small-scale business rose by 14.8% during 2001 to Rp65 trillion (Table 8.10). With this development, as of the end of 2001, credits extended to small-scale business were equivalent to 18.5% of total banking sector credits.

Bank Indonesia also assisted small- and medium-scale business in other ways. For example, Bank Indonesia provided an opportunity for Coordinators of State-Owned Enterprises (BUMN) to re-channel the KLBI (Bank Indonesia Liquidity Credit) installment until the credit becomes due. As of end-2001, total repayments of KLBI managed by the coordinator of BUMN amounted to Rp1.45 trillion, up by around 44% compared with that of previous year. Of those repayments, Rp1.3 trillion has been re-channeled, which is up by some 186% from the previous year. The re-channeling of funds was largely executed by PT Permodalan Nasional Madani and Bank Tabungan Negara.

Looking at the continuing low re-channeling of the KLBI repayments by the coordinator of BUMN, particularly in 2000, in 2001 Bank Indonesia considered it necessary to undertake an evaluation of the implementation of KLBI management by the coordinator of BUMN. In general, the results of the evaluation concluded that the management of KLBI by the 3 the coordinator of BUMN had been sub-optimal. This was due to various problems and constraints at each the coordinator of BUMN, including the repayment period of the KLBI being shorter than the period of the credits that were to be re-lent, which could create a funding mismatch. In addition, the limited office network and capital of PT Permodalan Nasional Madani was a constraint in the low re-channeling of the KLBI repayment funds.

To cope with the problems above, Bank Indonesia made recommendations to the government to empower the coordinator of BUMN so that they can execute their tasks better. The recommendations covered the need to appoint one coordinator of BUMN as the overall manager of program credits. That manager would further be developed as a bank (or temporarily as an institution) that specifically provides funding for small- and medium-scale business.

Table 8.10
Credit to Small-Scale Enterprises

Credit to Small-Scale Enterprises	Outstanding (Trillions of Rupiah)			Growth (%)		Share (%)
	1999	2000r	2001	2000	2001	2001
By Usage	**37,2**	**56,6**	**64,9**	**52,1**	**14,8**	**100,0**
Working Capitals	15,7	22,0	27,3	40,0	23,8	42,0
Investment	5,4	7,8	9,4	44,0	21,3	14,5
Consumption	16,1	26,8	28,3	66,6	5,4	43,5
By Economic Sectors	**37,2**	**56,6**	**64,9**	**52,1**	**14,8**	**100,0**
Agriculture	7,7	9,3	11,4	19,8	23,3	17,6
Manufacturing	1,1	1,7	2,6	54,5	51,3	4,0
Trade, Restaurant and Hotel	8,8	10,3	12,8	17,0	24,0	19,7
Services	3,4	4,7	5,2	38,7	11,0	8,1
Others	16,2	30,6	32,9	89,3	7,6	50,6
By Type of Bank	**37,2**	**56,6**	**64,9**	**52,1**	**14,8**	**100,0**
State-owned banks	25,4	30,5	36,9	20,3	21,0	56,8
Private national forex banks	5,9	12,3	13,7	108,7	11,5	21,1
Private national non-forex banks	1,8	5,1	2,5	180,4	-51,3	3,8
Regional development banks	4,1	8,6	11,8	111,9	36,9	18,2
Joint and Foreign banks	0,1	0,1	0,01	-1,4	-90,3	0,01

21 Bank Indonesia Regulation Number 3/2/PBI/2001 dated 4 January 2001 concerning Provision of Credits to Small Business and Circular Letter Number 3/9/BKR dated 17 May 2001 concerning Operational Guidelines for the Provision of Credits to Small Business.

Further in relation to the development of small- and medium-scale business, various inputs have been submitted by Bank Indonesia to the government. These have covered, among others, the need to utilize available funds (related to program credits)[22] more effectively. As of the end of 2001, funds available under the Government Indebtedness Letter number 5 amounted to Rp3.1 trillion, out of which only Rp850 billion had been drawn by the government, leaving Rp2.2 trillion undrawn.

Capital

During the reporting year, bank capital rose by 19.1%, reaching Rp52.3 trillion. This rise in capital stemmed from current-year profits and from additional paid-in capital from several A-Category banks, BPDs, and foreign joint venture banks in relation to fulfillment of the 8% minimum CAR requirement by the end of 2001.

Since quarter II-2000, all bank groups have recorded positive capital. The state banks have the largest capital (Rp20.7 trillion), while the foreign banks have the smallest (Rp1.4 trillion). On an individual basis, there were A-category banks and national private commercial banks with CARs still below 8%. Efforts to raise banks' CAR to 8% included requests that bank owners add paid-in capital or undertake mergers. As of the end of 2001,[23] 138 banks or 95% of all banks had fulfilled the minimum 8% CAR target.

22 Government Indebtedness Letter number 005 in relation to program credits was issued by the government to provide program credit funding to replace KLBI funds because with the effectiveness of Act 23 of 1999 Bank Indonesia is no longer allowed to provide KLBI for program credits financing. According to Government Indebtedness Letter number 005, the available amount is Rp9.97 trillion, however withdrawals depends on KLBI that have been given to program credits that become due and accepted by Bank Indonesia in 2000 - 2001.

23 Using data up to November 2001.

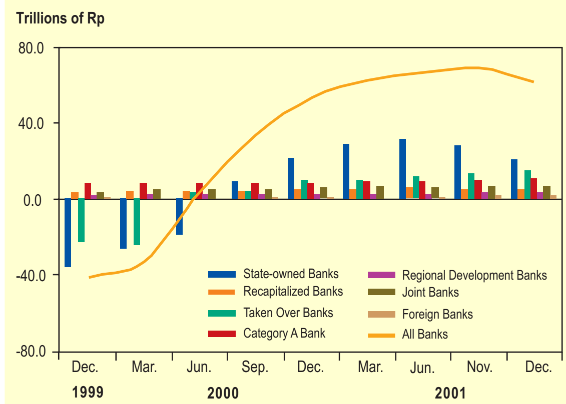


Chart 8.4
Banking Capital

Profitability

In the reporting year, banks' activities continued to improve as reflected in the rise of operating profits. Before-tax profits earned during 2001 reached Rp13.1 trillion, up by Rp10.5 trillion compared with year 2000 (Chart 8.5). Although banks still experienced operational losses of Rp0.2 trillion, this was smaller than the Rp0.7 trillion of the previous year. Banks' losses were partly due to the continuing heavy burden of building reserves for asset write-offs and other overhead costs borne by the banks. Non-operational profits earned by banks amounted to Rp13.3 trillion, rising from Rp11.2 trillion compared with the previous year. This rise mainly stemmed from profits on exchange rate valuations and on reserves for asset write-offs correction as a result of repayment of previously written-off credits.

The net interest margin (NIM) earned by banks during the reporting year rose to Rp37.8 trillion, or an average of Rp3.2 trillion per month (Chart 8.6) compared with the previous year of only Rp22.8 trillion or Rp1.9 trillion per month. The rise in NIM earned was due to the rise in credit extensions in

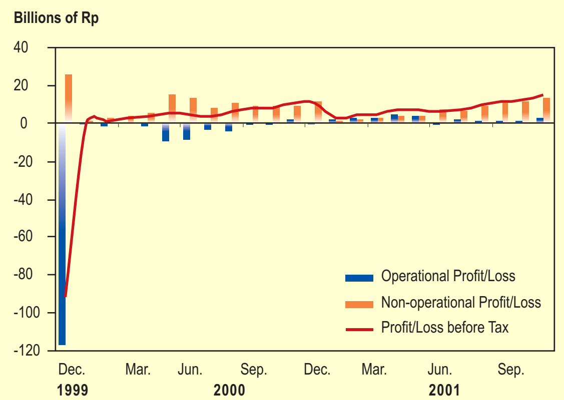


Chart 8.5
Banking Profit/Loss

2001 and higher interest revenue, originating from SBI interest and government bond interest of several recapitalized banks with variable-rate bonds. By source, banks' interest revenue mostly came from government bonds (45.3% of total interest revenue); interest revenue from credits and SBIs amounted to 32.2% and 9.7%, respectively. This condition reflected bank's continuing high dependency on interest revenue from government bonds. Among the bank groups, the taken-over banks were the most dependent on interest revenue from government

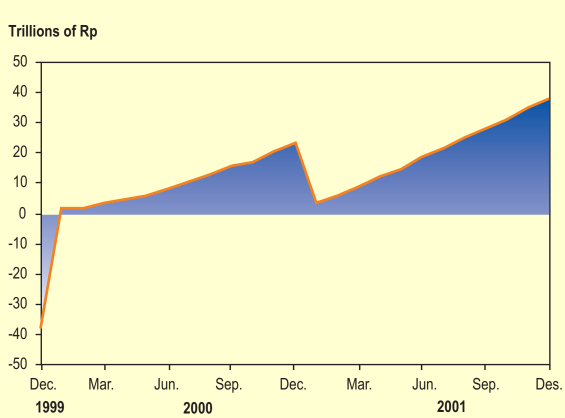


Chart 8.6
Net Interest Margin

bonds (69.1% of total interest revenue), followed by the state banks and the recapitalized national private commercial banks (56.6% and 20.4%, of total interest revenue, respectively).

OTHER FINANCIAL INSTITUTIONS

In line with better banking conditions during 2001, finance companies were able to obtain more financing from the banking sector, which enabled them to improve their own performance as reflected in expanded business activities. Meanwhile, banks' reluctance to channel credits have provided an opportunity for Perum Pegadaian (the state-owned pawn company) to expand business, mainly for public consumption and for short-term capital.

Multifinance Companies

The performance of multifinance companies during 2001 was still on an improving trend, although at a slower pace compared with the previous period. Better performance was reflected in the rise in the total value of business activities, which through November 2001 rose by 28.9% compared with the year before.

During the reporting year, three new multifinance companies were established (PT Karya Technik Multifinance, PT Kembang Delapan Delapan Multifinance, and PT Sinar Mitra Sepadan Finance), and two multifinance companies were liquidated (PT Bahan Pembinaan Usaha dan PT Bali Tunas Finance).[24] Consequently, as of November 2001, there were 246 multifnance companies.

24 Decisions were made based on: Minister of Finance decrees numbers 275/KMK.06/2001 dated 8 May 2001, 364/KMK.06/2001 and 365/KMK.06/2001 dated 11 June 2001, 626/KMK.06/2001 and 365/KMK.06/2001.

Table 8.11
Selected Indicators of Multifinance Companies

Item	Outstanding (Trillions of Rupiah)			Growth (%)	
	1999	2000r	2001 1)	2000	2001 1)
Number of companies 2)		245	245	246	
Business activities	**22.2**	**29.4**	**31.4**	**32.4**	**7.0**
Leasing	10.9	13.7	14.39	25.7	4.8
Factoring	6.4	6.6	3.4	2.3	-47.7
Credit card	0.3	0.4	0.8	19.9	89.2
Consumer finance	4.3	8.5	12.6	97.0	47.9
Others	0.2	0.2	0.3	-5.7	44.7
Borrowings	**14.4**	**17.1**	**18.5**	**18.8**	**7.9**
Domestic	14.4	17.1	18.5	18.8	**7.9**
- Bank	10.7	11.3	14.8	5.6	**30.8**
- Non-bank	3.7	5.8	3.7	56.9	**-36.7**
Foreign	10.8	12.5	11.2	15.2	**-10.3**
Bond	0.6	0.8	0.8	51.9	-1.0
Subordinated Loan	1.4	1.7	2.2	18.8	29.0

1) November 2001
2) Units

Table 8.12
Sources and Uses of Fund by Multifinance Companies

Item	Outstanding (Trillions of Rupiah)			Growth (%)	
	1999	2000r	2001 1)	2000	2001
Sources of Fund	**30.2**	**35.8**	**38.2**	**18.3**	**6.8**
Domestic bank borrowings	10.7	11.3	14.8	5.6	30.8
Foreign bank borrowings	8.6	7.6	7.26	-11.7	-4.1
Other domestic borrowings	4.7	7.1	5.0	52.7	-30.3
Other foreign borrowings	11.9	11.8	13.7	-0.4	16.1
Capital 2)	-1.3	-2.2	-0.3	-62.6	85.5
Others	-4.3	0.1	-2.2	97.4	1957.8
Uses of Funds	**30.2**	**35.8**	**38.2**	**18.3**	**6.8**
Financing	22.2	29.4	31.4	32.5	7.0
Bank deposit	5.1	3.7	3.0	-26.9	-20.7
Equity participation	0.1	0.1	0.1	1.6	-21.7
Others	2.8	2.5	3.7	-10.2	45.9

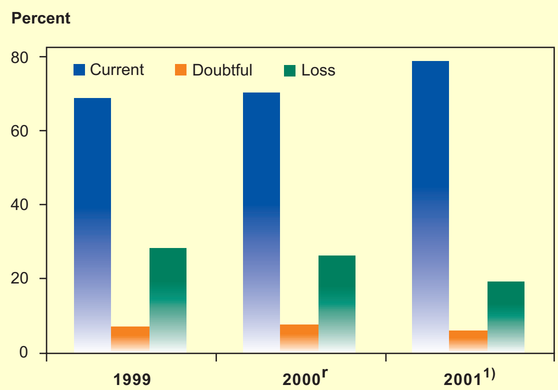
1) November
2) Net capital after compensated by unrealized profit/loss

Compared with the end of the previous year, all types of business activity of multifinance companies rose except factoring, which dropped by 47.7%. The largest rises occurred in credit cards and consumer financing of 89.2% and 47.9%. This was in line with expanding domestic consumption, which may have been assisted by financing from multifinance companies (See the "Macroeconomic" Chapter). By composition of business activities, leasing still dominated the activities of multifinance companies, reaching 45.8% of total financing. The shares of the other business activities were as follows: consumer financing at 40.0%, factoring at 10.9%, and credit cards at 2.4%.

As of November 2001, funds accumulated by multifinance companies rose by Rp2.4 trillion or up by 6.8% compared with the end of December 2000 (Table 8.12). As was the case in the previous year, their main source of funds was borrowing from domestic banks, which rose by Rp3.5 trillion to Rp14.8 trillion, in line with improved performance of the banking sector. Despite net profits of Rp396.4 million in 2001, multifinance companies' capital was still negative due to their profits being used to offset the losses of previous years.

During the reporting year, most funds were channeled in the form of financing, amounting to Rp31.4 trillion or 82.4% of total funds owned (Table 8.12). In line with slower economic growth, financing activities also experienced a slowdown, from 32.5% in 2000 to 7.0% in 2001 (up to November). Meanwhile, fund placements at banks dropped by 20.7%. This was indicated by a shift of funds from placements at banks to financing, which may indicate that extensions of financing to consumers were more profitable than placement in bank products.

The quality of multifinance companies' productive assets (comprised of marketable securities, and



1) up to November

Chart 8.7
Earning Quality of Financing Companies

Table 8.13
Quality of Earning Assets

Productive C Assets (%)	1999			2000r			2001 1)		
	D	L	C	D	L	C	D	L	
			(%)			(%)			
Financing :									
- Leasing	70.3	10.3	19.4	69.0	12.4	18.6	77.0	7.4	15.6
- Factoring	36.3	5.2	58.5	42.7	4.2	53.1	27.4	6.5	66.2
- Credit Card	31.4	3.8	64.7	66.8	1.5	31.7	75.1	2.1	22.8
- Consumer financing	90.9	2.4	6.7	94.7	1.6	3.7	96.2	1.6	2.1
Securities	88.5	2.4	9.0	88.0	0.2	11.7	82.5	6.7	10.8
Equity participation	97.8	0.0	2.2	97.7	0.0	2.3	92.9	0.2	6.9

C = Current. D = Doubtful. L = Loss
1) = November

financing activities such as leasing, factoring, credit cards, and consumer financing) also improved in 2001. Productive assets that were categorized as "current" rose from 67.8% to 78.2%. Problem productive assets (that is, those categorized as "doubtful" or "loss") dropped from 32.2% to 21.8% (Chart 8.7). Viewed by type of financing, factoring had the worst asset quality, where the share of those categorized as "loss" reached 66.2%, while the best asset quality was owned by consumer financing where the share of assets categorized as "loss" was only 2.1% (Table 8.13).

State-owned Pawn Company

The performance of the state-owned pawn company improved during 2001. This development was the result of increases in coverage and service quality through the establishment of new branches, product diversification, enhanced professionalism of its human resources, and internal restructuring of units that were considered non-productive. In addition, continued bank disintermediation provided an opportunity for the pawn company to meet needs for funds, mainly for short-term capital and consumption, particularly for the public and small- and medium-scale businesses.

In order to increase its service coverage, the pawn company has added new branch offices during 2001, bringing the total to 714 branches.[25] Meanwhile, during 2001, the pawn company diversified its products and services, including through cooperation with Usaha Aneka Tambang as the main distributor of jewelry products and the provision of assessment service for precious stones and diamonds. In addition, the pawn company provided for new types of collateral, namely gabah (un-hulled paddy) and motor vehicles, as an effort in product development to accommodate the demand of village communities.

Stronger business activity of the pawn company was reflected in the rise in business turnover (lending), business revenue, and the total number of customers. Business turnover rose by 41.1% to Rp6.0 trillion compared with the end of 2000 (Table 8.14). This growth was far higher than the 31.0% of the

25 Based on December 2001 report on operational data of the pawn company.

Table 8.14
Performance of State-owned Pawn Company

Item	1999 1)	2000 2)	2001 2)
	Millions of Rupiah		
Credit extended	3,229,280	4,230,778	5,970,310
Operational income :	449,087	373,233	553,487
- Capital leasing	417,370	341,936	500,562
- Appraisal services	16	16	27
- Consignment services	10	11	18
- Income from custody and insurance	25,319	31,270	47,033
- Others	6,372	3,929	5,847
Liabilities			
- Short-term liabilities	243,612	454,176	551,785
- Bank loan	120,067	157,631	425,240
- Others	123,545	296,545	126,545
- Bonds	389,556	439,486	635,933
- Long-term loan	100,000	105,000	105,000
- Equity	409,553	415,258	574,105
Value of auctioned goods	91,712	38,946	47,298
Number of Customer 3)	12,427,554	12,982,306	15,692,228

1) Revised data based on State-owned Pawn Company Annual Report (2000)
2) Data based on Operational Report (December 2001)
3) Persons
Source : State-owned Pawn Company

previous year, in line with increases in its services and larger number of customers. The total number of customers rose by 20.9% to 15.7 million customers, while business revenue rose by Rp180.3 billion. All types of the pawn company's business activities expanded with the largest contribution coming from its main activity, capital leasing (90.4% of total business revenue). In addition to extending credit, the pawn company also provided capital and assistance in management and marketing to its debtors, particularly small-scale businesses.

Meanwhile, credits not re-paid by customers, as reflected in the value of goods put up for auction, rose by 21.5% to Rp47.3 billion at the end of the year (Table 8.14). This was due to a rise in collateral goods unredeemed by debtors.

On the funding side, most funds came from the issuance of bonds, in the amount of Rp635.9 billion or 34.1% of total funds. During 2001, the Indonesian Rating Company (Pefindo) gave a rating of A+ to the bonds issued by the pawn company. This rating was based on the performance of the pawn company in 2000 and its small number of "delinquent" credits, as reflected in low collateral auctioned. Other sources of funds came from own capital (30.8%), bank lending (22.8%), other short-term debts (6.8%), and long-term debts (5.6%).

box

Deposit Insurance Institution

In an effort to maintain the stability and resilience of the national banking system, a mechanism needs to be created to maintain public confidence in banking institutions. One of the supporting instruments will be the availability of a financial safety net, which can provide assurance concerning the protection of customers' funds in the event that a bank fails to fulfill its obligations. The costly experience resulting from diminishing public confidence was proven after the liquidation of 16 banks in November 1997 when banking sector's liquidity dropped drastically as the result of runs on bank deposits. The lack of an explicit guarantee on public saving funds was one factor causing that bank run. To stabilize the situation, the government provided a blanket guarantee in order to regain public confidence in the banking sector. The government guarantee policy is regulated in Presidential Decree number 26/1998, which is further regulated by Minister of Finance Decree number 197/KMK.017/2000.

The policy to provide a blanket guarantee proved effective in regaining public confidence. Within a relatively short time, public funds flowed back into the banking system, and currently total public savings have reached approximately 70% of total bank assets. However, behind this success is the large burden that has to be borne by the government and the potential emergence of moral hazard in the future in the banking sector. To rectify this situation, it would be helpful to formulate a more effective guarantee of customers' savings. The concept of a limited guarantee, such as deposit insurance that is used in several countries, is one alternative. There are other alternatives, such as a joint-funding scheme, as indicated in Act 10 of 1998 concerning Banking.

With this background, a Working Team (comprising representatives from Bank Indonesia, the Ministry of Finance, and IBRA) has been appointed with the task of preparing for the establishment of the deposit insurance institution (LPS). The focus of this Working Team is diviided into two parts. The short-term agenda is to formulate a phasing-out for the guarantee coverage on almost all bank obligations; it would be limited to savings, collections (inkaso), incoming/outgoing transfers, interbank lending, and Letters of Credit.

Meanwhile, the long-term agenda is to make preparations for the establishment of deposit insurance institution, using an insurance scheme with a limited guarantee coverage. Several specific criteria for the deposit insurance institutions also need to be determined including, institutional status, premiums, and membership.

To enable LPS to execute its tasks effectively, there needs to be a guarantee of its independence in executing its tasks and authority. It is expected that the LPS would be a legal entity outside the government, accountable directly to the People's Representatives. With regard to the determination of the guarantee premium, for the time being, a flat-fee pattern will be adopted. It is planned to impose risk-adjusted fees soon to reflect different risks, objectively assessed on each of the banks. The membership of the LPS will be compulsory for all banks operating in Indonesia, including foreign banks, to ensure equal business opportunities.

The establishment of LPS of course will take into account several prerequisites, including the existence of a sounds and stable banking system. In line with this prerequisite, bank restructuring needs to be continued. It is expected that a period of 3 years from 2001 will be sufficient for making preparations on the establishment of this institution, and as such year 2004 is considered the right time to start applying guarantees based on LPS.

box

Blueprint for The Development of Sharia Banking

Act 10 of 1998 and Act 23 of 1999 have mandated and given the legal basis for Bank Indonesia to develop sharia banking in Indonesia. In addition, the development of sharia banking is considered important: (i) to fulfill a public need for the provision of bank services that are in accordance with sharia principles; (ii) to mobilize public funds that have not been absorbed by the existing banking system; (iii) to enhance national banking system resilience; and (iv) to provide a facility for international investors to undertake financing and financial transactions in accordance with sharia principles.

In relation to the efforts to develop sharia banking, there are a number of problems that need to be tackled immediately and others that may be tackled within short-, medium-, and long-term time frame. Incomplete regulations and infrastructure for sharia banks are one of the basic problems that need to be tackled immediately so that sharia banks can operate at an optimal level in accordance with their special characteristics. Enhancement of regulations for sharia banking becomes very important, considering that existing regulations do not fully accommodate sharia banking business activities. On another side, the relatively low public understanding on the operations of sharia banking and the limited availability of experts in sharia banking are challenges in the development of sharia banking. In addition, the relatively limited office network of sharia banking implies limited service for customers that desire sharia banking services. In addition, supporting institutions for effective sharia banking are also believed to be insufficient. Moreover, a number of issues related to technology development and wider banking products require some regulation in order to assist development of sharia banking.

The development of national sharia banking is also influenced by globalization of financial services. A number of issues related to international sharia banking need attention so that the national sharia banking institution will be accepted internationally. The main issues include: (i) establishment of an International Islamic Financial Market (IIFM), which is currently at the finalization stage and is expected to support the efficient management of funds internationally; and (ii) 18 member countries of the IMF are currently making preparations for the establishment of the Islamic Financial Services Organization (IFSO), an international institution that will issue prudential regulations for sharia banks.

Realizing the complexity of efforts to develop sharia banking, there is a need for clear policy directions in the development of national sharia banking. For this purpose, a Blueprint for the Development of Sharia Banking needs to be developed, which is expected to provide the following benefits, among others: (i) standard guidelines for Bank Indonesia in developing sharia banking in stages; (ii) a reference for external parties in economic development and for other sharia financial institutions; (iii) ensuring sustainability in regulation and supervision of sharia banks;

and (iv) the provision of sharia banking that is healthy and consistent (istiqamah) with sharia principles.

Bank Indonesia's mission in developing *sharia* banking is to nurture a climate conducive to the development of healthy *sharia* banking, fully consistent with *sharia* principles. Further, the vision for the development of *sharia* banking is the realization of a banking service that is able to activate the real sector through equity-based financing within the framework of helping one another (*ta'awun*) and directed for the good (*fastabiqul khairat*) in order to achieve public goodness prosperity (*rahmatan lil alamin*). To achieve that mission and vision, Bank Indonesia's policies in developing sharia banking are based on the principles of a fair, gradual, sustainable and market-driven approach that is consistent with sharia principles and international standards.

Sharia banking that is in accordance with above mission and vision, is also related to accompanying values with micro and macro perspectives. A micro perspective is related to values in the sharia bank management, namely the values of *Shidiq, Tabligh, Amanah, Fathanah,* including *Ri'ayah* (correct and polite) and Mas'uliyah (responsible). The macro perspective is more related to the existence of *sharia* banking that reflects *zakat* values in promoting investments, eliminating uncertainty *(ghoror)* in order to promote transparency, eliminating *riba* (interest) in order to avoid predetermined results and preparedness to face risks, and to eliminate *maisir* in order to promote linkages to the real sector.

In accordance with the principles of gradualism and sustainability, noted above, the development of sharia banking has certain objectives by well-defined time horizons. Within the short-term period (2002-2004), the objective is to position sharia banking so that it becomes an alternative to conventional banking. Within the medium-term (2004-2008), the objective is for *sharia* banks to take a more active role in promoting the real sector. While the long-term objective (2006-2011) is to make *sharia* banks more efficient and for them to operate internationally.

box

Supervision Institution for the Financial Services Sector

As mandated in Article 34, Act 23 of 1999 concerning Bank Indonesia, there should be a new institution for consolidated supervision of the financial sector. In accordance with this mandate, the bank supervision function will be transferred from Bank Indonesia to this new independent institution, which has to be established before 31 December 2002. With the transfer of this supervision function, Bank Indonesia will only function as the monetary authority with its main task focused on monetary and payment system issues. The idea of segregating the bank supervision function and transferring it from the central bank to another institution is not a new one in the banking supervision practice in other countries. Britain, Japan, Korea, and Australia are examples of countries that have transferred the supervision function and task from the central bank to another institution.

Although institutionally the bank supervision function will be given to a new institution, Bank Indonesia still has the authority and responsibility for maintaining overall financial system stability. Bank Indonesia's function in maintaining financial system stability related to banks and other financial institutions will involve handling systemic risks faced by banks as well as the overall financial industry. Systemic risk involves risks faced by several banks, which have the potential to spread (domino effect) instability throughout the entire banking and financial industry. Consequently, its handling must be conducted on a macro basis. The new Supervision Institution for the Financial Services Sector will put more emphasis on micro aspects of banking, namely prudential regulations in terms of individual banks and non-bank financial institutions' compliance with all prevailing stipulations.

Structure wise, the new Supervision Institution for the Financial Services Sector is planned to be a government institution outside the cabinet, which is accountable to the President. The objective of the establishment of this institute is to undertake supervision over all institutions providing financial services in the framework of creating a healthy, accountable and competitive financial services industry. The coverage of the tasks of the new institution will include the supervision of banks and all non-bank financial institutions, such as insurance, venture capital companies, pawn companies, leasing companies, pension funds, security companies, and other financial services companies, including public fund managers.

Currently, supervision of the various financial services companies is conducted by various institutions which are not integrated with one another. For example, the authority for the supervision of banks is under Bank Indonesia, the authority for the supervision of security companies is under the Capital Market Supervisory Board (Bapepam), and the authority for the supervision of insurance companies is under the Minister of Finance. The existence of many different financial services supervisory institutions that are not related with one another, in some cases, has caused overlapping authority and inefficiencies in coordination among these institutions. In addition, the relationship between banks and non-bank financial institutions is very close with similarities in business operations and risks. With the establishment of one institution that supervises overall financial services, it is expected that supervision over those institutions can be more efficient and conducted in a consolidated and integrated way, which in the end will be more beneficial for all stakeholders.

Conceptually, the Supervision Institution for the Financial Services Sector will not only have authority to supervise, but will also have the authority to regulate, including to issue and revoke business licenses of financial service management institutions. In addition, to ease investigation of illegal practices in the financial sector, the new institution will also be given the authority to investigate, such as that held by other law-enforcement apparatuses, although this authority would be limited to the financial sector. With the termination of Bank Indonesia's functions in these areas, there is a need to amend Act 7 of 1992 concerning banks as amended by Act 10 of 1998.

A team comprising members from the Ministry of Finance, Bank Indonesia, the Capital Market Supervisory Board, and the Department of Law, assisted by consultants from ADB, have been working for two years to formulate the review and concept of the new financial service supervisory authority. Up to now, the team has succeeded in developing the blueprint for the establishment of the Supervision Institution for the Financial Services Sector as well as a draft law concerning this new institution. It is expected that the draft act will be submitted for approval in mid-2002 so that, by the end of 2002, it can be enacted as law and the institution can be established. After the institution is established, the transfer of banking supervision and regulation from Bank Indonesia to the new institution will be done gradually. Consequently, preparations will be needed in Bank Indonesia and in the new institution, particularly concerning systems, data/information, and human resources in order for the transfer process to run without disruptions.

box

The Integrated Information System for Small Business Development (IIS-SBD)

In an effort to provide greater value added and benefits from research on the development of small business, it is considered necessary to widely disseminate research findings to the public. In this regard, Bank Indonesia has made available some results of its research in an Integrated Information System for Small Business Development (SI-PUK), which can be accessed via the internet/Bank Indonesia's website in Bahasa Indonesia and English. SI-PUK constitutes a group of internet-based information systems for small business, which have been developed by Bank Indonesia in an integrated way to provide information that is easily accessible by the users. The information systems integrated into the SI-PUK are as follows:

1. Information System for the Baseline Economic Survey (SIB)

   Research on basic economic potential (known as the Baseline Economic Survey, and conducted since 1979) is preliminary research on the potential of economic subsectors and commodities in provinces, particularly in relation to the development of small business. In order to spread the results of the Baseline Economic Survey, those results are transfered into an information system known as Information System for the Baseline Economic Survey (SIB). The benefits of the SIB are: (i) to give information on economic subsectors/commodities that have developmental potential; and (ii) to identify opportunities for small business as well as the positive and negative factors influencing them.

   Information provided in the SIB covers results of the research over 23 provinces: North Sumatra, Riau, West Sumatra, South Sumatra, Jambi, Bengkulu, Lampung, Jakarta, West Java, Central Java, Yogyakarta, East Java, East Kalimantan, West Kalimantan, South East Kalimantan, North Sulawesi, South Sulawesi, Bali, West Nusa Tenggara, and East Nusa Tenggara. In an effort to maintain timely information, an update of the research is undertaken every five years. The final result of the Baseline Economic Survey is a Priority List of economic subsectors and commodities that have potential for development in each Province, District, and Sub-Distric region grouped into three categories: high Potential (Sangat Potensial/SP), Potential (Potensial/P), and Lacking Potential (Kurang Potensial/KP). These categories are viewed from 6 perspectives: Marketing, Entrepreneurship, Production Technique, Growth, Infrastructure, and Government Policy towards small business development.

2. Information System for Export-Oriented Agroindustry (SIABE)

   In an effort to reduce the impact of the economic crisis, in 1999 Bank Indonesia developed the Information System for Export-Oriented Agroindustry (SIABE). The system contains data from research on agroindusry commodities with the potential for export. The purpose includes the provision of public information for the banks and prospective foreign importers, concerning the various agroindustry commodities that have the potential for export. Other information includes: (i) commodity profiles, technology processes, raw material areas, export volumes, regulations concerning export tariffs, export values, export-destination countries, and names of exporters; (ii) volume and value of exports for each destination country, by each province; (iii) list of exporters, covering names, addresses, contact persons, telephone/facsimile numbers, types of commodities, and provinces; (iv) potential areas for the commodities in each Province and district; (v) quality standards, tariff constraints, and export regulations. All this information is expected to help prospective foreign importers cooperate with domestic exporters, which in the end will increase exports of agroindustry commodities and raise foreign currency inflows.

Meanwhile, information in the SIABE includes research on 15 commodities: leather, cassava, palm oil, cashew nut, shrimp, rubber, chocolate, coffee, tea, furniture (teak/mahogany wood), cinnamon, patchouli (nilam), fish, pepper, tobacco, including derivative products of around 500 commodities, covering 23 provinces as with the SIB.

3. Information System for Small Business Financing/ Lending Model (SI-LMUK)

   The Information System for Small Business Financing/Lending Model (SI-LMUK) is an information system that provides the results of Bank Indonesia's research on financing for small business with the potential for development. This information on financing could be used by business people as preliminary information for banks in financing a commodity.

   The coverage of the SI-LMUK includes marketing, production techniques, finances, economic and environment impact. Currently, there are 37 models of business financing provided by the system.

4. Supporting System for Investment Decision (SPKUI)

   This system complements the SI-LMUK and can be used for business simulation. The simulation is performed by changing the data for volume and/ or value in the financial analysis of the lending model, which represent assumptions used for investment cost/financing, profit-loss, and cash flow.

   Through this system, a user can automatically and quickly calculate the financing of a commodity in a lending model. The calculation simulation is expected to quickly provide users with a picture of the financial feasibility of a business in accordance with the conditions of the region and the commodity.

5. Information System for Procedures to Obtain Credit (SI-PMK)

   This system provides information to prospective customers on the procedures for submitting a credit request to a bank. Through this information system, prospective bank borrowers learn the general procedures for requesting credit from banks, although each bank has its own procedures for credit requests, such as the request form and other requirements.

The coverage of this system includes information concerning the meaning, function, benefit, management, and types of credit, as well as procedures to obtain credit and business feasibility analysis using financial ratios of the prospective debtors.

chapter 9 PAYMENT SYSTEM

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PAYMENT SYSTEM

Within the framework of fulfilling Bank Indonesia's objective as stated in Act 23 of 1999 concerning Bank Indonesia, which is to achieve and maintain stability in the value of the rupiah, a payment system that is efficient, fast, safe, and reliable is needed to support the implementation of monetary policy and the development of a prudent banking system. To realize this policy objective, various policies in the cash and non-cash payment systems have been adopted.

During 2001, policies in cash payment system area included Bank Indonesia's measures to enhance cash-related services to banks, to enhance distribution of small denominations of bank notes in cooperation with third parties, and to distribute new bank notes with designs and sizes that are in accordance with Bank Indonesia's standards. Meanwhile, in the non-cash payment system area, policies are directed at reducing interbank payment risk that could disrupt financial stability; supporting implementation of monetary policy; enhancing the quality and capacity of payment system services; strengthening regulations; and improving regulatory supervision of the payment system.

PAYMENT SYSTEM POLICY IN 2001

In 2001, the supply of money increase in line with the expanding role of the small- and medium-scale business sector and the informal sector of the Indonesian economy, which use more own- financing than financing from the banking sector. Also, there were exceptional public needs for cash in relation to Ramadhan, Idul Fitri, Christmas, and New Years, whose timing nearly converged in 2001. Aside from that, in order to standardize the sizes of rupiah bank notes and enhance security features of bank notes, Bank Indonesia has issued notes of Rp5,000 denomination with a new design and in the same size as the Rp1,000 denomination bank notes and the Rp100,000 plastic bank notes. Further, in order to fulfill public needs for small denominations (Rp5,000 and below), a pilot project has been developed in cooperation with third parties for the distribution of small denominations in Jakarta. With this policy, the public can obtain the small denominations needed free of charge at those third parties, operating at public centers.

In addition, Bank Indonesia also undertook cooperation with several state universities, namely Sepuluh November Technology Institute and University of Gajah Mada, Yogyakarta, to conduct research on Indonesian plants that could be used as alternative raw materials for bank notes. This is expected to reduce the dependence on imports and to enhance Bank Indonesia's efficiency. Further, in order to enhance cash services to the public, Bank Indonesia has implemented the Automated Cash Administration and Currency Circulation Information System, whereby cash activities at head office can be done on-line.

With regard to counterfeiting of rupiah, Bank Indonesia has adopted preventive and repressive measures to tackle that problem. Preventive measures included enhancement of currency design and increased usage of security features in the printing of new issues of rupiah bank notes. In addition, Bank Indonesia also disseminated information on features of genuine rupiah currency; distributed widely posters and stickers regarding easy ways to recognize authentic rupiah currency; enhanced upgrading activities; and prepared public service advertisements on television in cooperation with the Police. Another effort was to enhance coordination with related parties that are members of the National Coordinationg Board for Counterfeiting and Forgeries Eradication (Botasupal).

Repressive efforts were made by coordination with related parties in the arrest of parties involved in counterfeiting and in bringing them to court. The amount of counterfeit money discovered in 2001 was smaller than the year before. However, quality was better due to technology improvements, for example computers and scanners.

With regard to the non-cash payment system, the Bank Indonesia - Real Time Gross Settlement system (BI-RTGS), a mechanism for interbank payment settlement of high value and urgent payments has been implemented in 12 Bank Indonesia regional offices in Bandung, Surabaya, Denpasar, Samarinda, Balikpapan, Manado, Medan, Padang, Batam, Pekanbaru, Semarang, and Yogyakarta. Implementation of the BI-RTGS system in Bank Indonesia regional offices accomplishes two functions. First, it accelerate fund transfers and flows. And second, it supports implementation of the centralized settlement account.

When the BI-RTGS system has been implemented in all areas of Bank Indonesia regional offices, each bank in Indonesia will only maintain one current account at Bank Indonesia. By the end of 2001, the number of accounts that were maintained at Bank Indonesia decreased from 38 accounts to 26 accounts. This comprises 1 account at the RTGS Central Computer (which is a combined account from bank current accounts originally at Bank Indonesia head office and 12 Bank Indonesia regional offices that have implemented the BI-RTGS system) and 25 current accounts representing the accounting system at 25 Bank Indonesia regional offices that have not implemented the BI-RTGS system.

The maintenance of only one account for each bank at Bank Indonesia will assist the tasks of monitoring bank compliance in fulfilling the minimum reserve requirements (GWM) and monitoring bank liquidity, particularly for banks that are experiencing liquidity problems. From the banks' side, the maintenance of one account at Bank Indonesia will be easier than 38 accounts.

Meanwhile, in order to improve the efficiency and effectiveness of the electronic and automated clearing systems, a facility is needed to provide information on the results of local clearing operations in an early, accurate, complete, safe, and fast manner, and that can be accessed through a remote system. Accordingly, Bank Indonesia has developed a facility for dissemination of information known by the name Remote Acces Clearing Information System (RAIS). The RAIS is the follow-up on the policy for standardization of systems and supporting matters for clearing operations run by Bank Indonesia. Currently, dissemination of information on available clearing results is done through the facilities of the Money Market Information Center and Electronic Clearing Terminal of the Jakarta Electronic Clearing System. This system still have limitations in providing the information of clearing position.

Development of the RAIS will enhance the quality and capacity of payment system services and fulfill the information needs of clearing member by providing results of clearing calculations in a faster, informative and timely manner. With the RAIS, clearing participating banks can access data and other information on their daily clearing position through the internet facility.

During 2001, development of the RAIS went through an internal trial run conducted by Bank Indonesia and by banks, covering comprehensive activities from registration up to access the information. The system was first implemented in the Bank Indonesia regional office in Surabaya in November 2001. The Surabaya regional office was chosen for the first implementation of this system because of its large share of clearing transactions (after Jakarta) and its "voice kit" was no longer functioning. To standardize operations for participants and operators, a guidance manual for the operation of the RAIS was developed at the end of 2001. It covers procedures for the use of all functional menus.

Another aspects of the clearing process that should get more attention is data security. To extend the storage life of clearing transaction data, another storage media has been added in the form of a CD Burner. This media is able to store clearing images for more than 10 years. Longer storage life of clearing images will support (external and internal) audits and investigations into clearing activities. The CD Burner system will be installed in four offices: the Jakarta head office, Surabaya, Medan, and Bandung. During 2001, this system was installed in the Jakarta head office and the Surabaya regional office. With regard to the Bank Indonesia Medan and Bandung regional offices, the system is planned to be installed in 2002 when clearing operations in these two offices will be automated in image-based.

Concerning strengthening of regulations and supervision of the payment system, the following matters have been undertaken:

1. **Amendment of Bank Indonesia Regulation Number 2/24/PBI/2000 Concerning Current Account arrangement between Bank Indonesia and External Parties**

   Based on Bank Indonesia regulation number 2/24/PBI/2000, the only external parties that can open current accounts at Bank Indonesia are: banks; the Ministry of Finance in relation to the implementation of state budget; and the International Monetary Fund (IMF). This limited number of parties has an impact on the implementation of Bank Indonesia's tasks concerning monetary policy, the payment system, and settlement of liquidity credit policies.

   To anticipate future possible problems resulting from this limitation, it would be helpful to broaden the coverage of external parties that can open current accounts at Bank Indonesia. In this regard, on 20 June 2001, Bank Indonesia regulation number 3/11/PBI/2001 was issued which enables banks, government institutions, international financial institutions, and other institutions to open current accounts at Bank Indonesia.

2. **Drafting of Bank Indonesia Regulation Concerning The Operation of The Payment System Services Using Non-Cash Payment Instruments And Supporting Services**

   Article 15 of Act 23 of 1999 concerning Bank Indonesia states that the licensing, regulation and supervision of the payment system services are under the authority of Bank Indonesia. Currently, there are a number of authorities regulating payment system services, for example the Ministry of Finance. In addition, the plan to establish the Institution for the Supervision of Financial Service Sector will add another institution with authority to regulate payment system services. It is feared that this will create duplication in regulation and supervision, and therefore more explicit regulation of inter-department authority limits is needed. To handle this, a draft Bank Indonesia regulation is being developed concerning The Operation of The Payment System Services Using Non-Cash Payment Instruments and Supporting Services.

3. **Supervision of The Payment System**

   In the general provision of Act 23 of 1999, it is stated that Bank Indonesia is also given the authority and responsibility related to the supervision of payment system services so that the public can obtain the services of a payment system that is efficient, fast, and safe. Supervision of the payment system in this manner protects the financial system from possible domino effects in the event that participants in the payment system experience credit or liquidity risks.

   To minimize or eliminate systemic risks arising from operation of the payment system, in 2001 a mechanism for the supervision of an overall payment system was under review and development. It will be formulated into an academic paper concerning the national payment system supervision. With the existence of a comprehensive supervision mechanism, the supervision of the payment system can be performed in a more accurate and focused manner. Coverage of payment system supervision will include clearing activities, the BI-RTGS system, card-based payment systems (ATM cards, credit cards, debit cards, and prepaid cards) and their supporting services.

4. **Development of Guidelines for The Assessment on The Operations of the Clearing System and the BI-RTGS System**

   In order to maintain financial stability, a systemically important payment system needs to be protected from systemic risks. Based on Core Principles for Systemically Important Payment Systems, developed by the Bank for International Settlements (BIS), Bank Indonesia is currently undertaking an assessment of its fulfillment of these payment system principles.

   By the end of 2001, assessment guidelines had been developed to evaluate operation of the payment system with the BIS Core Principles for Systemically Important Payment Systems. At the preliminary stage, the assessment is applied to the clearing system and the BI-RTGS system. It is expected that gradually the assessment can also be applied to payments systems operated by other parties outside Bank Indonesia even though those systems are not categorized as systemically important. These exercises are intended to demonstrate that Bank Indonesia is committed to meeting the BIS Core Principles for the operation of payments systems in Indonesia.

DEVELOPMENT OF PAYMENT INSTRUMENTS

In line with rising economic activity in 2001, use of cash and non-cash payment instruments rose from the year before. In addition, the near convergence of the religious holidays and New Years sharply increased the use of both types of payment instruments.

Cash Payment Instruments

The position of currency in circulation at the end of December 2001 reached Rp91.3 trillion, up only 1.76% from the same period the year before, largely due to shifting seasonal factors. By contrast, the average end-of-month position of currency in circulation in 2001 reached Rp77.0 trillion, up 18.48% from the monthly average of the year before. The rise in currency in circulation generally reflected strong public demand for currency in line with national economic development. Steep rises occurred in the months of November and December 2001, due to large withdrawals by the public in relation to Ramadhan, Idul Fitri, Christmas, and New Year of 2002, which nearly converged.

Viewed by type of currency, the proportion of bank notes and coins during quarter 2001 did not change much, with the share of each type at 98% and 2%, respectively. By denomination, the position of currency in circulation was dominated by the Rp100,000 and Rp50,000 denominations with their shares of total currency in circulation reaching 41.35 % and 28.90%, respectively.

Table 9.1
Currency in Circulation by Denomination

Item	Dec 1997	Dec 1998	Dec 1999	Dec 2000	Dec 2001
	Trillions of Rupiah				
Currency in Circulation	33.6	48.5	72.6	89.7	91.3
Banknotes	32.9	47.5	71.2	87.9	89.6
Coins	0.7	1.0	1.4	1.8	1.7

To meet public needs for currency in 2001, Bank Indonesia supplied 4.0 billion new bank notes (worth Rp48.1 trillion) and 1.7 billion coins (worth Rp0.4 trillion). Most (around Rp33.4 trillion) were used to replace currency that had been destroyed because it was no longer fit for circulation. The rest was to meet rising economic needs and to increase Bank Indonesia's stock of currency. Printing by Perum Peruri (the state-owned currency printing company) up to December 2001 amounted to Rp41.3 trillion or 85.15% of total provision of currency. Bank Indonesia's cash position at the end of 2001 was quite safe at Rp34.1 trillion, sufficient to fulfill more than 2 months of average public demand.

Table 9.2
Destroyed Banknotes

Period	Denomination								Total
	100,000	50,000	20,000	10,000	5,000	1,000	500	100	
	Billions of Rupiah								
1994		870	2,199	6,345	2,214	924	385	66	13,003
1995		749	2,247	3,920	1,615	894	407	56	9,889
1996		2,789	7,363	8,618	1,726	1,016	474	50	22,035
1997		3,615	8,301	8,440	1,866	1,277	564	36	24,099
1998		2,103	3,506	5,046	2,209	882	428	15	14,187
1999	0	20,645	12,473	10,582	3,461	805	362	6	48,333
2000	51	42,940	13,360	6,872	2,404	867	261	10	66,765
2001	354	15,092	9,637	5,144	2,329	642	144	20	33,362

In addition to providing currencies in sufficient amount, Bank Indonesia also maintains the quality of currency held by the public by adopting a "clean money policy". This operates by withdrawing and destroying currencies that are no longer fit for circulation (known as *Pemberian Tanda Tidak Berharga*/PTTB), and replacing them with new currencies. Total PTTB currencies in 2001 was Rp33.4 trillion, down 50% from the year before. This drop in PTTB currencies stemmed from the implementation of the policy to reduce PTTB currencies for large denomination notes (Rp50,000 and Rp20,000 denominations).

In nominal terms, the largest part (45.24%) of total PTTB currencies consisted of Rp50,000 denomination, followed by Rp20,000 denomination at 28.89%, and Rp10,000 denomination at 15.42%. Viewed by number of notes, the largest part (22.16%) of PTTB currencies consisted of Rp1,000 denominations, followed by Rp10,000 denomination at 17.75% and Rp20,000 at 16.62%.

Development of Cash Inflows/Outflows and Cash Position

Cash inflows on a national basis have tended to fluctuate. The average monthly cash inflow in 2001 was Rp15.4 trillion, up 24.48% from 2000. Meanwhile, the average monthly cash outflow in 2001 was Rp15.6 trillion, up 13.55% from 2000.

Net outflows amounted to Rp1.8 trillion in 2001 or an average of Rp0.15 trillion/month. By area, almost all Bank Indonesia regional offices outside Java experienced a net outflow, while those on-Java (except Jakarta) experienced a net inflow. This was mainly due to most of public spending/expenditure activities having flowed to Java.

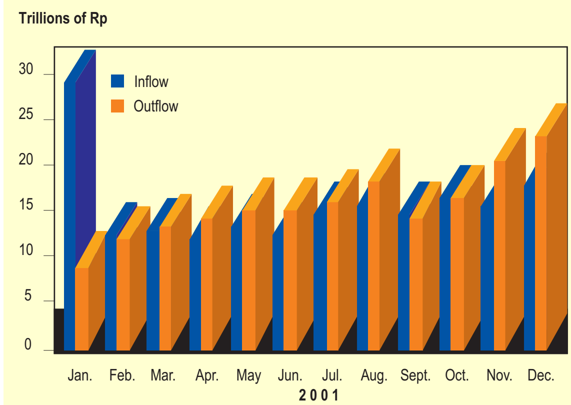

Chart 9.1
Flows of Currency

The cash position of Bank Indonesia at the end of 2001 stood at Rp34.1 trillion, up 22.91% compared with that at the end of 2000. This rise in cash position was in line with the drop in the amount of PTTB currencies, due to the policy to focus PTTB on Rp50,000 and Rp20,000 denominations.

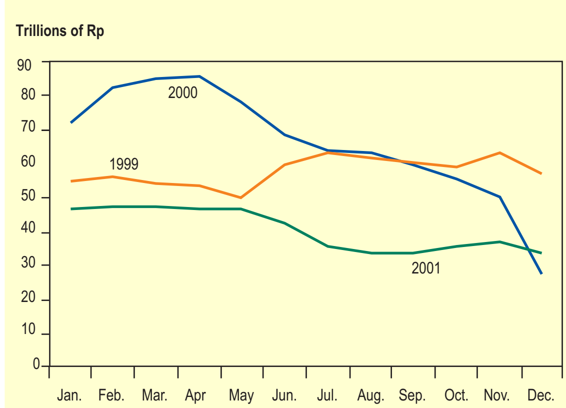

Chart 9.2
Currency Held by Bank Indonesia

Development of Counterfeiting

Discoveries of counterfeit money (from reports by banks, the Police, and Bank Indonesia) for the period January up to November 2001, amounted to 97,642 notes (for a value of Rp3.88 billion). Of that total, most notes were of the Rp50,000 denomination amounting to 65,307 notes (66.88%), followed by the Rp20,000 denomination amounting to 25,305 notes seized (25.92%). The total of counterfeit money discovered dropped by 30.31%, from 322,108 notes for the same period in 2000 to 97,642 notes.

The Police discovered most of this counterfeit money before it circulated among the public. Data for January up to November 2001 showed that 63.42% of this counterfeit money was from Police reports; the remainder was from bank reports.

Although the amount of counterfeit money discovered in 2001 dropped, Bank Indonesia continues to increase cooperation with related institutions in an effort to eradicate counterfeit money, among others with the Coordinating Board for Eradication of Counterfeit Money. Bank Indonesia also issued circulated posters and stickers regarding easy ways to recognize the authenticity of rupiah currency. Bank Indonesia also made preparations for public service advertisements on television in cooperation with the Police.

In addition, Bank Indonesia continuously enhances the security features of each type of bank note and takes socialization activity to assist with the recognition of genuine rupiah currencies by the public. During 2001, 47 dissemination sessions were held, with participation by students, teachers, public figures, cashiers, hotel employees, and police officers. In addition to these preventative efforts, Bank Indonesia also took repressive steps, through coordination and

Table 9.3
Counterfeit Banknotes by Denomination from 1994 to 2001

Period	Denomination					
	Banknotes					
	100,000	50,000	20,000	10,000	5,000	Total
1994	–	14	2,340	1,925	624	4,903
1995	–	74	5,349	7,224	403	13,050
1996	–	128	5,379	9,904	2,537	17,948
1997	–	16,392	139,938	82,274	234	238,838
1998	–	107,520	9,758	59,633	754	177,665
1999	–	89,137	100,536	26,053	224	215,950
2000	–	282,424	24,993	12,836	1,855	322,108
2001	425	65,307	25,305	6,317	288	97,642
Total	**425**	**560,996**	**313,598**	**206,166**	**6,919**	**1,088,104**

Table 9.4
Counterfeit Banknotes by Sources of Report

Period	National Police	Banks
	Share (%)	
1997	92.89	7.11
1998	84.36	15.46
1999	80.39	19.61
2000	83.58	16.42
2001 1)	70.29	29.71

1) Up to November 2001

Table 9.5
Ratio of Counterfeit Banknotes to Currency in Circulation

Period	Denomination				
	Banknotes				
	100,000	50,000	20,000	10,000	5,000
1994	-	0.0000001	0.0000070	0.0000030	0.0000020
1995	-	0.0000010	0.0000140	0.0000090	0.0000010
1996	-	0.0000010	0.0000110	0.0000140	0.0000080
1997	-	0.0000970	0.0002500	0.0000920	0.0000000
1998	-	0.0002840	0.0000140	0.0000620	0.0000010
1999	0.0000000	0.0001240	0.0001230	0.0000350	0.0000004
2000	0.0000000	0.0005150	0.0000360	0.0000210	0.0000030
2001	0.0000011	0.0001619	0.0000466	0.0000105	0.0000005

cooperation with related parties in the arrest of those involved in counterfeiting and in bringing them to court. While the amount of counterfeit money discovered in 2001 was smaller than the year before, the quality of counterfeiting was improved due to technology advancements (for example, computers and scanners).

Viewed in relation to currency in circulation, the ratio of counterfeit currency for year 2001 was an average of 36 counterfeit notes for every 1 million currencies in circulation (0.0036%). Other details of the ratio of counterfeit currency to currencies in circulation are presented in Table 9.5.

Non-Cash Payment Instruments

Development of BI-RTGS Transactions

In 2001, the nominal value of total transactions processed through the BI-RTGS system were relatively stable with an average transaction volume of Rp43.4 trillion per day (Chart 9.3). However, the number of transactions was on the rise, to an average 3,996 (Chart 9.4). This was due to an expansion in the coverage of the BI-RTGS system,

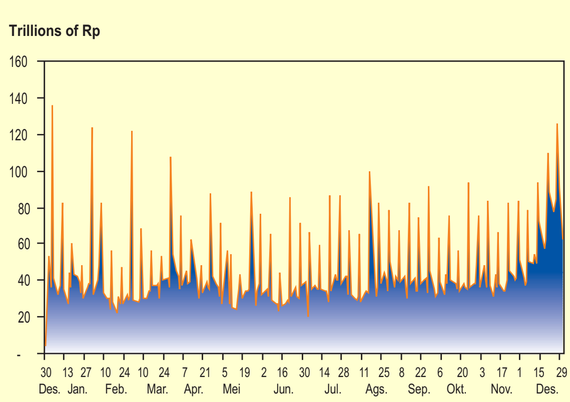

Chart 9.3
Volume of BI-RTGS Transactions

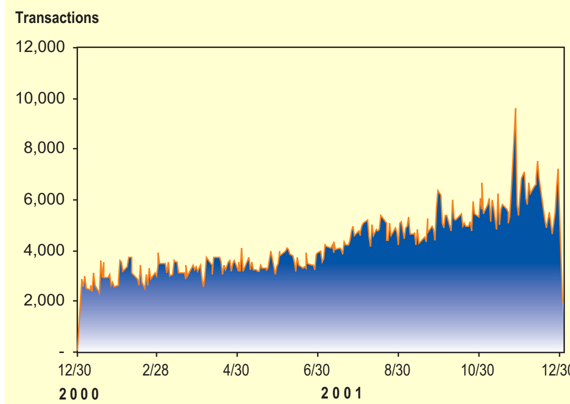

Chart 9.4
BI-RTGS Transactions Activities

which has increased the number of users of the payment system.

Development of Clearing Transactions

As of end-December 2001, the nominal value of clearing activities on a national basis dropped by 72.1% from the previous year, from Rp7,305 trillion to Rp2,035 trillion. This drop followed a decline of 3% in number of clearing item cleared, from 73,704 thousand items in 2000 to 71,616 thousands in 2001. The decline in nominal clearing and in the number of

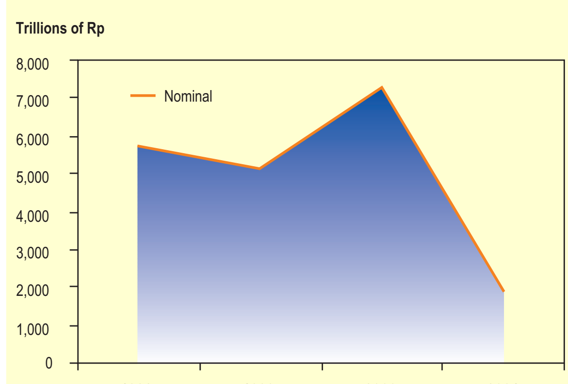

Chart 9.5
National Clearing Turnover (Nominal)

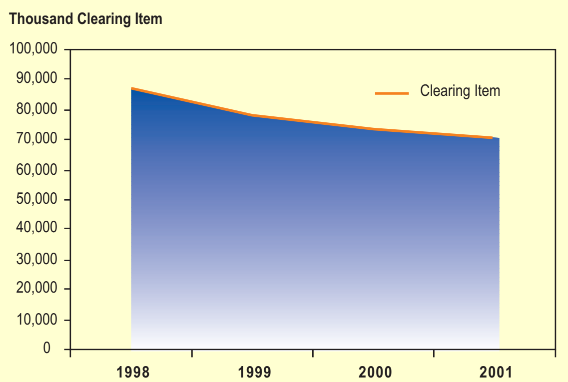

Chart 9.6
National Clearing Activity (Clearing Item)

transactions was due to the shifting of high value settlements, which were previously processed through the clearing system, to the BI-RTGS system.

The Development of Card Payment Instruments

In 2001, there was a rise in activities related to the use of card-based payment instruments, namely credit cards, debit cards, and ATM cards. The rise in the number of transactions using these three types of cards was accompanied by the rise in transaction value. Among the three types of cards, the use of

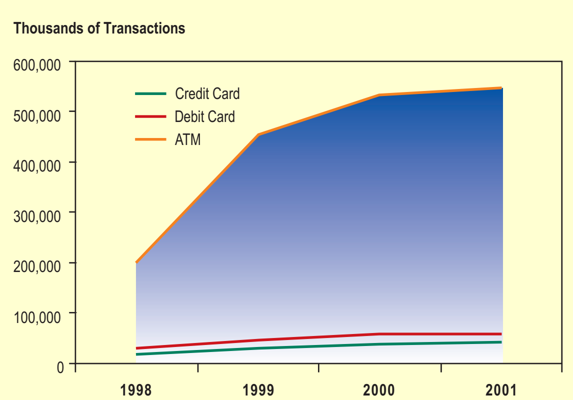

Chart 9.7
Volume of Credit Card/Debit Card/ATM Transactions

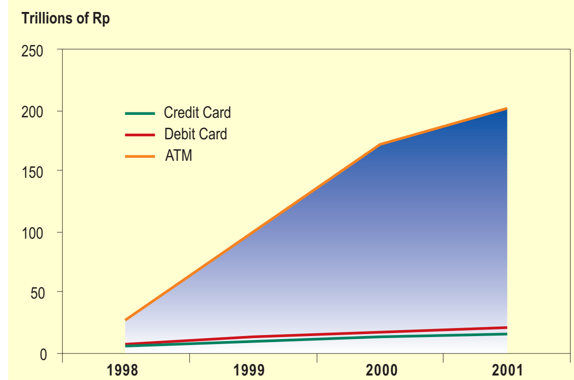

Chart 9.8
Value of Credit Card/Debit Card/ATM Transactions

ATM cards experienced the largest rise in total value of transactions, 17.4% (from Rp153.6 trillion to Rp180.3 trillion). Meanwhile, the total value of transactions with credit cards rose by 13.9% (from Rp13.6 trillion to Rp15.5 trillion); the total value of transactions with debit cards rose by 10.6% (from Rp4.7 trillion to Rp5.2 trillion).

The rise in number of ATM transactions was in part spurred by widening of the ATM network in Indonesia, reflected in greater numbers of ATM machines (up 16.4%, to 7,878 machines in 2001).

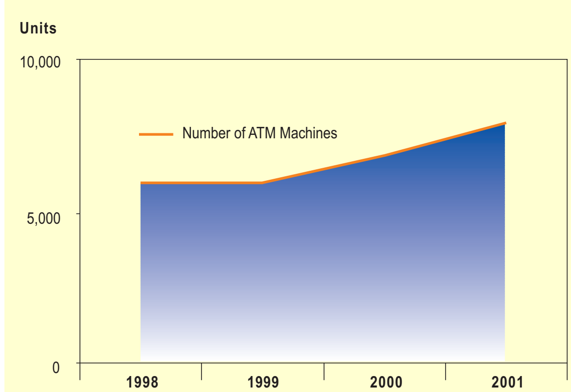

Chart 9.9
Number of ATM Machines

PLAN FOR DEVELOPMENT OF THE NATIONAL PAYMENT SYSTEM

Cash Payment System

Undertake a review concerning exemptions from the obligation to use rupiah currency

As mandated by Act 23 of 1999 concerning Bank Indonesia, the areas and types of transactions that may be exempted from the obligation to use rupiah currency need to be regulated. Consequently, during 2002 Bank Indonesia will undertake a review of transactions that need to be exempted from the obligation to use rupiah currency. This regulation will be important to provide legal assurance for the public.

Rearrange money distribution channels

In order to improve the efficiency and effectiveness of money distribution, and to ensure more appropriate stocks of money in all Bank Indonesia regional offices, Bank Indonesia will rearrange its money distribution channels during 2002. This will include a review of cash depots, transportation facilities, and vault capacity.

Implement the Money Circulation Information System to support money distribution

In order to support money circulation activities (such as development of printing plans, the provision of stocks of money and paper material for money, the distribution system of bank notes/coins, etc.), implementation of the Money Circulation Information System will be continued in Bank Indonesia coordinating offices, to integrate them with head office.

Set up mini laboratory for testing money materials

In order to check the quality of procured money against identified technical specifications, Bank Indonesia will set up a mini laboratory to test money. This laboratory will be furnished with equipment that can test the money received from the public and Perum Peruri, as well as the quality of materials to be used for money.

Review of coin standardization

In 2002, a review will be undertaken to examine alternative metals for coins (the metal must be cheaper than the nominal value of the coins and have a relatively long circulation lifetime). Consideration will be given to standardization of sizes of coins, including the impact on coin-operated public telephones.

Non-Cash Payment System

To support stability of the financial system and effectiveness of monetary policy, payment system policies will be adopted in 2002 as follows :

Development of Delivery Versus Payment

To reduce settlement risk in the capital market, Delivery Versus Payment System will be developed. With this development, an integrated settlement system will be created between the payment side (payment leg) through the BI-RTGS system and the securities delivery side (delivery leg) through the securities delivery system.

Development of a Payment System supervision mechanism

The objective of this development is to ensure a safe and efficient payment system and to protect the stability of the financial system from possible domino effects, when participants in the payment system experience credit or liquidity shortages.

Development of Failure to Settle Scheme

Bank Indonesia is currently studying possibilities whereby the Central Bank does not need to be responsible for shortages of funds when banks settle their clearing activities. A smooth clearing settlement system would still need to be maintained.

Development of a Regulation Concerning the Operation of Payment System Services using Non-cash Payment Instruments and Supporting Services

Currently, there are a number of institutions (including Bank Indonesia) with authority over operation of payment system services. There is a concern that this situation could create duplication in the regulation and supervision of the payment system. In this regard, a draft regulation concerning inter-department coordination is currently being developed.

box

Bank Indonesia - Real Time Gross Settlement (BI-RTGS)

Bank Indonesia's policy towards the non-cash payment system is directed at reducing interbank payment risk. One of the outcomes of this policy is the development of a gross-based settlement system using on-line electronic connections between the banks and Bank Indonesia. The system is known by the name Bank Indonesia-Real Time Gross Settlement (BI-RTGS). The BI-RTGS system is a real time (electronically processed) system that processes final settlement of payment transactions; transactions are processed individually (gross settlement) and the bank accounts of participants can be debited/credited many times during one day in accordance with payment instructions and the resultant payment receipts.

The BI-RTGS system allows banks to improve their liquidity management. Use of the BI-RTGS system reduces certain payment system risks, namely credit risk and liquidity risk. With a settlement system that is based on sufficient balance in each bank's account at Bank Indonesia, the possible risk of failure on the part of one bank in fulfilling its obligations—which can cause other banks to also experience liquidity problems—can be eliminated.

The use of BI-RTGS system will reduce systemic risks in three ways :

a. A significant decline in intraday interbank exposure reduce the likelihood of a bank not covering its liquidity shortage due to another bank not being able to fulfill its obligations.
b. The BI-RTGS system can prevent the occurrence of unwinding payment.
c. The timing of settlements that are done at any time during window time gives banks sufficient time to settle their liquidity problems by borrowing from other banks or by waiting for incoming transfers from other banks.

box

Funds Transfer Through the BI-RTGS System

In general, the mechanism for transfer funds through the BI-RTGS system covers the following steps:

1. A sending bank inputs a credit transfer into its RTGS terminal (which are located in a bank), and notice of the credit will be transmitted to the RTGS Central Computer (RCC) located at Bank Indonesia.
2. The RCC will further process the credit transfer by the following mechanism :
   i. Check balance sufficiency, i.e. whether the balance in the sending bank's current account is bigger or the same as the nominal value of the credit transfer.
   ii. If the balance in the sending bank's current account is sufficient, simultaneously post the transaction to the current accounts of the sending bank and the receiving bank.
   iii. If the balance in the sending bank's current account is not sufficient, the credit transfer will be put into a queue in the RCC while waiting for an incoming transfer that will generate a sufficiently large balance.
3. Information on the settled credit transfer will be transmitted automatically by the RCC to the RTGS terminal of the receiving bank.

Based on the mechanism above when the sending bank's balance is smaller than the nominal value of the transaction and the transaction is put into a queue, this does not mean that the sending bank has experiences a liquidity problem because the bank may soon be expecting incoming transfers from other banks. This situation is referred to as an intraday gap between outgoing and incoming transactions at a certain point in time. To handle the intraday gap, a supporting facility is needed in the form of an Intraday Liquidity Facility, which would be very useful in expediting real time transactions.

chapter 10 THE WORLD ECONOMY AND INTERNATIONAL COOPERATION

chapter 10

THE WORLD ECONOMY AND INTERNATIONAL COOPERATION

During the reporting year, world economic conditions were marked by a slowdown in economic activity in several regions. The slowdown was particularly noticeable in several of the main industrial countries, and it was a major cause of lower world economic growth in 2001 (Table 10.1). Economic activities in industrial countries tended to slow further after the WTC tragedy on 11 September 2001. In line with the slowdown in overall economic activity in various regions, the volume of world trade slumped sharply. This situation led to declines in international prices of various commodities-particularly primary commodities, such as crude oil. As a result of this slump in world trade volume and lower prices of commodities, the external sector of developing countries recorded a significant deterioration. World economic developments in 2001 were also marked by rising global risks, which influenced international capital flows, particularly to emerging market countries. One phenomenon that stood out in movements of funds during the reporting year was "flight to safety". To avoid a deep economic recession, advanced and developing countries adopted expansionary monetary and fiscal policies, which were facilitated by relatively limited inflationary pressures. With the adoption of various economic policies, the world economy is expected to begin recovering in semester II-2002.

Table 10.1
Selected World Economic Indicators

Indicators	1999	2000	2001*
Economic Growth (%)			
World	3.6	4.7	2.4
Industrial countries	3.3	3.9	1.1
Developing countries	3.9	5.8	4.0
C P I (%)			
Industrial countries	1.4	2.3	2.3
Developing countries	6.8	5.9	6.0
World Trade Volume			
(percent change)	5.4	12.4	1.0
Exchange Rate			
USD/JPY	102.51	114.41	131.66
EUR/USD	1.01	0.94	0.89
World Trade Prices			
(percent change)			
Manufactured goods	-1.8	-5.1	-1.7
Crude oil	37.5	56.9	-14.0
Non-oil and gas			
primary commodities	-7.0	1.8	-5.5
LIBOR (%)			
US Dollar	5.5	6.6	3.8
Japanese Yen	0.2	0.3	0.2
Euro	3.0	4.6	4.1

Sources : – IMF, World Economic Outlook, December 2001
– Bloomberg

These various problems coloring the world economy in 2001 received major attention in various forums for international cooperation. In addition to discussing efforts to avoid global economic recession, these forums also discussed efforts to quickly and effectively cope with financial crisis. Further, these discussions focused on efforts to eradicate funding sources for terrorism. For example, in the G-20 and IMF Committee (IMFC) Meetings,[1] agreements were

1 The IMFC meeting was held on 17 November 2001 to replace the IMF Annual Meeting that was cancelled due to the WTC tragedy on 11 September 2001

reached concerning steps by member countries to eradicate funding sources for terrorism. Meanwhile, other international financial forums continued to discuss reform of the international financial system; ways to prevent the reoccurrence of financial crisis; and ways to provide assistance for tackling on-going economic crises in several developing countries. In the regional Asian forum, cooperation to prevent the crisis is provided through the Asian Surveillance and Bilateral Swap Arrangement.

WORLD ECONOMY

In 2001, world economic growth reached only 2.4%, down sharply from 4.7% in 2000. This drop was particularly due to slower growth in the industrial countries, which began at the end of 2000. Prospects for a recovery in industrial countries at the end of 2001 were undermined by the WTC tragedy on 11 September 2001. This tragedy further weakened the US economy. Being heavily dependent on the US economy, gobal demand also slumped. The WTC tragedy has also increased global security risks, which hampered investment. In the light of these developments, overall economic growth of the industrial countries is estimated to reach only 1.1% in the reporting year (Chart 10.1).

In line with economic slowdown in advanced countries, world trade volumes slowed significantly from 12.4% in 2000 to only 1.0% in the reporting year. This prompted price drops in various commodities, particularly crude oil, which slid 14% in the reporting year. The price of crude oil averaged only $24.0 per barrel in 2001, and it fell as low as $18.0 per barrel at the end of November 2001. Meanwhile, prices of non-oil/gas primary commodities and manufacturing goods dropped by 5.5% and 1.7%, respectively. Among non-oil/gas primary commodities, the price drops were especially sharp for coffee, cotton, copper, aluminum, tin, and nickel. Manufacturing products also experienced price drop, with price of semiconductor being the most eroded in which sales in 2001 reaching only 20% of their value in 2000. By contrast, the price of gold actually rose, attributable to a rise in higher world demand in the midst of great uncertainty after the WTC tragedy.

Weaker world trade put considerable pressure on the advanced and newly industrialized countries, particularly those that are highly dependent upon exports. Overall, the economic growth of developing countries slipped to 4.0% in the reporting year, down from 5.8% in 2000, caused mainly by lower exports. Several newly industrialized economies even recorded a contraction. For example, the economies of Singapore and Hong Kong shrank by 2.9% and 0.3%, respectively, attributable to export declines of 19.6% and 10.4% in 2001. Economic growth of developing countries was supported by continuing high (although

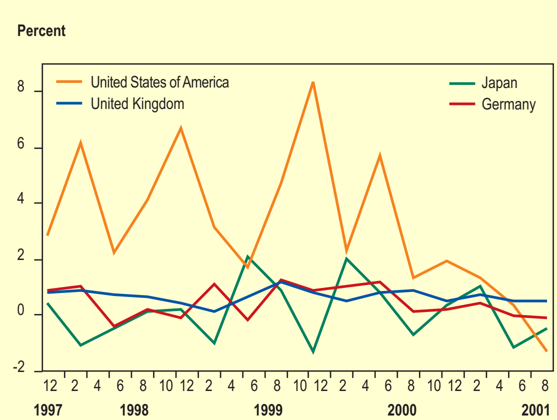

Chart 10.1
Major Industrial Countries Economic Growth

with slight decrease) growth of the People's Republic of China.

Slower world economic and trade growth kept global inflation in check. During the reporting year, inflation in advanced industrial countries was little changed, at 2.3% (Chart 10.2). Meanwhile, the inflation rate in developing countries stood at 6.0%, just a bit above 5.9% of the year before. Relatively stable inflation has provided room for a number of advanced and developing countries to adopt expansionary monetary and fiscal policies to avoid deep economic recession.

Expansionary monetary policies adopted by the central banks of advanced countries were expected to stimulate economic activity. In the US, the reduction of interest rates was directed at stimulating consumption and investment, particularly after the WTC tragedy. In Japan, interest rate policy, which was directed towards rates of zero percent, was intended to promote recovery from a decade-long recession. Meanwhile, in the Euro area, declines in interest rates have been less aggressive

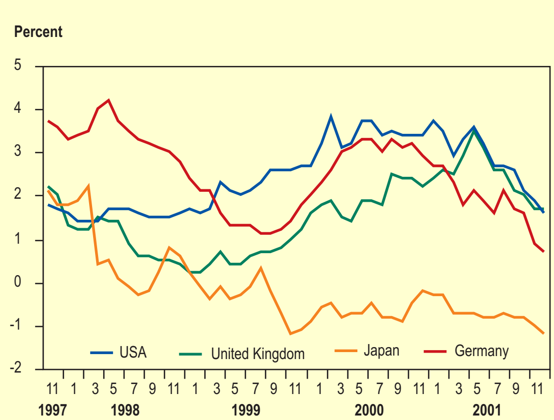

Chart 10.2
Inflation in Major Industrial Countries

because inflation in this region was generally still above the target of the European Central Bank (ECB).

Monetary policies in developing countries varied according to local conditions of inflation and other domestic problems. The complexity of problems faced by developing countries often created a dilemma in the implementation of monetary and fiscal policies. Government financial problems have prompted some countries to adopt economic policies that prioritize domestic interests. This is the case of Argentina, which sank into an economic and social crisis towards the end of 2001, particularly spurred by the government's failure to control its budget deficit and to make scheduled payments on foreign debts because of a decline in the country's tax revenue and exports.

Expansionary economic policies have implications for the development of the international financial markets. The combination of expansive monetary and fiscal policies in several countries increased optimism as regards economic recovery, which prevented those economies from sinking deeper into prolonged crisis. Waves of reductions of benchmark interest rates by various monetary authorities have prompted interest rate declines in international financial markets, which then is expected to stimulate economic activity. However, these policy measures have not revived the world capital markets, as reflected in the index of world stock prices, which tended to decline during the reporting period. Activities in world bourses were also much influenced by sluggish world economic conditions and by rising uncertainty especially as concerns the prospects for global recovery.

The United States

After a strong economic expansion in the last 10 years, the US economy began to show indications of a slowdown in early 2000. The slowdown became more apparent during the reporting year and the economy is estimated to grow by only 1.0%, far lower than the previous year's 4.1%. In line with the weakening economic activity, inflation declined from 3.4% in 2000 to 2.9% in 2001. The slowdown in overall economic activity in 2001 was particularly reflected in consumption (which only grew by 3.03%) and private investment (which dropped by 7.99%). These two components of aggregate demand had been the largest contributors to high growth of the US economy over a long period. The slowdown in the US economic expansion was reflected in several important real economic indicators, such as a significant slowdown in retail sales and housing and a rise in the unemployment rate during the reporting year. Weaker consumption and private investment stemmed from declining consumer and business confidence, which caused delays and reductions in consumption spending and investment.

Declining consumer and business confidence was related to the deteriorating performance of capital markets in the US, particularly the stock markets, which had been an important foundation of growth in previous year. During the reporting period, the US stock markets fell sharply, eroding a good part of the US public's wealth and discouraging consumption and business investment. Stock prices fell particularly spurred by overvaluations of shares of Internet (dot-com) companies and although magnified by the WTC tragedy, there was some recovery towards year-end. During 2001, the Dow Jones Stock Index (DJIA) fell by 7.10%, while the NASDAQ and S&P 500 fell by 21.05% and 13.04%, respectively.

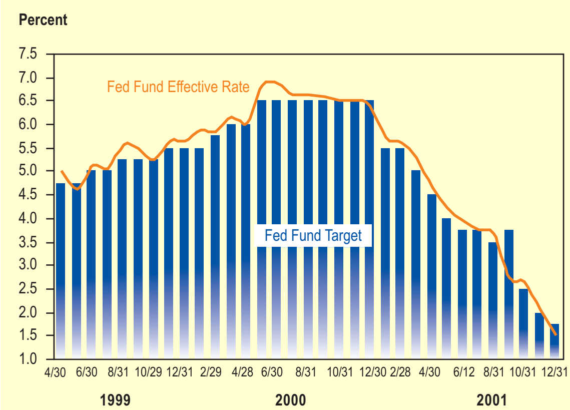

Chart 10.3
Fed Fund Rate

To prevent deep economic contraction, the Federal Reserve adopted an aggressively expansionary monetary policy by reducing the federal funds interest rate 11 times during 2001 to 1.75% (Chart 10.3). In addition, the US government adopted an expansionary fiscal policy through tax cuts and infrastructure development in order to stimulate domestic demand.

Western Europe

The slowdown in the US economy had a large impact on countries within the Euro area, which are important US trade partners. In 2001, economies within the Euro area expanded by only 1.5%, lower that the previous year's 3.4%. The slowdown occurred in the three largest economies, namely Germany, France, and Italy. In 2001, German's economy is estimated to grow only by 0.5%, down sharply from 3.0% in 2000. Meanwhile, growth in France and Italy are estimated to slow to only 2.1% and 1.8% compared with 3.5% and 2.9%, respectively, in 2000. Weakening economic activity in the Euro area was mainly attributable to worsening performance of the external sector and the weakening in consumption and private domestic investment. As the result of weak private investment, layoffs by the business sector tended to rise, resulting in rising unemployment.

Despite this economic slowdown, inflation in the Euro area was still on an upward trend. In the reporting year, inflation reached 2.7%, compared with 2.4% in the previous year. Higher inflation was mainly contributed by increases in the prices of food and fuel, as well as lag effects from the weakening of the Euro currency during 2000. However, towards the end of the year, inflation declined slightly from 2.1% in November to 2.0% in December, for the first time matching the 2% ceiling for overall inflation set by the European Central Bank (ECB). This December inflation rate was the lowest in the last 19 months, mainly driven down by the plunge in oil prices toward the end of 2001. From September through November 2001, Brent crude (which is the benchmark price from 2/3rds of world's oil supply) plunged by 35%.

These developments provided maneuvering room for the ECB to cut interest rates. During the review period, the ECB cut interest rates 4 times (cumulatively by 1 1/2 percentage points) to 3.5% by the end of 2001. Compared with the policies of the Federal Reserve (which cut interest rates 11 times), the interest rate cuts by the ECB were conservative, mainly because inflation generally exceed the ECB's ceiling of 2.0%. Inflation peaked at 3.4% in May 2001.

Outside the Euro area, economic activity also slowed in the United Kingdom. In 2001, the UK economy grew by 2.3%, down from 2.9% in 2000. Meanwhile, inflation rose slightly, from 2.1% in 2000 to 2.3% in 2001, which is still below the target of 2.5% set by the Bank of England (BoE). To stimulate the economy, the BoE cut interest rates 7 times during the reporting year, causing its benchmark interest rate (base rate) to fall to 4%, compared with 6% in 2000.

Japan

The impact of the US economic slump also hit Japan as one of the main US trading partners. In 2001, the Japanese economy contracted by 0.4%, having expanded by 2.2% in 2000. This deterioration mainly stemmed from a downshift in export performance in line with the slump in import demand from the US (which accounts for roughly 1/3rd of Japan's export revenues). Japan's exports are estimated to have contracted by 6.6% in 2001.

To cope with prolonged crisis, the Japanese government continued its intensive expansionary fiscal and monetary policies. In the monetary area, the Bank of Japan maintained the overnight call rate at 0.1%. In the banking area, which experienced severe problems of delinquent credits and falling asset values due to plunges in stock and property prices, the Japanese government has given assistance of 26 trillion yen for bank recapitalization, payment of customer funds, and loan extensions. Meanwhile, to maintain export competitiveness, the Japanese government let the yen depreciate quite sharply. During the reporting year, the yen weakened sharply against the US dollar, particularly caused by rising portfolio outflows spurred by gloomy economic prospects and slow progress in resolution of structural problems in the banking sector.

Non-Japan Asia

The newly industrialized countries of Asia (such as South Korea, Hong Kong, Taiwan, and Singapore) were hard hit by the economic slowdown in the advanced industrial countries, particularly the US. The large contribution of their export sector to the economy made these countries extremely susceptible to fluctuations in global trade and international commodity prices. In addition, the export structure of those countries is dominated by manufactured products, particularly electronic components, which are generally very elastic with respect to GDP in destination countries such as the US. In 2001, South Korea's economic growth is estimated to reach to only 2.6% after recording quite high growth in 2000 of 8.8%. Meanwhile, the economies of Hong Kong, Taiwan, and Singapore in 2001 are estimated to contract by 0.3%, 2.2%, and 2.9%, after experiencing expansions of 10.5%, 6.0%, and 9.9%, respectively, in 2000. Malaysia and Thailand, which have the potential to become newly industrialized countries in Asia, grew by only 0.3% and 1.5% in 2001, down from 8.3% and 4.4% in the year before. The economic slump in those countries enabled the inflationary pressures to be controlled at quite low levels.

Facing the threat of global economic recession, a number of newly industrialized countries in Asia adopted expansionary monetary and fiscal policies. Expansionary policies were intended to raise domestic consumption and prevent a rise in unemployment rate due to weak exports. Slump in import demand from advanced industrial countries rose competition among Asian countries and led these countries to adopt various measures to increase their production efficiency and competitiveness. In order to increase competitiveness of their exports, several industrial countries in Asia let their exchange rates depreciate.

Some Asian economies continued to perform well. In 2001, the economy of the People's Republic of China (PRC) continued its impressive performance with a growth rate of 7.3%. Its inflation rate was still controlled at 1.0%, compared with 0.4% in 2000. This excellent economic performance was particularly due to expansionary fiscal policy and rising foreign direct investment. The main motivation for the rise in direct foreign investment was to establish a local operating base to capture local market in anticipation of PRC's entry into the World Trade Organization in the reporting year.

Latin America

In line with the US slowdown, the economies of Latin America also tended to slow in 2001. In the reporting year, the growth rate of the Latin American countries reached only 1.0%, down from 4.1% in the previous year.

The economic performance of the four largest economies in Latin America, namely Mexico, Brazil, Chile, and Argentina, deteriorated significantly, with the Argentina's economy expected to remain in crisis. Mexico, which is one of the US's main trading partners on the American continent, would record a slower growth from year 2000 of 6.9%. Meanwhile, economic growth in Brazil and Chile reached only 1.8% and 3.3%, compared with 4.4% and 5.4% in the previous year. Argentina's economy is estimated to shrink by 2.7%, continuing the contractions of 3.4% and 0.5% that occurred in 1999 and 2000, respectively. Argentina's escalating economic crisis peaked towards the end of 2001, mainly spurred by the government's failure to control its deficit and default on its foreign debts. The result was political crisis and social unrest. Argentina's financial crisis was mainly caused by its inability to accumulate enough domestic funds to pay major amounts of government short-term liabilities that came due. The decline in domestic revenue stemmed from lower tax and export revenues due to weakening world demand and decline in Argentina's exports competitiveness. Argentina's products became uncompetitive due to its exchange rate policy of a one-for-one peg of the peso to the US dollar, which resulted in the overvalued peso.

International Financial Markets

Development in international financial markets during the reporting year, were marked by appreciation of the US dollar, drop in money market interest rates, and globally weaker stock prices. Despite the weak US economic performance and the declining interest rates, the US dollar strengthened against almost all world currencies. This demonstrated that the US dollar was still considered to be the safest currency in the world, which is particularly important when global risks are rising. These global risks rose further after the WTC tragedy, which prompted international investors to take a more cautious attitude, including as regards undertaking investments in developing countries. As a result, international capital flows were characterized by flight-to-safety considerations, which caused reflows into the financial markets of the advanced countries, particularly the US.

As various countries follow loose monetary policies to avoid recession, interest rates in money markets trended downwards. The average 6-month LIBOR rate for the US dollar, which is a benchmark for several major financial markets, experienced a substantial drop from 6.6% at the end 2000 to 3.8% at the end of the reporting year (Chart 10.4). However, the declines in interest rates in individual countries varied considerably, depending upon local inflation rates.

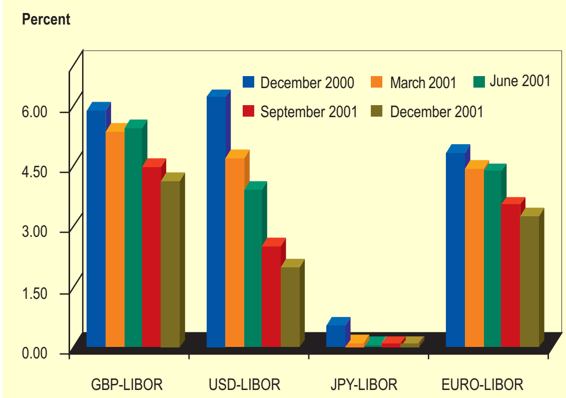

Chart 10.4
LIBOR

In line with slower economic activity in almost all regions, stock prices in various world bourses experienced large declines. Drops in stock prices mainly occurred in the US market, which then spread globally, including to those Asian countries with high dependency on US economic performance. These declines were particularly pronounced in the information technology sector and several related industries, such as computer components and electronics, these sectors dominate exports for a number of newly industrialized countries in Asia.

INTERNATIONAL COOPERATION

Discussions in various international and regional cooperation forums during the reporting year emphasized efforts to cope with the economic slowdown through appropriate monetary and fiscal policies, strengthening of financial systems, and undertaking regional surveillance to bolster crisis prevention. Various forums also discussed efforts to prevent financing of international terrorism in response to the WTC tragedy. An important development in world trade was accession by the People's Republic of China and by Taiwan to the World Trade Organization (WTO).

Cooperation in Monetary, Financial, and Banking Areas

International Monetary Fund (IMF)

During the reporting year, issues discussed in the IMF covered: (i) efforts to strengthen the international financial system, including the IMF's role; (ii) streamlining conditionality and strengthening the sense of ownership by member countries with IMF programs; (iii) eradicating money laundering and terrorism financing, and (iv) good governance. To strengthen the financial systems of member countries, the IMF played a role in promoting macroeconomic and financial stability as a prerequisite for sustainable economic growth; promoting the stability and integrity of the international monetary and financial systems as public goods; and assisting member countries in developing sound financial sectors.

The IMF has taken measures to streamline the conditionality of policy programs of member countries, to be more efficient and effective. The implementation of conditionality for structural reform can be conducted on a case-by-case basis, by emphasizing areas that largely influenced macroeconomic stability and sustainable growth. To enhance a sense of ownership of economic reform programs within the borrowing member countries, the IMF is studying the possibility of using results-based conditionality. It was proposed that terms and conditions for drawing on IMF facilities be based on results achieved in order to give greater flexibility and accountability to those countries in determining performance targets. The greater flexibility and accountability will drive countries to have stronger sense of ownership of programs agreed with the IMF.

After the WTC attack, issues concerning combating the money laundering and financing of terrorism became the main focus of IMF meetings. The International Monetary Financial Committee (IMFC) gave serious attention to the use of the international financial system for financing terrorist actions and money laundering for illegal activities. Therefore, the IMF has asked its members to ratify and implement United Nation resolutions, specifically number 1373, as well as to welcome and support the Special Recommendations from Financial Action Task Force (FATF) concerning eradication of funding for terrorism. In relation to the issue of good corporate governance, the IMFC meetings agreed that the IMF needs to handle this problem through special measures to cope with poor governance and corruption.

G-20

In the reporting year, international cooperation within the G-20 framework stressed efforts to prevent the use of the financial sector for terrorism activities, and discussions of policies to cope with current world economic conditions and waves of globalization. Steps to be taken are formulated into an Action Plan on Terrorist Financing, which in principal covers :

(a) Freezing of assets belonging to terrorists. Each member country will implement relevant resolutions of the UN Security Council, particularly resolution number 1373, in order to stop financing for terrorism.

(b) Implementation of international standards. Each member country will ratify and implement the UN Convention for the Suppression of the Financing of Terrorism as soon as possible and ratify the UN Convention against Transactional Organized Crime.

(c) International cooperation through exchanges of information and inter-G20 member access. Further, each member will establish a Financial Intelligence Unit and take steps for exchanges of information.

(d) Technical assistance. Member countries, whenever possible, will provide technical assistance in preventing terrorism financing and in eradicating money laundering for other countries that need technical assistance. In addition, the G-20 will appeal to international and regional institutions to give technical assistance.

(e) Compliance and reporting. Member countries will take steps to ensure that financial institutions and all its citizens comply with regulations concerning the eradication of terrorism financing and other criminal actions.

Manila Framework Group (MFG)

During the reporting year, the Manila Framework Group (MFG) emphasized the following problems: (i) financial and corporate restructuring; (ii) reform of the international financial system; and (iii) the MFG Financing Arrangement. In addition to discussing these issues, the MFG also discussed the issue of regional surveillance, and strengthening IMF surveillance by involving the private sector in crisis resolution.

Central Bank Cooperation

In the review period, cooperation between central banks continued through various forums, among others the Executive Meeting of East Asian and Pacific Central Banks (EMEAP) and South-East Asian Central Banks (SEACEN).

EMEAP Forum

In discussing economic and financial issues, the EMEAP forum stressed the influence of the US and global economic slowdowns on the economies of the EMEAP region as well as susceptibility of the region to crisis. In facing this development, members of EMEAP consider that there is a need for implementing appropriate policies in order to promote domestic demand. In relation to efforts in promote financial stability, several EMEAP member countries have focused on the “one-size-fits-all” approach in relation to the implementation of international standards amid differences in characteristics and abilities of members to implement the said standard. In relation to the IMF’s policy response to the Asian crisis, EMEAP considers that the IMF policies in handling the crisis have created deeper economic difficulties. In this regard, the IMF needs to consider the peculiar economic fundamentals in different countries; to simplify conditionality; and to enhance the sense of ownership of members that are assisted through IMF programs.

SEACEN

During the reporting period, various topics have been discussed in the SEACEN forum, including: (i) the SEACEN Trust Fund (STF), (ii) the SEACEN Experts Group (SEG) on Capital Flows, (iii) the establishment of an Electronic Data Exchange in the SEACEN Center, and (iv) financial aid from Japan.

In the framework of the SEACEN Trust Fund (STF), SEACEN recorded special progress during the reporting year, namely the formal acceptance of the Bank of Mongolia into the membership of STF. Efforts to improve management included among others: the granting flexibility to the Director of Investment and Financial Market Operations of Bank Negara Malaysia as an additional signatory; and the changing of the application procedures for scholarship assistance back to the previous system, which was considered more effective.

Meanwhile, SEACEN, functioning as a research and training institute for central banks in South-East Asia, has made an effort to control potential risks arising from the volatility of capital flows through the meeting of SEACEN Experts Group (SEG) on Capital Flows. Within this framework, SEACEN strengthened surveillance over capital flows of its member countries through exchanges of data and information among the SEACEN member countries and by creating SEG Database.

During the reporting period, the Bank of Japan (BOJ) offered financial assistance in the amount of JPY10 million each year to finance certain SEACEN training activities identified by BOJ without any conditions. The vast development of the SEACEN Center activities have attracted two other monetary authorities, namely the Monetary Authority of Brunei and the Reserve Bank of Fiji, to take up membership in the SEACEN Center.

Cooperation in Development Areas

The World Bank

During the reporting year, the World Bank continued to focus on issues on poverty alleviation and growth promotion, particularly for the poorest countries. Discussions were related to four main topics, namely: (i) follow up on the Highly Indebted Poor Countries (HIPC) Initiative and Debt Sustainability; (ii) enhancement of process for the Poverty Reduction Growth Facility (PRGF) and Poverty Reduction Strategy Paper (PRSP); (iii) improved market access for developing countries' exports; and (iv) assistance for countries that have recently experienced conflicts.

Steps taken by the World Bank concerned several matters. First, the World Bank would make a recommendation on the strategy for sustainable development, and it would promote equality for poor countries through funding assistance and opening of market access by donor countries. Second, the World Bank would streamline, refocus, and prioritize its conditionality based on strategies that would be developed by member countries themselves (within the PRGF and PRSP) for growth promotion and poverty alleviation. Third, the World Bank, together with the IMF, would give technical assistance and capacity building assistance to accelerate recovery in those countries.

The Asian Development Bank (ADB)

The ADB continued to participate in programs concerning poverty alleviation, community empowerment, good governance, and private sector development. In addition, the ADB took part in efforts to prevent crisis by giving assistance in surveillance activities through cooperation with the ASEAN Secretariat. It is expected that future initiatives undertaken by the ADB will move toward statistical standardization and methodology for early warning systems.

Regional Cooperation

Asia Pacific Economic Cooperation (APEC)

In the framework of promoting sustainable economic growth, the Asian Pacific Economic Cooperation (APEC) forum has made efforts to adopt financial policies and to promote policy dialogue concerning macroeconomic issues, including strengthening the international financial system to create strong economic foundations for long-term growth. APEC has also committed to further liberalize trade and investment, and to promote the new round of WTO negotiations. APEC stressed the need for the agenda of the new WTO round to include agriculture, industrial products and services; strengthening WTO rules; implementation; issues and any other issues which are in the interest of all members, particularly developing countries, in facing the challenges of the 21st century. In addition, APEC members also acknowledged the need to strengthen banking regulations and supervision, good governance and financial disclosure; to fortify domestic financial systems in order to ensure consistency with macroeconomic policies; to improve global financial sector surveillance; and to continue efforts to enhance the effectiveness of international financial institutions.

Association of South East Asian Nations (ASEAN)

During the reporting year, various meetings have been held within the framework of ASEAN, such as the ASEAN Central Bank Forum, ASEAN Finance Ministers and Central Bank Deputies, as well as ASEAN Finance Ministers. One particularly important development was the agreement on the Bilateral Swap Arrangement (BSA). The arrangement is intended to provide short-term financial assistance in the form of swaps arrangement to countries participating in the Chiang Mai Initiative. During the reporting year, ASEAN+3 (that is, ASEAN and its three partner countries, namely Japan, the People's Republic of China, and South Korea) have signed several BSAs. These BSAs were made between Japan and South Korea (amounting to $2 billion), Japan and Thailand ($3 billion), Japan and Malaysia ($1 billion), as well as Japan and the Philippines ($3 billion). Indonesia has not finalized its BSA because of several un-solved problems between Indonesia and the ASEAN partner countries. Those problems included lack of clarity as regard the maximum government guarantee of the BSA facility.

As a follow up on the establishment of the Task Force on ASEAN Currency and Exchange Rate Regime, ASEAN countries have agreed to implement a feasibility study on the possibility of implementing an ASEAN Currency and Exchange Rate Mechanism. The objective of the feasibilty study are as follow : (i) to enhance financial stability, particularly at regional level, (ii) to avoid the possibility of financial crises in the future, and (iii) to boost trade and investment through reductions in transaction costs.

chapter 11

ECONOMIC PROSPECTS AND POLICY DIRECTIONS IN 2002

chapter 11

ECONOMIC PROSPECTS AND POLICY DIRECTIONS IN 2002

Indonesia's economic growth is expected to encounter large ongoing challenges in 2002. The threats of global economic recession and various domestic structural problems have reduced potential sources of economic growth. On the assumptions of progressing socio-political conditions, declining pressures on the exchange rate, and accelerating economic restructuring, economic growth in 2002 is projected to reach 3.5%–4.0%.

On the demand side, economic growth would depend more on domestic demand, particularly private consumption; while export and investment would remain unfavorable. This projection is based on a world economy that would continue weak in the short-term. Consequently, the climate would not be conducive for exports nor for foreign capital inflows that would boost private investment. On the fiscal side, government spending is projected to decelerate and, as such, would not provide any meaningful stimulus to the economy. Because domestic demand is expected to be the engine for economic growth, more serious efforts to overcome various basic problems and domestic risks, will be very important for sustaining the momentum of Indonesia's economic recovery.

On the supply side, almost all economic sectors are expected to contribute to growth in 2002. In line with the role of consumption as the dominant engine of growth, the largest contribution would originate in the manufacturing and trade sectors, especially retail trade. The agriculture sector would remain weak, owing to a possible return of El Niño and by problems in fertilizer production and distribution. Export-oriented plantations would remain under quite heavy pressure in line with continuing weak world demand. The mining sector would expand, but at a relatively slow pace, mainly owing to on-going security disturbances affecting this sector and weak foreign demand for several minerals. Construction sector is projected to rebound in line with the realization of several large projects, such as the Jakarta Outer Ring Road and housing, which has picked up vigorously in line with expanding housing credits.

The rupiah exchange rate is predicted to strengthen despite some potential for depreciation. Aside from structural economic factors, exchange rate developments will be influenced by market sentiment vis-a-vis several economic-political problems, such as fiscal sustainability and events surrounding the forthcoming annual National Assembly Meeting (MPR). For 2002 as a whole, the rupiah is expected to average Rp9,500 –Rp10,500 per dollar. A significant strengthening would occur in middle of the year in line with continuously lower risks in the socio-political, financial, and economic fields. This view is further supported by the possibility of stronger balance of payments underwritten by an improved capital account. This projection would be more optimistic conditional there were progressing implementation of government economic programs, such as sales of

IBRA assets and privatization of SOEs to improve market perceptions.

Inflationary pressures are projected to remain strong in 2002, originating in high inflationary expectations, strong demand for foreign exchange which is not adequately offset by an increase in the supply of foreign exchange, and the impact of government prices and incomes policies. Inflation could intensify further if El Niño disrupts food production and distribution in any significant way. Against this background, the CPI inflation target for year 2002 is set in the range of **9.0%–10.0%.**

To reach this reasonably realistic inflation target, monetary policies will be conducted in a cautious and measured way in order to maintain price stability and to support the ongoing economic recovery, so that in the long term sustainable economic growth can be achieved. Operationally, Bank Indonesia will optimize its available monetary instruments, mainly through the Open Market Operation and foreign exchange sterilization in order to reduce pressures on inflation and the exchange rate. In addition, efforts to restore bank intermediation will be continued so that credits can be channeled to well-prepared economic sectors with low risk.

Furthermore, since consumption will remain the main engine of economic growth, various policies will be needed to ease certain supply-side constraints on financing and distribution, so that the increase in consumption would not create excessive price rises. In addition, with the existence of many non-monetary factors influencing inflation, coordination among various parties, particularly the government, is vital in minimizing the impact of inflationary pressures stemming from government policies, declining supply, and disturbances in the distribution of goods and services.

The basic assumptions underlying the above projections will face several challenges and uncertainties. Although these matter had been identified in the previous year, efforts to overcome them have not shown meaningful progress yet, which could lead to public doubts about the economic recovery. Consequently, resolution of these problems must be undertaken immediately to restore public confidence.

FUTURE CHALLENGES

Settlement of various fundamental problems and risks in 2001 was not as rapid as expected, which will heighten the challenges of monetary control in 2002. Overcoming such risks and uncertainties will be the key to better economic prospects in the coming years. These risks and uncertainties include:

- **First**, the slow progress in corporate debt restructuring. This has hindered the pace of economic recovery and the extension of bank credits, because the corporation undergoing the restructuring program constitute the major segment in the economy.
- **Second,** bank intermediation has not fully restored. On one hand, this has limited financing for production and investment while on the other hand there is excess liquidity in the banking sector which has the potential to exert pressure on the exchange rate and inflation, and reduce the effectiveness of monetary policy.
- **Third,** the heavy burden of the state budget, mainly due to a large subsidies and huge government debts. Asset recovery by the IBRA and State Owned Enterprises (SOEs) are

estimated to be inadequate to cover the burden of government debts. In such condition, there is little room of fiscal stimulus to accelerate the economic recovery.

- **Forth,** legal uncertainty persists and problems remain in implementing economic policies in various other areas. These conditions hamper economic restructuring and delay improvements in Indonesia's country risks and impede economic recovery.
- **Fifth,** the emergence of various problems associated with the implementation of regional autonomy which are not conducive to investment in the region. In addition, inefficient utilization of General Allocation Funds (Dana Alokasi Umum) could further limit fiscal stimulus.
- **Sixth,** on the external front, the world economy is still in recession as 2002 begins and an improvement is anticipated only in the second semester. This will reduce external demand for Indonesian products. In addition, the implementation of AFTA (starting early 2002) will provide new export opportunities but the opening of domestic market to foreign competitors could also threaten domestic producers.

GLOBAL ECONOMIC PROSPECTS

Economic Growth and World Trade

The slowdown in the global economy that occurred in 2001 is projected to continue in 2002. This slowdown is inseparable from the tight monetary policies adopted by the majority of advanced countries in the last two years in order to dampen domestic demand pressures that were considered excessive. However, these policies turned out to be more contractionary than initially estimated. As a further complication, the WTC tragedy has raised concerns of an even-larger contraction. These events have spurred the majority of advanced countries to expand monetary and fiscal policy more aggressively in order to boost demand. On that basis, the IMF estimates world economic growth of 2.4% in 2002[1] with a significant recovery expected in semester II of 2002. In line with this, the growth of world trade volume is estimated to rise slightly, from 1.0% in 2001 to 2.5% in 2002.

In general, economic growth in advanced countries is projected to decline. The US economy, which is the locomotive of the global economy, would expand by only 0.7% in 2002. The European Union economy would grow by only 1.3% in 2002, which is particularly due to weak domestic demand in Germany. Meanwhile, Japan's economy, which has been in economic recession for more than a decade, is projected to get worse, contracted by –1.0% in 2002. The newly industrialized economies of Asia, namely, South Korea, Singapore, Hong Kong, and Taiwan, are projected to grow by 3.2%, 1.2%, 1.0% and 0.7%, respectively.

Although global economic conditions are still shrouded in uncertainty and risk, opportunities for faster economic recovery are still available. In addition to support from looser monetary and fiscal policies, faster-than-expected improvements in consumer confidence could strengthen the recovery of the world economy. Furthermore, continuing low oil prices and improvements in information technology (IT) would boost productivity, thereby accelerating gains in production capacity.

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1 IMF, World Economic Outlook, December 2001

Table 11.1
Economic Growth in Several Regions of the World

Item	2000*	2001**	2002[2]
World Economic Growth	**4.7**	**2.4**	**2.4**
Industrial Countries	**3.9**	**1.1**	**0.8**
United States of America	4.1	1.0	0.7
Japan	2.2	–0.4	–1.0
European Union	3.4	1.7	1.3
Asian Newly Industrialized countries	8.2	0.4	2.0
Developing Countries	**5.8**	**4.0**	**4.4**
Africa	2.8	3.5	3.5
Asia	6.8	5.6	5.6
People's Republic of China	8.0	7.3	6.8
ASEAN - 4[1]	5.0	2.3	2.9
Latin America	4.1	1.0	1.7
Countries in transition	6.3	4.9	3.6

1) Consist of Indonesia, Malaysia, Philippines and Thailand
2) Projection
Source : IMF, World Economic Outlook, December 2001

In developing countries, and with only a few exceptions (most notably, China and India) economic prospects are less encouraging. Economic growth in Latin America is expected to deteriorate, mainly due to the financial crisis and uncertain political conditions in Argentina and the energy crisis in Brazil.

Inflation and International Interest Rates

With weakening world demand and a declining trend in international oil prices, world inflation is projected to decline further in 2002. This declining trend of inflation would be experienced by the majority of advanced countries. Meanwhile, inflation in developing countries would be determined in substantial part by developments in their respective external sectors. In this regard, inflation in advanced countries would decline to 1.3%, while inflation in developing countries would be 5.3%.

To prevent a continuing decline of aggregate demand, monetary policies in advanced countries are projected to remain relatively loose and short-term market interest rates would continue low. Meanwhile, long-term interest rates will be relatively high in line with expectations of improving world economic conditions.

Table 11.2.
Development of Inflation and International Interest Rates

Item	2000	2001	2002
	Percent		
Inflation			
Industrial Countries	2.3	2.3	1.3
Developing Countries	5.9	6.0	5.3
Transitional Countries	20.1	16.0	11.0
Short Term Interest Rate			
United States of America	6.6	3.8	2.8
Japan	0.3	0.2	0.1
European Union	4.6	4.1	2.9

Source : IMF, World Economic Outlook, December 2001

Prospects for International Market Commodity Prices

In general, international commodity prices in 2002 will tend to remain low. In addition to weak demand, low commodity prices stem from high production in 2001, which caused a large buildup of inventories. In relation to this, prices for several of Indonesia's export commodities (such as mining and agricultural products) are projected to continue under heavy pressure. In addition, weak demand conditions might spur intense price competition which would work against exporters. To reduce such price pressures, market expansion and diversification must be undertaken, although technical dependence on traditional markets (such as the US and Japan) will be relatively difficult to overcome in the short term.

Relatively weak economic growth in the advanced countries will also prompt declines in oil prices, towards the bottom of the range agreed by

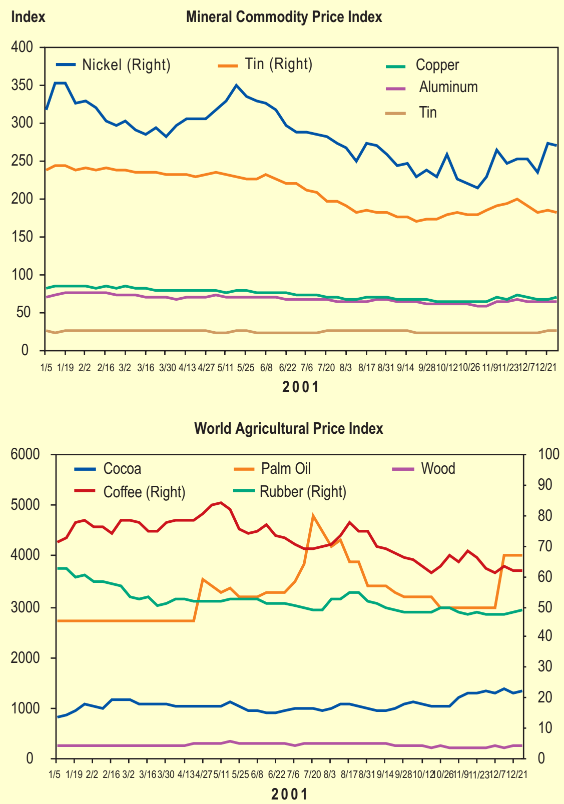


Chart 11.1.
Development of Export Commodity Prices

OPEC members, namely $22/barrel. This will be due to winter needs, which have been relatively normal, and high US oil stocks, which stemmed from excess supply in the international oil market in 2001.

In order to push oil prices back into the range of $22–$28 per barrel, OPEC countries have agreed to reduce oil production by 1.5 million barrels per day starting 1 January 2002. However, for that policy to run effectively, the reduction in OPEC production needs to be balanced with a parallel policy on the part of non-OPEC producers, such as Russia, Norway, Oman, and Mexico. In relation to OPEC policy, Indonesia's quota for oil production is estimated to fall by 77 thousand barrels per day.

PROSPECTS FOR INDONESIA'S ECONOMY

Economic growth in 2002 is projected to rise from that recorded in 2001. This is suggested by, among others, the Leading Economic Indicators (LEIs; Chart 11.2), which are on a rising trend. Higher economic growth is also supported by survey results that indicate a higher office occupancy rate.

On the demand side, economic growth is projected to originate in rising domestic demand, particularly from consumption activities. Meanwhile, foreign demand is projected to remain weak as the result of stagnant demand in most conventional markets for Indonesia's export products. On the supply side, high domestic demand would be matched by improved performance in manufacturing, trade and transportation. Overall, Indonesia's economy in 2002 will grow in the range of **3.5%– 4.0%.**

In addition to various domestic risks, projected growth for 2002 is heavily dependent upon recovery of foreign trade and the development of commodity prices in international markets. As mentioned, prices for Indonesia's main export commodities, including crude oil, would tend to remain under

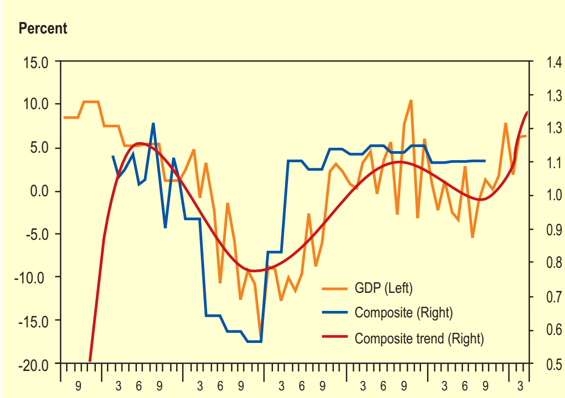


Chart 11.2.
Leading Economic Indicators

pressure. It is notable that a decline in oil prices by $2/barrel is projected to prompt a decline in economic growth of roughly 0.23%.

Agregate Demand

From **the demand side**, economic activity in 2002 will be driven by domestic demand. Consumption, which rose significantly in 2001, is expected to expand further in 2002. Investment is also projected to increase, but export growth is still limited due to weak external demand. Despite weak exports, import growth would remain strong, mainly because of the continued strong domestic demand.

Relatively high consumption growth is supported, among others, by the household consumer survey, which still suggests optimism prompted by expectation of improving incomes within the coming 6–12 months, and by expectations of improving macroeconomic conditions (Chart 11.3). On the financing side, the upward trend in consumption credits will continue, supporting spending for consumer durable goods. Optimism towards higher consumption is also reflected in the behavior of producers, who imported large amounts of raw materials and capital goods – amid declining export conditions – in the first three quarters of 2001.

Government consumption will continue to grow although at a lower rate than last year, in line with a slight decline in government routine spending. Viewed by allocation, government's limitations for stimulating consumption stem from relatively high allocations for interest payments and subsidies budgeted for 2002. However, the share of the General Allocation Fund (Dana Alokasi Umum) in the 2002 state budget which reaches more than 20% of total government spending, is expected to be able to boost consumption, mainly to consumers in the regions.

Table 11.3
GDP Growth by Expenditure

Item	2001**	2002[1]
	Percent	
Total Consumption	6.2	4.3 - 4.8
Private Consumption	5.9	4.3 - 4.8
Government Consumption	8.2	4.8 - 5.3
Total Investment	4.0	6.0 - 6.5
Exports of Goods and Services	1.9	2.3 - 2.8
Imports of Goods and Services	8.1	8.3 - 8.8
Real GDP	**3.3**	**3.5 - 4.0**

1) Projection

Investment is also projected to expand in 2002, amid mixed indicators of likely performance. On the negative side, the international market is very cautious, which makes it difficult to attract foreign investors into Indonesia. On the positive side, several pieces of micro data continue to show interest on the part of investors. For example, the business activity survey still shows a positive trend, and several large

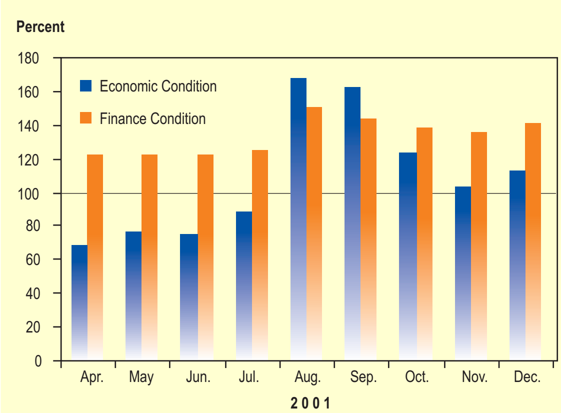


Chart 11.3.
Consumer Expectations Survey

corporations in the mining and manufacturing industry sectors have planned for quite robust expansion in 2002. In light of the downward trend in (foreign and domestic) investment approvals, investment growth is expected to originate with existing corporations that have been in Indonesia for a long time.

On the financing side, investment growth is expected to be bolstered by improved bank intermediation, suppliers' credits and internal sources of financing. In addition, the government has committed to accelerate private investment, including plans to establish an institution to supply investment funds and to expand credits to small- and medium-scale enterprises (UKM). In addition to more conducive economic fundamentals, improved socio-political conditions are expected to be able to boost the confidence of the business community and to accelerate realization of their investments in Indonesia.

Government investment is projected to remain low or even to decline a little. in 2002, due to limited sources of financing, specifically program loans and project loans. From the budgetary side, limited financing is reflected in the planned deficit, which drops from 3.7% of GDP in year 2001 to 2.5% of GDP in year 2002. In nominal terms, total government investment spending is projected to reach Rp77.7 trillion, of which 32.6% is allocated for regional governments.

On the external side, **export growth** is projected to increase, but at a relatively low rate due to the world economy, which is projected to recover only in the second half of 2002. Exports would be promoted by non-oil/gas exports, despite several commodities remaining under heavy pressure. Meanwhile, oil and gas exports are projected to decline due to the downward trend in oil prices and the reduction in Indonesia's oil production quota. Non-oil/gas exports impacted by weak external demand include: steel tube products (70% of steel tube exports are directed to the US); textiles (26% of textile market is directed to the US); and handicrafts and furniture to the European market (Germany and Denmark). This soft outlook for exports is supported by preliminary data from various associations, which suggest declining demand from Indonesia's traditional export destinations.

In addition to weak world demand, low export growth is also due to international commodity prices, which in general would not record any meaningful rise. Relatively low prices are projected for several prime commodities, such as agricultural and mining products, including crude oil. Another factor holding down exports is heightened international competition in the face of weak global demand. Moreover, foreign buyers are concerned about the continuity of Indonesian exports due to negative perceptions about local security conditions.

For its part, **import growth** is projected to remain quite high, due mainly to strong private consumption and to the slight increase in exports. In addition, low world commodity prices and the appreciation of the rupiah would give a boost to import growth. Another factor pushing up imports would be driven by the limited production of several agricultural commodities due to productivity declines and natural disasters. However, several government policies are aimed at reducing high dependence on imported goods. These include policies to stimulate domestic production and trade policies that will dampen imports in the coming year.

Agregate Supply

On a sectoral basis, moderate economic growth in 2002 will be contributed by all sectors with the largest contribution originating in manufacturing and trade.

The **agricultural sector** is expected to remain weak in 2002, particularly with regard to foodstuffs. This would be due to the possible return of El Niño; to problems in distribution of fertilizer to farmers, owing to the liberalization of fertilizer exports; and to limited financing for farmers. Domestic fertilizer needs are expected to be inadequate due to shortfalls in production in Aceh that stem from disruptions in gas supply from Exxon. Agriculture output in 2002 would decline by 1.89%, due to a decline in harvested land.[2]

As a result of lower foreign demand, exports of several agriculture products (such as wood, rubber, coffee, and tea) would remain weak. A significant decline, of some 20% – 25%, is expected in coffee production. This reduction is due to the fact that the small holders coffee plantations are not well maintained, especially with regard to fertilization, because of low prices for coffee beans. Meanwhile, the forestry sub-sector would not exhibit any meaningful recovery, due to severe forest destruction and vigorous wood plundering, stealing, and smuggling.

By contrast, production of 4 prime horticultural commodities (namely, fruit, vegetables, various plants, and decorative plants) are projected to rise by 17% in 2002, from 16.1 million tons to 18.9 million tons. In addition, production of cattle and cattle-products are projected to make a positive contribution to agricultural output, as was the case in 2001.

2 Estimate figure of BPS in February 2002.

Table 11.4
GDP Growth by Sector in 2002 (% yoy)

Sector	2001**	2002[1)]
	Percent	
Agriculture	0.8	- 0.2 – 0.3
Mining	0.1	0.7 – 1.2
Manufacturing	4.7	5.0 – 5.5
Electricity	8.8	9.4 – 9.9
Construction	2.2	3.9 – 4.4
Trade	5.6	5.3 – 5.8
Transportation	6.3	6.5 – 7.0
Finance	2.6	3.3 – 3.8
Services	1.7	1.5 – 2.0
Total	3.4	3.5 – 4.0

1) Projection

The **mining sector** is projected to expand at relatively slow pace. Security and legal assurance, particularly as regards unlicensed mining activities, are still problems in this sector. In addition, export demand for some products, such as tin, copper, nickel, aluminum, and coal, is estimated to decline. Nevertheless, investment in the mining sector, among others, by British Petroleum, Exxon Mobil, Unocal, and Gulf, for oil and gas explorations in Central Java and Papua, would go on.

Manufacturing is poised to continue as the engine for the economy, which will particularly be boosted by high domestic demand. This can be seen from the estimate of rising capacity utilization. Among the manufacturing industries that plan to add to their total production or raise their utilization rates in 2002 are: motorcycle assembling; electronics; beverages; tires; cement; pharmaceuticals; cattle feed; and plastics. In addition, several industries have plans to expand, among others the lamp industry, printing and packaging. Meanwhile, as the result of sluggish growth in the US and European economies, output of several prime export industries such as the textile and textile-product industry, and the footwear industry, is expected to decline, at least through mid-2002.

Growth in the **electricity sector** is projected to remain high. Although the capacity and production of PLN (state electricity company) in Java-Bali are not projected to increase by much in 2002, the capacity of independent power producers (IPP) will expand. This rising capacity is a response to high demand, which is reflected in a rising trend of electricity sales. The high (9.3%) annual growth of electricity sales from 1995 up to 2000 indicates continuing strong demand for electricity. Sales of electric power from the Java-Bali system by PLN in 2002 are estimated to grow by 10.2%.

The **construction sector** will begin to rebound in 2002. Several large projects, such as the Jakarta Outer Ring Route (JORR), will be realized. Housing developers have started to construct houses and market them vigorously, in line with strong demand for dwelling places. The retail property and middle- to lower-class housing sub-sectors are expected to expand, while the office space, apartments, condominiums, and industrial area will tend to be stagnant. Sales of new housing in 2002 are predicted to rise by 11%, due to expanding bank credit for housing ownership and a recovery in public purchasing power. Sales would rise despite hikes in houses' selling prices by an average of 4.7% up to 9.4%. Expansion of the property business is supported by an upward trend in cement sales and by projections of a 15.6% rise in credit to the property sector.

The **trade sector** is projected to expand robustly. The retail market in the area of Bogor–Tangerang–Bekasi is expected to rebound in 2002, whereas the retail market in Jakarta has been moving since 2001. Retail sales growth in 2002 is estimated at 15%. This is bolstered by, among others, plans to add several new mini-markets by Indomaret in Surabaya, the plan to expand Rimo department stores in Balikpapan, Riau, and Pontianak, as well as the plan to add new locations of Ramayana department stores in several provinces and districts outside Java. High retail sales indicate that domestic demand is the main engine of economic growth. Another indicator is motorcycle sales, which are expected to continue on a rising trend in 2002.

Visits by foreign tourists to Indonesia are projected to improve in 2002. This will be accounted for by repeated visitors and by a shift in the origin of tourists away from America and Europe to Asia. Multinational tourist visits in 2002 are projected to reach 5.3 million, up from 5.0 million in 2001.

Transportation is the third largest contributor to economic growth after manufacturing and trade. This sector is projected to expand quite rapidly in 2002, in part because the WTC tragedy did not have any significant impact on this sector, particularly domestic shipping. Total ship cargo volume for domestic and international shipping is projected to rise, and the total number of train passengers is estimated to continue rising. In addition, total domestic air transport passengers in 2002 would rise by 9.8%, to 8.8 million people. This is due to rising purchasing power over domestic flight tariffs (which are coming within the reach of more people) and market transfers to potential areas as a result of the implementation of regional autonomy.

The air transport sub-sector is projected to continue growing due to a large captive domestic market, particularly the transport of haj pilgrims. Sea and air transport modes are not expected to add new investments in 2002, although their utilization of existing capacity would rise. Meanwhile, investment in land transport modes, specifically trains and busses, would continue to rise. This includes a plan for the operation of a fast passenger train for the Yogyakarta-Solo-Semarang line, which is currently being pioneered by the Central Java regional government and local investors.

The domestic **financial sector** is expected to improve in 2002. In the banking sub-sector, various financial indicators are projected to recover somewhat. Based on the banking survey for quarter IV-2001, demand for new credits is projected to rise in line with improving prospects for customers' businesses.

The **services sector** is also projected to expand. The implementation of regional autonomy might give a boost to this sector, particularly public service activities. Meanwhile, entertainment and recreation activities would expand vigorously. Also, the Jakarta (metropolitan) district government plans to build facilities for tourist shopping and agribusiness centers in the Sukarno-Hatta airport area. These would sell prime export products, including agro-business products.

PROSPECTS FOR BALANCE OF PAYMENTS

Indonesia's balance of payments would improve somewhat in 2002. This is reflected in among others, the movement of capital flows. The current account will remain in surplus, although on a narrowing trend.

Export would slow in 2002, as a result of lower economic growth in advanced countries that are Indonesia's main export destinations (e.g., the US, Japan, and the European Union). Also, non-oil/gas commodity prices would remain low in the international market place.

However, these demand and price pressures are predicted to be short-term in nature, and they would ease in the second half of 2002. In this regard, non-oil/gas exports would still expand in 2002. By contrast, oil/gas exports would decline. International oil prices would improve slightly as the January 2002 agreement on the distribution of OPEC production quota takes effect, but this would not be enough to offset Indonesia's reduction in its oil production quota. Meanwhile, import growth is projected to remain strong

Table 11.5.
Indonesia's Balance of Payments Prospect Prospect

Item	2001*	2002**
	Billions of $	
A. Current Account	**5.0**	**3.1**
1. Goods	21.6	20.3
a. Exports f.o.b.	58.7	59.7
- Non-oil and gas	45.8	48.3
- Oil and gas	12.9	11.4
b. Imports f.o.b.	-37.0	-39.4
- Non-oil and gas	-31.4	-34.0
- Oil and gas	-5.6	-5.4
2. Services	-16.7	-17.3
a. Non-oil and gas	-12.4	-14.2
b. Oil and gas	-4.3	-3.0
B. Capital Account	**-8.9**	**-2.8**
1. Net official capital	-0.3	0.9
a. Official in flows	3.3	5.3
b. Debt repayment	-3.6	-4.4
2. Net private capital	-8.6	-3.8
a. Direct investment (net)	-5.9	-5.3
b. Others (net)	-2.7	1.6
C. Total (A+B)	**-3.9**	**0.3**
D. Net Errors and Omissions	**2.6**	**0**
E. Monetary Movements[1)]	**1.4**	**-0.3**

1) Minus (–) = surplus, and otherwise

prompted by continuing strong consumption and a modest pick-up in investment and exports in 2002.

In more detail, the current account in 2002 will record a surplus of $3.1 billion, lesser/lower than the past year's surplus. The trade balance would be in a surplus of $20.3 billion, while the services account would record a deficit of $17.3 billion. The trade account surplus would be largely contributed by a rise in non-oil/gas exports, which would increase by 5.5%, to $48.3 billion. Meanwhile, oil and gas exports would amount to $11.4 billion, a decline of 11.4% relative to 2001. Total imports would amount to $39.4 billion; non-oil/gas imports would reach $34.0 billion, up 8.5% from 2001. On services, the deficit will widen by $0.6 billion to $17.3 billion. This would mainly originate in rising payments for transportation, which are related to expanding imports, amounting to $342 million. There would also be a wider deficit on net investment income amounting to $738 million. Meanwhile, the sources of income from services would mainly arise from increasing foreign tourist arrivals. Foreign exchange revenue from tourism activities will increase by $764 million.

Meanwhile, capital flows would strengthen, reflected in a deficit on capital account that would narrow to $2.8 billion. Government net capital flows would be in a surplus of $930 million while private net capital flow record a deficit of $3.8 billion. Delays in the withdrawal of government foreign loans in 2001 due to policy shortfalls, are expected to be realized in 2002. In addition, to reduce the repayment burden of government foreign debts, the government will ask for rescheduling in the Paris Club III forum.

The deficit on private capital would narrow to $3.8 billion. This mainly stems from estimates of lower private sector foreign debt repayments in line with declines in outstanding private foreign debts and limited inflows of new private foreign debts. In addition, the deficit of net portfolio investment would narrow from $1.4 billion to $0.2 billion, which will be mainly due to net debt securities that are estimated to swing into a surplus of $162 million from a deficit of $1.2 million in 2001.

PROSPECTS FOR THE EXCHANGE RATE

In 2002, the rupiah exchange rate is expected to average between Rp9,500 – Rp10,500 per dollar[3] and the movement will be less volatile. This projection would be more optimistic if, in the near future, several concrete restructuring steps were taken to improve market expectations.

The rupiah would begin to strengthen in mid-2002. This is based on the expectation of stable socio-political conditions, which would open the way to accelerated resolution of various economic restructuring programs. These would create conducive, fundamental economic conditions. However, uncertain socio-political conditions could re-emerge as the transformation to democracy is still fragile.

With the prospect of better socio-political conditions, the real, banking, and monetary sectors would function better, enhancing bank intermediation process. This in turn would reduce rupiah excess liquidity in the financial sector, which has the potential to put pressure on the exchange rate. Coincident with improved domestic conditions, the world economy would begin to recover in mid-2002.

Improved domestic and foreign conditions would narrow the gap between foreign currency

3 Estimated using the approach of Technical Adjusted Behavioral Equilibrium Exchange Rate model (BEER).

demand and supply. Large foreign currency needs for imports and for private debt service payments would be matched by stronger foreign currency inflows, mainly export earnings and foreign investment (both FDI and portfolio investment). In addition, with an improving trend in socio-political conditions, pressures on foreign currency demand (which originate in speculative and asset saving activities) can be minimized. Re-enforcing these trends, a more stable exchange rate would reduce uncertainty, helping the economy to run more effectively. Various economic restructuring programs, such as debt and corporate restructurings, would make significant progress, thereby eliminating foreign exchange pressures stemming from foreign debt repayments. Meanwhile, stability in the exchange rate would reduce fiscal uncertainty, wich would assist macroeconomic stability, while improving public confidence.

INFLATIONARY PROSPECTS AND DIRECTIONS

Prospects for Inflation

Inflation in Indonesia is influenced by macroeconomic conditions and by disturbances (shocks) that reflect developments outside the macroeconomic sphere. Macroeconomic conditions mainly comprise: aggregate demand and supply; external factors; and the public's inflationary expectations. Factors outside the macroeconomic sphere include: government prices and incomes policies; natural disasters; and problems related to production and distribution.

In the short-term, inflationary pressures from the interaction of aggregate demand and supply are expected to increase. However, these pressures stem more from aggregate supply (i.e., due to limited growth of production capacity) as suppose to aggregate demand which is not expected to expand overly rapidly, given low investment in the face of robust private consumption growth. In addition, declining productivity in agricultural would contribute to higher prices for foodstuffs, because additions to supply do not match rising demand.

For their part, inflationary pressures from the external side are expected to be subdued in the coming years. Commodity prices in the international market would be low and world inflation would be limited. In addition, the exchange rate is projected to strengthen a bit, reaching an average between Rp9,500 – Rp10,500 per US dollar, due to declining political risk. However, exchange rate movements still need to be carefully monitored, because the pass-through effect of exchange rate is a significant determinant of inflation.

Another fundamental factor is public expectations towards inflation, which constitute the dominant factor in determining inflation. Inflation expectations are mainly determined by inflation in

Table 11.6.
Impact of Government Policies on CPI Inflation in 2002

Government Policy	Price/Tariff Increase (%)	Effective
Electricity tariff 1st stage	6	quarter I
Electricity tariff 2nd stage	6	quarter II
Electricity tariff 3rd stage	6	quarter III
Electricity tariff 4th stage	6	quarter IV
Fuel	22	quarter I
Excise Tax on Cigarette	10	quarter I
Telephone tariffs	15	quarter I
Minimum wage	30	quarter I

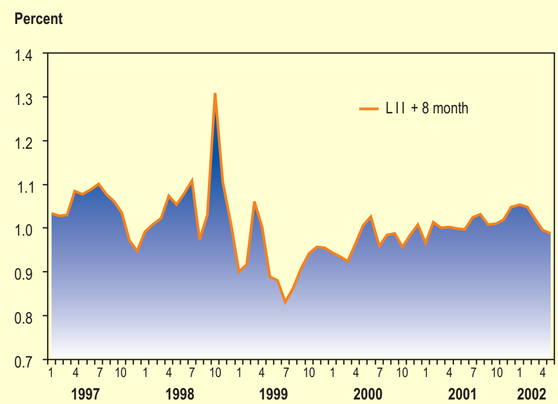


Chart 11.4.
Leading Inflation Indicator

previous periods (adaptive expectations) and by certain economic variables, particularly those that bear a close relationship with inflation (for example, the exchange rate and government prices and incomes policies). For 2002, inflationary expectations are estimated to decline a bit compared with 2001. This is based on the average inflation forecast from various research institutes of around 10%.

Outside the macroeconomic sphere, certain factors would exert strong pressure on inflation in 2002, including the implementation of government prices and incomes policies (which will result in cost-push inflation). These include: hikes in fuel prices basic electricity tariffs, and telephone tariffs; higher excise taxes on cigarettes; and the plan to raise regional/provincial minimum wages. Rough estimates indicate these will have an inflationary impact on the CPI around 2.6%.

Other factors that could have a significant impact on inflation are natural disasters and distributional problems. Disturbances in the form of natural disasters in 2002 could include a return of the El-Ni˜no weather phenomenon, which would disrupt agricultural production. This would reduce food supply and increase the price of foodstuffs.

Meanwhile, leading indicators of inflation are estimated to have peaked around October 2001. With an estimated lead time of around 8 months, these indicators suggest that the inflation cycle will peak around the first semester of 2002. On this basis, inflation (y-o-y) is expected to start declining in mid-2002.

Over **the medium term**, inflation will be dominated more by the public's inflationary expectations. At one side, Bank Indonesia's efforts to control inflation would direct the public's expectations towards declining inflation in the coming years. On another side, government prices and incomes policies will continue to push up some prices in line with government's efforts to reduce the budget deficit through lower subsidies and higher tax revenues. However, their inflationary impact is expected to decline, as the intensity of measures eases in the coming years. In addition, a stable exchange rate would hold down inflation over the medium term.

Inflation Target

Based on an evaluation of its experience in the past two years, in 2002 Bank Indonesia has decided to change the method of determining its inflation target. In this regard, the type of inflation target should be easily accepted by the public, and the level and length of the period for reaching the target should be set optimally *(Box : Setting Bank Indonesia's Inflation Target)*. For this purpose, Bank Indonesia uses CPI inflation for its target. In addition, Bank Indonesia announces a short-term inflation target (for 2002) and a medium-term inflation target that would be reached in 5 years.

The use of CPI inflation for Bank Indonesia's target is necessary in an effort to increase Bank Indonesia's role in shaping public inflationary expectations. Various criteria are considered in choosing the type of inflation target, including: acceptability; predictability; and controllability. At this moment, Bank Indonesia tends to prioritize the acceptability criterion. From among the various indicators of inflation that could be used as a target by Bank Indonesia, CPI inflation constitutes the type of inflation that comes closest to meeting the acceptability criterion. CPI inflation is the most well-known and it is easily understood by the public.

In considering macroeconomic prospects and sources of inflationary pressures, as well as the limitations of monetary policies in facing the trade-off between inflation and growth, low inflation will not be targeted in 2002. A low inflation target for 2002 would need a very tight monetary policy, which could endanger Indonesia's economic recovery. Therefore, the optimum inflation target to be achieved by the end of 2002 will be the level that is within the range of projected inflation rate for that year, namely in the range of **9%–10%.**

Over the medium term, Bank Indonesia will reduce inflation by setting a target that gradually declines. Based on a simulation, using assumptions of less intense government price policies and no fluctuation in the exchange rate, lower inflation can be achieved through cautious implementation of monetary policies. Through these policies, in the next 5 years inflation can gradually be directed into the range of 6%–7%.

By reducing inflation only gradually, excessively tight monetary policy can be avoided, so that the economic recovery can be sustained. In the meantime, success in gradually achieving the inflation target will increase Bank Indonesia's credibility, which would allow inflation to come down further with minimum social costs.

POLICY DIRECTIONS

Taking into account economic prospects, the inflation target and various challenges that will be faced in 2002, Bank Indonesia will make efforts to adopt policies in the monetary, banking, and payment system areas in a consistent manner.

In the **monetary area**, Bank Indonesia will continue to direct policies towards achieving its inflation target. Polices will focus on absorbing excess liquidity in order to meet only the real needs of the economy. This would be conducted with consideration to positive real interest rates of around 4–5%. Operationally, monetary control would be undertaken by optimizing the monetary instruments through OMO using the SBI auctions, supported by foreign exchange intervention and sterilization. These will be conducted in a cautious and measured way, so that price stability can be achieved in support of the ongoing economic recovery and long run-sustainable economic growth.

In addition, (direct and indirect) supervision will continue to be made with respect to foreign exchange transactions by non-residents. Also, various steps will be taken to improve the micro structure of the foreign exchange market, including the elimination of market segmentation to realize a more liquid and efficient market.

Considering that many non-monetary factors determine inflation, coordination needs to be improved between Bank Indonesia and the Government in order to cope with inflation arising from the impact of government policies, production factors, and the distribution of goods and services.

In the **banking area**, the main policy priority is to strengthen banking system resilience. To achieve this objective, Bank Indonesia will continue the implementation of the 25 Basle Core Principles for Effective Banking Supervision, whose details have been developed into the Master Plan for the Enhancement of Banking Supervision Effectiveness. Efforts to maintain banks' CAR at 8% will continue to be made, particularly for banks whose capital structures are still susceptible to interest rate increases, exchange rate weakness, and deteriorating asset quality. Big banks with international operations will be encouraged to raise their CAR above 8%. Furthermore, within the framework of strengthening the national financial system, Bank Indonesia is currently reviewing the Indonesian banking landscape, which is integrated with other financial institutions.

Meanwhile, in order to accelerate bank intermediation, Bank Indonesia will encourage banks to extend more credits to sectors that are considered to be ready and to be relatively low-risk (such as export credits and credits for small- and medium-scale business). In addition, Bank Indonesia will improve several stipulations to accelerate intermediation. Efforts to enhance banks' health will be further supported by continuing efforts to lower national banks' NPLs by requiring banks to achieve an NPL target of 5% by end-2002. Other efforts to strengthen banking infrastructure, generally in conjunction with the government, will include: the development of sharia banks and BPRs; establishment of a Deposit Insurance Institution and creation of a supervision institution for the financial services sector.

In the **cash payment system area**, policies will be directed at the provision of money in fit-for-circulation condition and in sufficient amount to meet public needs in terms of nominal value and denominations. These policies include, among others, rearrangement of the money distribution channel and the establishment of a laboratory for testing materials for money. In addition, Bank Indonesia will continue the implementation of the Money Market Information System at coordinating offices that are integrated with the head office.

On the **non-cash payment system**, policies will continue to reduce payment risks; to enhance payment system service quality and capacity; and to regulate payment system supervision, in order to create a payment system that is fast, secured, and efficient. These policies will be realized by continuing the implementation of the BI-RTGS system in 15 Bank Indonesia regional offices. When all Bank Indonesia regional offices have been using this system, the system will greatly assist with the implementation of Bank Indonesia's tasks to monitor banks' compliance with the minimum reserve requirement (GWM) and bank liquidity.

Meanwhile, in order to enhance the quality and capacity of payment system services, particularly those related with clearing operations, Bank Indonesia has developed the Long Distance Clearing Information System, which is to be implemented at the Jakarta head office and Bank Indonesia regional offices that are already using the automated clearing system. In addition, Bank Indonesia is also undertaking the development of certain stipulations, including : supervision of payment system operator; operation of payment system services using non-cash payment instruments; the payment system's supporting services; and coping with clearing participants' failures to meet their settlement obligations.

In order to reduce settlement risks in the capital market, Bank Indonesia will undertake the development of stage one of the Delivery Versus Payment (DVP) system. This will enable the formation of an integrated settlement system between the payment side (payment leg) through the BI-RTGS system and the delivery side of securities (delivery leg) through securities settlements.

APPENDICESS

Appendix A

BANK INDONESIA

Head Office

Jakarta

Representative Offices

London
New York
Singapore
Tokyo

Regional Offices

Ambon, Balikpapan,
Banda Aceh, Bandar Lampung,
Bandung, Banjarmasin, Batam, Bengkulu, Cirebon
Denpasar, Jambi, Jayapura, Jember, Kediri, Kendari,
Kupang, Lhokseumawe, Makassar, Malang, Manado, Mataram,
Medan, Padang, Palangkaraya, Palembang, Palu,Pekanbaru,
Pontianak, Purwokerto, Samarinda, Semarang,
Sibolga, Solo, Surabaya, Tasikmalaya,
Ternate, Yogyakarta

Appendix B

Board of Governors of Bank Indonesia

As of December 31, 2001

Governor

Syahril Sabirin

Senior Deputy Governor

Anwar Nasution

Deputy Governors

Miranda S. Goeltom

Aulia Pohan

Achjar Iljas

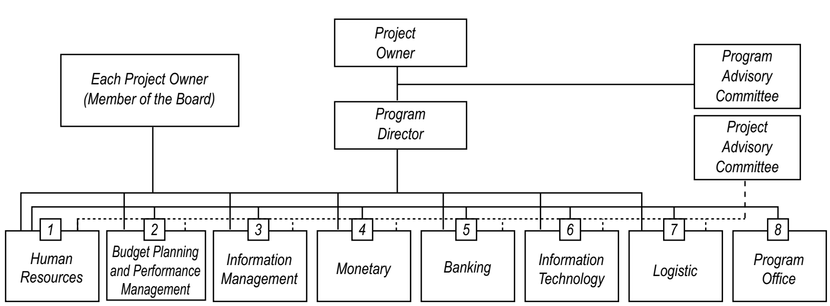
Appendix C.1

Organization and Human Resources

During the reporting year, Bank Indonesia made several improvements in its organization and human resource development.

To cope with the undertaking of basic and overall change Bank Indonesia is implementing Bank Indonesia's Transformation Program. This program will be implemented in stages and has been undertaken since October 2001 following earlier Diagnostic Study activity. This study resulted in determined 7 priority programs, which have strategic values for Bank Indonesia to implement. These programs concern the areas of Budget Planning and Performance Management, Human Resource Development, Banking, Information Management, Information Technology, Monetary, and Logistic (Diagram 1). For the implementation of these strategic programs a separate work unit, named "Special Unit for Transformation Program" has been established.

In addition to the above Transformation Program, several organizational enhancements continued to be undertaken, in particular those that have important impacts for Bank Indonesia in enhancing the implementation quality of its tasks. Those enhancements covered organizational enhancement at the Economic and Monetary Statistics Directorate due to a new framework of foreign currency flow monitoring; the establishment of Sharia Banking Bureau for a more focused handling of banks that operate based on the sharia principles, and organizational enhancement at the Foreign Affairs Directorate due to the implementation of off-site verification on guarantee for Trade Maintenance Facility (TMF) and Inter Bank Debt/ Exchange Offer (IBD/EO) previously handled by the Banking Directorate. In line with the guarantee on IBD/EO and on commercial banks/credit rural banks



Notes :
– Project Owner is the Governor of Bank Indonesia supported by the Board of Governors
– Each Project Owner is a Deputy Governor who directly manages the workstream

Diagram 1
Special Unit for Bank Indonesia Transformation Program

(BPRs) obligation payments, organizational enhancements were also undertaken in other Monetary Directorates due to the implementation of Government IOUs management tasks. Aside from that, organizational enhancement was undertaken at the Currency Circulation Directorate due to the implementation of efficient and effective Currency Handling System.

In relation to the human resource development, Bank Indonesia continued to improve the Human Resource Management System, including the enhancement of the professionalism of human resource functions supported by "man to job fit" personnel in accordance with work units' needs. During 2001 several new internal regulations concerning employee discipline and awards related to service periods were implemented. In addition, development of several regulations concerning career path management and promotion system were completed.

In line with new emerging provinces in Indonesia, such as the Provinces of Banten, Bangka-Belitung and Gorontalo, several Bank Indonesia regional offices job authorization were reviewed in line with their new geographical coverage.

In order to create a clean corporate governance free of corruption, collusion, and nepotism, members of the Board and high rank Bank Indonesia officials are obliged to submit formal reports on their assets and wealth.

Number of Personnel

No.	End of Financial Year	Head Office	Regional Offices	Representative Offices	Total
1.	1997/1998	3,341	2,882	67 1)	6,290
2.	1998/1999	3,299	2,852	21	6,172
3.	1999/2000	3,068	2,601	17	5,686
4.	2000/2001	3,123	2,615	18	5,756
5.	January 2002	3,119	2,556	18	5,693

1) Including those studying abroad

Head Offices

Directorate of Economic Research and Monetary Policy	:	Hartadi A. Sarwono
Directorate of Economic and Monetary Statistics	:	Ratnawati Priyono
Directorate of Monetary Management	:	Aslim Tajuddin
Directorate of Reserve Management	:	Made Sukada
Directorate of International Affairs	:	Veronica W.S.P.
Bureau of Credit	:	Roswita Roza
Directorate of Banking Research and Regulation	:	-
Directorate of Bank Licensing and Banking Information	:	Imam Sukarno
Directorate of Bank Supervision 1	:	Siti Ch. Fadjriah S.
Directorate of Bank Examination 1	:	Aris Anwari
Directorate of Bank Supervision 2	:	-
Directorate of Bank Examination 2	:	Octo R. Nasution
Directorate of Rural Bank Supervision	:	Abdul Salam
Directorate of Currency Circulation	:	Adi Putra Hasan
Directorate of Accounting and Payment System	:	Harmain Salim
Directorate of Logistics and Security	:	M. Ashadhi
Directorate of Information Technology	:	J. L. Mangunsong
Directorate of Human Resources	:	Baridjussalam Hadi
Directorate of Internal Financial Management	:	-
Directorate of Legal Affairs	:	Kusumaningtuty
Directorate of Internal Audit	:	Bachri Ansjori
Office of The Governor	:	Halim Alamsyah S.
Office of The Secretariat	:	Djatiwaluyo
Special Unit For Banking Investigation	:	Prihono Bagio
Center of Education and Central Banking Studies	:	Bambang S. Wahyudi
Bureau of Islamic Banking	:	Harisman
Special Unit For Transformation Program	:	Romeo Rissal

Representative Offices

Singapore	:	Kemas A. Sjarifuddin
Tokyo	:	Djakaria
London	:	Rasmo Samiun
New York	:	Maman Hendarman

Regional Offices

Category I

Bandung	:	Djoko Sarwono
Medan	:	Bambang Setijoprodjo
Semarang	:	Ardhayadi
Surabaya	:	Sumantri

Category II

Bandar Lampung	:	Imrandani
Banjarmasin	:	M. Zaeni Abu Amin
Denpasar	:	Ilham Ikhsan
Manado	:	M. Djaelani S.
Padang	:	Abdul Azis
Palembang	:	Irman Djaja Dalimi
Makassar	:	Djoko Sutrisno
Yogyakarta	:	Amril Arief

Category III

Ambon	:	M. Yusuf Oesep W.
Banda Aceh	:	Yusmanazir Katin
Cirebon	:	Djarot Sumartono
Jambi	:	Ade N. Rachmana
Jayapura	:	Sahat Tampubolon
Malang	:	Sentot Purnomo
Mataram	:	Satria Mulya
Pekanbaru	:	C. Y. Boestal
Pontianak	:	Amin Sisworo
Samarinda	:	Sarman Bona Sihotang
Solo	:	Adiastopo Joko Purnomo

Category IV

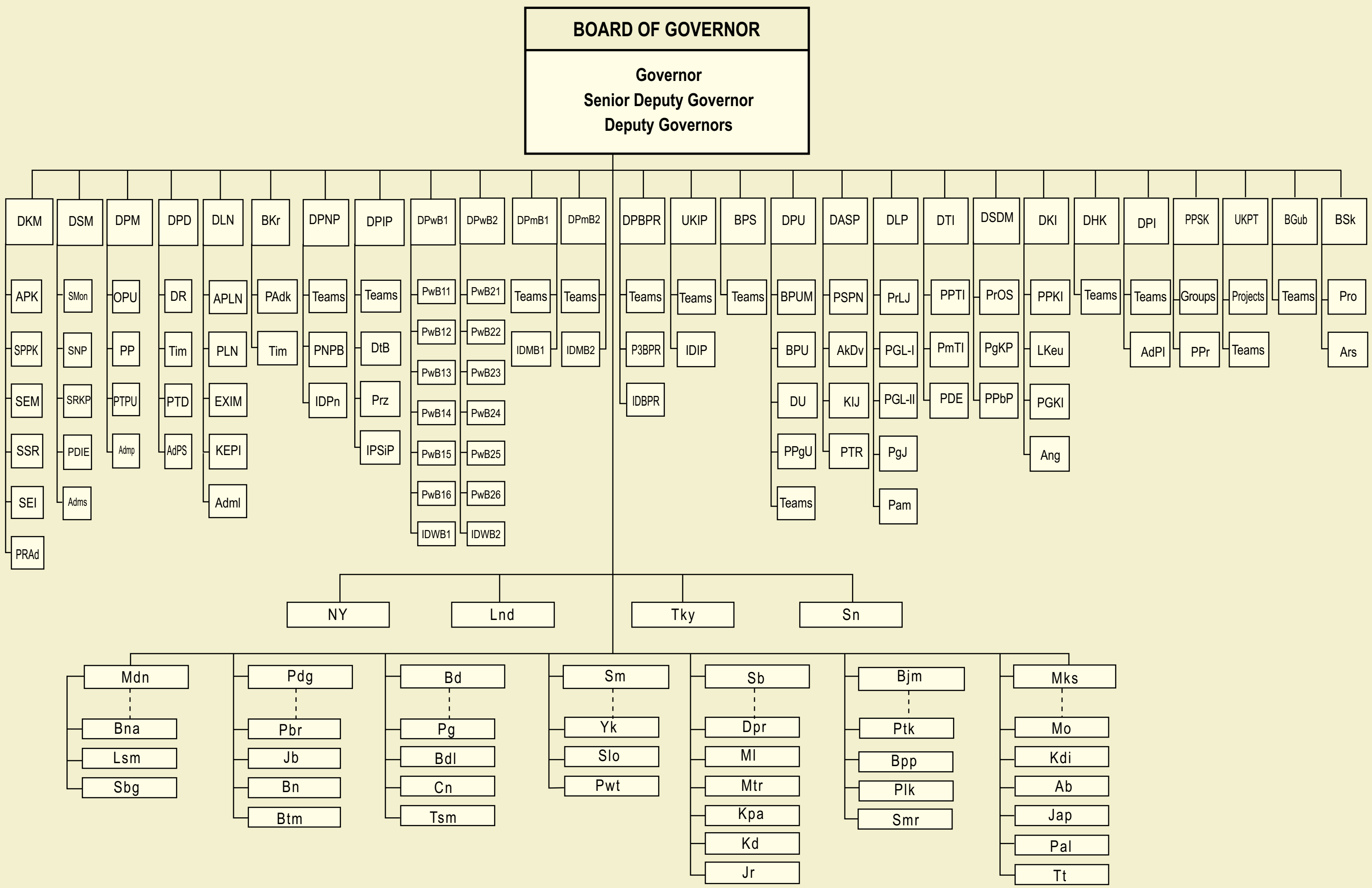
Balikpapan	:	Erman Kurnandi
Kupang	:	Dikan
Jember	:	Sutikno
Kediri	:	Budhi Santoso
Purwokerto	:	Sumarno
Tasikmalaya	:	Sunarko
Palangkaraya	:	-
Bengkulu	:	Joko Wardoyo
Kendari	:	Mokhammad Dakhlan
Palu	:	Moch. Zaenal Alim

Category V

Batam	:	Ali Imron Murim
Sibolga	:	Yasin Effendi
Lhokseumawe	:	Fachrurrazi
Ternate	:	Muh. Abdul Fadlil

Appendix C.2

ORGANIZATION CHART OF BANK INDONESIA



Head Office of Bank Indonesia

No.	Directorates and Divisions	Abbreviations
I.	**DIRECTORATE OF ECONOMIC RESEARCH AND MONETARY POLICY**	**DKM**
	1. Policy Analysis and Planning Division	APK
	2. Financial Market Structure Studies Division	SPPK
	3. Macro Economic Studies Division	SEM
	4. Real Sector Studies Division	SSR
	5. International Economic and Institution Studies Division	SEI
	6. Research Library and Administration Division	PRAd
II.	**DIRECTORATE OF ECONOMIC AND MONETARY STATISTICS**	**DSM**
	1. Monetary Statistics Division	SMon
	2. Balance of Payment Statistics Division	SNP
	3. Real Sector and Government Finance Statistics Division	SRKP
	4. Economic and Monetary Data and Information Processing Division	PDIE
	5. Administration Division of Economic and Monetary Statistics	Adms
III.	**DIRECTORATE OF MONETARY MANAGEMENT**	**DPM**
	1. Money Market Operation Division	OPU
	2. Money Market Development Division	PPU
	3. Money Market Settlement Division	PTPU
	4. Money Market Administration Division	Admp
IV.	**DIRECTORATE OF RESERVE MANAGEMENT**	**DPD**
	1. Dealing Room	DR
	2. Risk Management Team	-
	3. Economic Analysis and Reserve Regulation Team	-
	4. Reserve Settlement Division	PTD
	5. Administration and Treasury System Maintenance Division	AdPS
V.	**DIRECTORATE OF INTERNATIONAL AFFAIRS**	**DLN**
	1. Foreign Debt Administration and Analysis Division	APLN
	2. Foreign Debt Division	PLN
	3. Export and Import Division	EXIM
	4. International Trade and Economic Cooperation Division	KEPI
	5. Administration Division of International Affairs	AdmI
VI.	**BUREAU OF CREDIT**	**BKr**
	1. Credit Management and Administration Division	PAdk
	2. Research and Development Team	-
VII.	**DIRECTORATE OF BANKING RESEARCH AND REGULATION**	**DPNP**
	1. Teams	-
	a. Banking Regulation Team	
	b. Bank Supervision Development Team	
	2. Banking Research Bureau	PNPB
	3. Information and Documentation Division of Banking Research and Regulation	IDPnP

No.	Directorates and Divisions	Abbreviations
VIII.	**DIRECTORATE OF BANK LICENSING AND BANKING INFORMATION**	**DPIP**
	1. Bank Liquidation Team	–
	2. Banking Data Division	DtB
	3. Bank Licensing Division	Prz
	4. Information and Banking Information System Development Division	IDSiP
IX.	**DIRECTORATE OF BANK SUPERVISION 1**	**DPwB1**
	1. Bank Supervision Division 11	PwB11
	2. Bank Supervision Division 12	PwB12
	3. Bank Supervision Division 13	PwB13
	4. Bank Supervision Division 14	PwB14
	5. Bank Supervision Division 15	PwB15
	6. Bank Supervision Division 16	PwB16
	7. Information and Documentation Division of Bank Supervision 1	IDWB1
X.	**DIRECTORATE OF BANK SUPERVISION 2**	**DPwB2**
	1. Bank Supervision Division 21	PwB21
	2. Bank Supervision Division 22	PwB22
	3. Bank Supervision Division 23	PwB23
	4. Bank Supervision Division 24	PwB24
	5. Bank Supervision Division 25	PwB25
	6. Bank Supervision Division 26	PwB26
	7. Information and Documentation Division of Bank Supervision 2	IDWB2
XI.	**DIRECTORATE OF BANK EXAMINATION** 1	**DPmB1**
	1. Bank Examiner Teams	-
	2. Information and Documentation Division of Bank Examination 1	IDMB1
XII.	**DIRECTORATE OF BANK EXAMINATION 2**	**DPmB2**
	1. Bank Examiner Teams	-
	2. Information and Documentation Division of Bank Examination 2	IDMB2
XIII.	**DIRECTORATE OF RURAL BANK SUPERVISION**	**DPBPR**
	1. Teams	-
	a. Rural Bank Supervision Teams	
	b. Rural Bank Deposit Insurance and Liquidation Team	
	2. Rural Bank Licensing, Research and Regulation Division	P3BPR
	3. Information and Documentation Division of Rural Bank Supervision	IDBPR
XIV.	**SPECIAL UNIT FOR BANKING INVESTIGATION**	**UKIP**
	1. Banking Investigation Teams	-
	2. Information and Documentation Division of Banking Investigation	IDIP
XV.	**ISLAMIC BANKING BUREAU**	**BPS**
	1. Teams	–
	a. Islamic Banking Research and Regulation Team	
	b. Islamic Bank Supervision Team	
	c. Islamic Banking Licensing and Administration Team	

No.	Directorates and Divisions	Abbreviations
XVI.	**DIRECTORATE OF CURRENCY CIRCULATION**	**DPU**
	1. Cash Deposit Division	BPUM
	2. Cash Withdrawal Division	BPUK
	3. Currency Distribution Division	DU
	4. Currency Procurement Division	PPgu
	5. Currency Research, Planning and Regulation Team	–
XVII.	**DIRECTORATE OF ACCOUNTING AND PAYMENT SYSTEM**	**DASP**
	1. National Payment System Development Bureau	PSPN
	2. Foreign Exchange Accounting Division	AkDv
	3. Jakarta Clearing Division	KlJ
	4. Rupiah Settlement Division	PTR
XVIII.	**DIRECTORATE OF LOGISTICS AND SECURITY**	**DLP**
	1. Logistics and Services Planning Division	PrLJ
	2. Logistics Management Division I	PgL-I
	3. Logistics Management Division II	PgL-II
	4. Services Management Division	PgJ
	5. Security Division	Pam
XIX.	**DIRECTORATE OF INFORMATION TECHNOLOGY**	**DTI**
	1. Information Technology Research and Development Bureau	PPTI
	2. Information Technology Maintenance Division	PmTI
	3. Electronic Data Processing Division	PDE
XX.	**DIRECTORATE OF HUMAN RESOURCES**	**DSDM**
	1. Organization and Human Resources Planning Bureau	PrOS
	2. Career Development Division	PgKP
	3. Recruitment and Counselling Division	PPbP
XXI.	**DIRECTORATE OF INTERNAL FINANCIAL MANAGEMENT**	**DKI**
	1. Corporate Financial Planning and Controlling Bureau	PPKI
	2. Financial Report Division	LKeu
	3. Salary and Corporate Financial Administration Division	PGKI
	4. Budget Division	Ang
XXII.	**DIRECTORATE OF LEGAL AFFAIRS**	**DHk**
	1. Teams	–
	a. Legal Advisor Team	
	b. Legal Information and Documentation Team	
	c. Enquiry Point Team	
XXIII.	**DIRECTORATE OF INTERNAL AUDIT**	**DPI**
	1. Teams	
	a. Internal Audit Development Team	
	b. Regulation Analysis Team	
	c. Audit Teams	
	2. Administration and Information Division of Internal Audit	AdPI

No.	Directorates and Divisions	Abbreviations
XXIV.	**CENTER OF EDUCATION AND CENTRAL BANKING STUDIES**	**PPSK**
	1. Designing and Evaluation Group	-
	2. Researchers' Group	-
	3. Program Conducting Division	PPr
XXV.	**SPECIAL UNIT FOR TRANSFORMATION PROGRAM**	UKPT
	1. Projects	–
	2. Program Office Team	
XXVI.	**OFFICE OF THE GOVERNOR**	BGub
	1. Teams	-
	a. Planning and Monitoring Team	
	b. Public Relation Team	
	c. Governor Staff	
XXVII.	**OFFICE OF THE SECRETARIAT**	**Bsk**
	1. Protocol Division	Pro
	2. Archives Division	Ars

Regional Offices and Representative Offices		Abbreviations
Representative Offices		
1.	New York	NY
2.	London	Lnd
3.	Tokyo	Tky
4.	Singapore	Sn
Regional Offices		
1.	Ambon	Ab
2.	Balikpapan	Bpp
3.	Banda Aceh	Bna
4.	Bandar Lampung	Bdl
5.	Bandung	Bd
6.	Banjarmasin	Bjm
7.	Batam	Btm
8.	Bengkulu	Bn
9.	Cirebon	Cn
10.	Denpasar	Dpr
11.	Jayapura	Jap
12.	Jambi	Jb
13.	Jember	Jr
14.	Kediri	Kd
15.	Kendari	Kdi
16.	Kupang	Kpa
17.	Lhokseumawe	Lsm
18.	Makassar	Mks
19.	Malang	Ml
20.	Mataram	Mtr
21.	Medan	Mdn
22.	Manado	Mo
23.	Padang	Pdg
24.	Palangkaraya	Plk
25.	Palembang	Pg
26.	Palu	Pal
27.	Pekanbaru	Pbr
28.	Pontianak	Ptk
29.	Purwokerto	Pwt
30.	Samarinda	Smr
31.	Semarang	Sm
32.	Sibolga	Sbg
33.	Solo	Slo
34.	Surabaya	Sb
35.	Tasikmalaya	Tsm
36.	Ternate	Tt
37.	Yogyakarta	Yk

Appendix D.1

Bank Indonesia
Balance Sheet
as of December 31, 2001 and December 2000[1)]
(in Million Rupiah)

Assets	**Dec 31, 2001** *Unaudited*	**Dec 31, 2000** *Audited*
1. Gold	8,934,005	8,170,712
2. Foreign Currencies	453,368	794,307
3. Special Drawing Rights	165,030	317,855
4. Demand Deposits	**11,488,488**	**5,300,013**
4.1 Central Banks	8,758,350	2,950,464
4.2 Correspondent Banks	2,730,138	2,349,549
5. Time Deposits at Correspondent Banks	69,068,707	61,544,917
6. Marketable Securities	**209,659,339**	**218,064,845**
6.1 In Rupiahs	0	0
6.2 In Foreign Exchanges	209,659,339	218,064,845
7. Claims		
7.1 On Government	**315,944,501**	**279,600,597**
7.1.1 In Rupiahs	315,914,159	279,477,036
7.1.2 In Foreign Exchanges	30,342	123,561
7.2 On Banks	**19,182,641**	**20,296,434**
7.2.1 In Rupiahs	17,949,682	18,634,761
7.2.2 In Foreign Exchanges	1,232,959	1,661,673
7.3 On Others	**7,496,935**	**7,280,073**
7.3.1 In Rupiahs	7,496,935	7,280,073
7.3.2 In Foreign Exchanges	0	0
8. Allowance for Bad Debt	(49,455,231)	(27,654,796)
9. Equity Participation	238,974	241,955
10. Other Assets	9,400,041	6,364,478
Total Assets	**602,576,798**	**580,321,390**

Liabilities and Equities	**Dec 31, 2001** *Unaudited*	**Dec 31, 2000** *Audited*
A. Liabilities		
1. Currency in Circulation	91,275,598	89,704,449
2. Demand Deposits		
2.1 Government	**84,954,294**	**96,190,490**
2.1.1 In Rupiahs	47,984,852	66,228,447
2.1.2 In Foreign Exchanges	36,969,442	29,962
2.2 Banks	**41,863,845**	**41,105,359**
2.2.1 In Rupiahs	34,644,502	33,677,047
2.2.2 In Foreign Exchanges	7,219,343	7,428,312
2.3 Other Private Sectors	**1,141,237**	**1,933,458**
2.3.1 In Rupiah	1,014,322	1,731,572
2.3.2 In Foreign Exchanges	126,915	201,886
2.4 Internasional Financial Institution	**95,791,501**	**105,134,986**
2.4.1 In Rupiah	95,791,501	105,134,986
2.4.2 In Foreign Exchanges	0	0
3. Bank Indonesia Certificate	**102,143,747**	**78,672,929**
3.1 In Rupiahs	102,143,747	78,672,929
3.2 In Foreign Exchanges	0	0
4. Loans from Government	**30,226,201**	**28,092,771**
4.1 In Rupiahs	309,089	340,694
4.2 In Foreign Exchanges	2,679,045	2,721,585
4.3 Bank Indonesia Bond	27,238,067	25,030,492
5. Foreign Borrowings	19,872,947	19,142,030
6. Other Liabilities	1,432,711	1,143,421
Total Liabilities	**468,702,081**	**461,119,893**
B. Equities		
1. Capital	2,948,029	2,606,236
2. General Reserves	8,233,006	6,430,544
3. Statutory Reserves	3,528,431	2,755,947
4. Fixed Assets Revaluation Reserves	4,871,249	4,768,103
5. Exch Rate & Foreign Security Revaluations Reserve	50,675,217	79,950,773
6. Government Bond Indexation Reserve	48,575,749	18,817,604
7. Bank Indonesia Bond Indexation Reserve	(2,339,793)	(476,122)
8. Previous Year Surplus	0	1,773,466
9. Current Year Surplus	17,442,829	2,574,946
Total Equities	**133,874,717**	**119,201,497**
Total Liabilities and Equities	**602,576,798**	**580,321,390**

1) a. The Financial Report of Bank Indonesia in 2000 has been audited by the Supreme Audit Authority according to report No.01/01/Auditama II/GA/V/2001, May 8, 2001 with qualified opinion on claim account due to Bank Indonesia Liquidity Support (BLBI)

b. Unaudited. The Comprihensive Financial Report of Bank Indonesia in 2001 was submitted to Supreme Audit Authority through the letter No.4/1/GBI/DKI, dated January 31, 2002 to be audited.

c. Bank Indonesia Dollar/Rupiah Rate as of December 31, 2000: \$1 = Rp9.595,00 and as of December 31, 2001: \$1 = Rp10.400,00.

Appendix D.2

Bank Indonesia
Surplus Deficit Statement
For the Period ended December, 31 2001 and 2000
(In Million Rupiah)

	2001	2000
	Unaudited	*Audited*
Revenues		
1. Monetary Operations	**62,904,839**	**46,223,030**
1.1 Foreign Exchange Management	54,480,178	35,552,594
1.2 Money Market Activities	3,889	51,984
1.3 Loan and Financing	8,420,772	10,618,452
2. Payment System Services	**42,162**	**38,703**
3. Banking Supervision	**46,811**	**32,509**
4. Others	**173,919**	**3,295,396**
4.1 Other Revenues	173,919	570,849
4.2 Allowance for Bad Debt Recovery	0	2,724,547
Total Revenues	**63,167,732**	**49,589,638**
Expenses		
1. Monetary Operations	**(21,068,778)**	**(19,929,814)**
1.1 Formulating and Implementing Monetary Policy	(15,408,536)	(11,914,197)
1.2 Foreign Exchange Management	(5,660,242)	(8,015,617)
2. Payment System Services	**(727,482)**	**(720,873)**
2.1 Currency Circulation	(679,295)	(695,602)
2.2 Payment System Sponsoring	(48,187)	(25,271)
3. Banking Supervision	**(52,505)**	**(131,855)**
4. General and Administration	**(23,876,138)**	**(1,677,780)**
4.1 General, Administration and Others	(1,979,252)	(1,539,234)
4.2 Fixed Assets Depreciation	(127,393)	(138,546)
4.3 Allowance for Bad Debts	(21,769,493)	0
Total Expenses	**(45,724,904)**	**(22,460,322)**
Surplus Before Extraordinary Items	**17,442,829**	**27,129,316**
Extraordinary Expenses	**0**	**(24,554,370)**
SURPLUS	**17,442,829**	**2,574,946**

Appendix E.1

Bank Indonesia Regulation Issued in 2001

No.	PBI Number	Date	Gazette	Description
1	3/1/PBI/2001	04-01-2001	LN Thn 2001 No.2; TLN No.4071	Bank Indonesia adjusted the regulation to implement the Micro Credit Project (PKM) to ensure smooth implementation and to keep the project in accordance with Act Number 23 of 1999. The adjusment include: (i) source of loan, (previously provided by Bank Indonesia Liquidity Credit, now fully provided by Asian Development Bank) and (ii) extension of the duration of project implementation from December 2000 to the end of June 2001. *The regulation was later revised by PBI No.3/8/PBI/2001 dated 25-04-2001*
2	3/02/PBI/2001	04-01-2001	LN Thn 2001 No.3; TLN No.4072	Bank Indonesia amended the regulation on credits to small scale business (KUK). The amendment includes: (i) bank's obligation to extend KUK, (ii) bank's obligation to disclose its KUK plan in their Annual Work Plan (RKAT), (iii) bank's obligation to report its KUK extension in the Commercial Bank Monthly Report, (iv) bank's obligation to report its realized KUK in their Financial Report, (v) KUK ceiling adjusment to Rp500 million for each customer, (vi) Bank Indoneia technical assistance to banks extending KUK, and (vii) reducing the sanctions and incentives related to KUK extension.
3	3/03/PBI/2001	12-01-2001	LN Thn 2001 No.7; TLN No.4074	Bank Indonesia restricted banks to extend rupiah and foreign currency credit to non residents. The banks are also limited in performing foreign currency derivative transactions against rupiah with non-residents i.e., foreign citizens; foreign legal entities or other foreign entities, Indonesian citizens with foreign permanent resident status and domicile outside Indonesia; representatives of foreign

No.	PBI Number	Date	Gazette	Description
				countries and international institutions in Indonesia, and offices of Indonesian banks/legal entities abroad.
4	3/04/PBI/2001	12-03-2001	LN Thn 2001 No.7; TLN No.4080	Bank Indonesia issued a revised regulation on trade maintenance facility/TMF by extending the duration program implementation to June, 30, 2001. The extension is based on the consideration that TMF is still needed to support domestic economic recovery, particulary with respect to international trade. Revoked by *PBI No.3/20/ PBI/2001 dated 29-11-2001*
5	3/05/PBI/2001	22-03-2001	LN Thn 2001 No.23; TLN No.4082	The regulation on Government Guarantee on deposit and interbank money market, as stipulated in Bank Indonesia Board of Directors Decree No.31/32/Kep/Dir dated May 29, 1998, was amended by Bank Indonesia Regulation Number 3/5/PBI/2001. According to this regulation, the Government does not guarantee deposit bearing interest higher than the determined maximum interest rates.
6	3/06/PBI/2001	02-04-2001	LN Thn 2001	In accordance with Act Number 23 of 1999, Bank Indonesia is prohibited to extend any liquidity support except for overcoming the bank's short-term financial problem. To be eligible for such support, bank should provide high quality and liquid collaterals. Since the existing Guarantee and Financing Facility Program provided by Bank Indonesia contains elements of credit extension, Bank Indonesia revoked some regulations as follows: a. Bank Indonesia Board of Directors Decree Number 30/138/KEP/DIR concerning the Sale and Purchase of Bills issued based on Domestic Letter of Credit to Bank Indonesia, b. Bank Indonesia Board of Directors Decree Number 30/193/KEP/DIR concerning the Sale and Purchase of Foreign Exchange from Exports for Exporters and Certain Exporters, c. Bank Indonesia Board of Directors Decree Number

No.	PBI Number	Date	Gazette	Description
				30/194/KEP/DIR concerning the Sale and Purchase of Incoming Foreign Exchange for Certain Exporters, d. Bank Indonesia Board of Directors Decree Number 31/187/KEP/DIR concerning the Guarantee and or Financing Letter of Credits through Bank Indonesia placement in foreign banks.
7	3/07/PBI/2001	02-04-2001	LN Thn 2001 No.32	Bank Indonesia revoked the regulation regarding the government guarantee on commercial banks' obligation in accordance with prohibition on Bank Indonesia to provide financing and guarantee facility.
8	3/08/PBI/2001	25-04-2001	LN Thn 2001 No.39 TLN No.4089	Bank Indonesia issued regulation on micro credit project which raised the maximum ceiling of micro credits.
9	3/09/PBI/2001	06-06-2001	LN Thn 2001 No.70	Bank Indonesia issued special coins series in commemoration of Bung Karno's centennial anniversary on June 6, 2001. The coins are produced in denomination of Rp500,000 (Five Hundred Thousand Rupiah) and Rp25,000 (Twenty Five Thousand Rupiah).
10	3/10/PBI/2001	18-06-2001	LN Thn 2001 No.78 TLN No.4107	Bank Indonesia issued a regulation on the implementation of the Know Your Customer ("KYC") principles. The regulation concerns the principles implemented by banks in order to know and recognize their customer's identity and in monitoring its customer's transactions including to report suspicious transactions. Bank are obliged to establish a policy on customer acceptance and establish a policy and procedure for customer's identification, customer's account and transactions monitoring and risk management in line with the implementation of Know Your Customer Principles.
11	3/11/PBI/2001	20-06-2001	LN Thn 2001 No.79 TLN No.4108	In order to support the achievement of Bank Indonesia's objective in obtaining and maintaining the stability of the Rupiah, Bank Indonesia adjusted the list of external parties who are allowed to open an account with Bank Indonesia.

No.	PBI Number	Date	Gazette	Description
				Those are banks, government institutions, international financial institutions and any other institutions deemed necessary determined by Bank Indonesia.
12	3/12/PBI/2001	09-07-2001	LN Thn 2001 No.98 TLN No.4123	Bank Indonesia issued a regulation concerning the terms and arrangements in implementing the government guarantee on rural bank liabilities. This regulation amends the Bank Indonesia Board of Directors Decree Number 31/166/KEP/DIR and Number 31/167/KEP/DIR dated December 11, 1998. It stipulates among others the criteria for guaranteed deposit by considering the objective of the Government Guarantee Program Regulation, i.e to protect the customer's funds and public interest. To participate in the program, rural banks must fulfill the requirements, namely signing the participation statement, paying the guarantee fee and submitting the supporting administrative documents.
13	3/13/PBI/2001	03-09-2001	LN Thn 2001 No.115 TLN No.4135	The window time for Open Market Operation and Rupiah's Intervention was adjusted due to the implementation of Bank Indonesia System of Real Time Gross Settlement (RTGS).
14	3/14/PBI/2001	20-09-2001	LN Thn 2001 No.121 TLN No.4140	Bank Indonesia amended PBI No.2/12/PBI/2000 on Interbank Debt Exchange Offer. Banks are now allowed to repay all or partially its Interbank Debt Excahnge Offer through the prepayment and Buy Back scheme.
15	3/15/PBI/2001	21-09-2001	LN Thn 2001 No.122 TLN No.4141	Bank Indonesia issued a regulation regarding the status of BPRs under the Special Supervision Framework and frozen BPR's activities in order to enhance sound banking practices.
16	3/16/PBI/2001	03-10-2001	LN Thn 2001 No.123 TLN No.4142	Bank Indonesia issued a second amendment on Bank Indonesia Regulation Number 3/1/PBI/2001 concerning Micro Credit Project (PKM) by extending the PKM term to the end of December 31, 2001. The term may be revisited

No.	PBI Number	Date	Gazette	Description
				should there be new agreement between the Government and Asian Development Bank.
17	3/17/PBI/2001	04-10-2001	LN Thn 2001 No.125 TLN No.4143	Bank Indonesia issued a regulation concerning the Commercial Banks Report (Laporan Berkala Bank Umum-LBBU). Head offices of the commercial bank, including the office of foreign bank, are obliged report their LBBU accurately, completely and in a timely manner.
18	3/18/PBI/2001	17-10-2001	LN Thn 2001 No.130 TLN No.4147	Bank Indonesia amended the regulation on requirements and procedures to bring a certain amount of Rupiah currency out of or into the custom territory of the Republic Indonesia.
19	3/19/PBI/2001	26-10-2001	LN Thn 2001 No.131	Bank Indonesia issued the new 2001 emision of Rp 5,000 banknote. The front side of the new banknote depicts National Hero Tuanku Imam Bondjol, while the reverse side depicts the Pandai Sikek handloom weavers of West Sumatra.
20	3/20/PBI/2001	29-11-2001	LN Thn 2001 No. 140	Bank Indonesia revoked Regulation Number 2/13/PBI/2000 concerning Guarantee on International Trade Maintenance Facility and its amendment, Regulation Number 3/4/PBI/2001, due to the termination of the International Trade Maintenance Facility provided by Bank Indonesia on June 30, 2001.
21	3/21/PBI/2001	13-12-2001	LN Thn 2001 No.149 TLN No.4158	Bank Indonesia issued regulation requiring the commercial bank to maintain its Capital Adequacy Ratio (CAR) at least 8% by the end of December 2001 to comply with international standards.
22	3/22/PBI/2001	13-12-2001	LN Thn 2001 No.150 TLN No.4159	Bank Indonesia issued a regulation concerning transparency on bank financial condition to promote good corporate governance in the national banking system. By putting transparency in practice, the national banking system is expected to gain public trust. The transparency

No.	PBI Number	Date	Gazette	Description
				practice would decrease the lack of information, therefore enable the market participants to make a proper assessment and support the creation of market discipline. The regulation contains the Indonesian Banking Accounting Guide and the relationship between Banks, Public Accountants and Bank Indonesia.
23	3/23/PBI/2001	13-12-2001	LN Thn 2001 No.151 TLN No.4160	Bank Indonesia amended the regulation concerning the Implementation of the Know Your Customer (KYC) Principles. Banks implement of the KYC principles by, among others, establishing the policy and procedure of the KYC principles implementation in the Guideline, taking into account the Standard Guideline stipulated in the circular letter.
24	3/24/PBI/2001	24-12-2001	LN Thn 2001 No.155 TLN No.4163	Bank Indonesia amended the regulation concerning the determination of special surveillance and “frozen” status of rural banks in order to expedite the settlement of troubled Rural Banks as an effort to establish a sound banking industry.
25	3/25/PBI/2001	26-12-2001	LN Thn 2001 No. 156 TLN No.4164	Bank Indonesia issued a regulation concerning the determination on the bank status and the bank transfer to IBRA. With this stipulation, the Bank Indonesia Regulation Number 2/11/PBI/2000 is revoked. Under this regulation, a bank facing a potential financial default should be planced under Bank Indonesia’s intensive supervision.

Appendix E.2

Bank Indonesia Circular Letters in 2001

No.	No. BI Circular Letter	Date	Issues
1	3/1/DPNP	05-01-2001	Change in Interest Rate Margin on Deposit Guarenteed by the Government
2	3/2/BKr	11-01-2001	Credit Extended to Member of Prime Cooperative in an Effort to Re-channell the Installment Payments of BI Liquidity Credit Managed by PT. Permodalan Nasional Madani (Persero)
3	3/3/BKr	16-01-2001	Micro Cedit Project
4	3/4/DASP	23-01-2001	Type and Limits on Document and Schedule of Local Clearing in Jakarta
5	3/5/DPD	31-01-2001	Limitation on Rupiah Transactions and Foreign Currency Credit Extension by Banks
6	3/6/DPM	09-02-2001	Launching of Government Bonds Series VR 0003, VR 0004, VR0007, VR 0009, VR 0011, VR 0013, and VR 0015 Traded in the Secondary Market and the Percentage Increase of Tradable Government Bond Portfolio
7	3/7/DLN	09-03-2001	Revocation of SE No.5/163/ULN Dated 30 January 1973 Concerning the Monthly Report of Foreign Direct Invesment Rupiah Accounts with Banks
8	3/8/DPNP	16-03-2001	Commercial Banks
9	3/9/BKr	17-05-2001	Guidance for Small-Scale Business Credit (KUK) extension
10	3/10/DASP	28-05-2001	Clearing Schedule, Settlement date, the Conduct of Local Clearing, Types and Limits on Value Clearing Item or Electronics Financial Data

No.	No. BI Circular Letter	Date	Issues
11	3/11/DLN	07-06-2001	Second Revision of SE BI No.29/10/ULN, 4 June 1996 Concerning the Payment Settlement of Import Transactions
12	3/12/DLN	08-06-2001	Revision of SE BI No.2/20/DLN, 9 October 2000 Concerning the Obligation of Foreign Debt Reporting
13	3/13/DSM	13-06-2001	Report on Foreign Exchange Transaction by Banks
14	3/14/DSM	13-06-2001	Report on Foreign Exchange Transaction by Non Bank Financial Institutions
15	3/15/DPM	05-07-2001	Percentage Increase of Goverment Bond Portfolio Tradable by Recapitalized Commercial Banks
16	3/16/DPBPR	18-07-2001	Requirements and Procedure for Government Guarantee Program on Rural Bank (BPR) Obligations Payment
17	3/17/DPBPR	18-07-2001	Requirements and Guidance for Government Guarantee Program on Rural Bank (BPR) Obligations Payment
18	3/18/DPM	31-07-2001	Launching of Government Bonds Series VR0006, VR0008, VR0010, VR0012, VR0014 and VR0016 to be Traded at the Secondary Market and the Percentage Rise of Tradable Government Bond Portfolio for Recapitalized Commercial Banks
19	3/19/DPNP	14-08-2001	Interest Rate Margin on Deposit Guaranteed by the Government
20	3/20/DASP	31-08-2001	Revision of SE BI No.2/24/DASP, 17 November 2000 Concerning Bank Indonesia Real Time Gross Settlement
21	3/21/DPM	03-09-2001	Revision of SE BI No.2/27/DPM, 13 December 2000 Concerning the Provision of Commercial Bank Intra-day Liquidity Facilities
22	3/22/BKr	16-10-2001	Revision of SE No.3/3/BKr, 16 January 2001 concerning Micro Credit Project
23	3/23/DPNP	30-10-2001	Monthly Commercial Banks Financial Report

No.	No. BI Circular Letter	Date	Issues
24	3/24/DPM	16-11-2001	The Administration of Government Bonds
25	3/25/DASP	28-11-2001	Revision of SE No.1/4/DASP, 29 November 2001 Concerning Approving Other Agent to Perform Clearing Activities in Areas where BI Regional Offices do not Exist
26	3/26/DASP	5-12-2001	Revision SE No.3/10/DASP, 28 May 2001 concerning Clearing Schedule and Value Date of Foreign Exchange Settlement, Local Clearing System, Types and Limits on Value Clearing Item or Electronics Financial Data
27	3/27/DASP	12-12-2001	Value Clearing Item, Clearing Documents and their Printing at the Security Document Printing Company
28	3/28/DASP	12-12-2001	The Outsourcing of Courrier Services and the Use of Clearing Man Identification Card during the Operation of Electronic Automation System
29	3/29/DPNP	13-12-2001	Standard Procedure in Implementing the “Know Your Customer” Principles
30	3/30/DPNP	14-12-2001	Banks Monthly/Quarterly Published Financial Reports and Other Reports to be Submitted to Bank Indonesia
31	3/31/DPNP	14-12-2001	Banks’ Annual Financial Reports and Other Reports to be Submitted to Bank Indonesia
32	3/32/DPNP	14-12-2001	Relation between Banks, Public Accountant and Bank Indonesia
33	3/33/DPNP	14-12-2001	The Implementation of Indonesia’s Banks Accounting Standard

Appendix E.3

Regulations and Important Policies in Economic and Finance in 2001

Date	Regulation/Policy	Number
2001		
January		
4	Regulation regarding export quota on textile and textile product	Ministry of Industry and Trade Decree No.01/MPP/Kep/1/2001
18	To boost the economic cooperation among sub regional territories with those in the neighboring countries, the Government established a Sub Regional Economy Cooperation Team.	Presidential Decree No.13, 2001
29	Due to the organization and institution structural change in the Cabinet in the period of 1999-2004, the Government adjusted the membership formation of the National Team on Multilateral Trade Negotiation within the World Trade Organization framework.	Presidential Decree No.18, 2001
31	The Stock Market Supervisory Agent issued a regulation concerning the suspension on the registered securities company facing crucial incident which causes a significant effect to its business performance and or order, proper and efficient price formation in the stock market. The said crucial incident among others, are (i) the last two Annual Financial Report obtained a disclaimer opinion from registered public accountant (ii) the Company is filed by its creditors and (iii) the company is filling a Debt Payment Obligation Postponement proposal (PKPU).	Circular Letter PT Bursa Efek Jakarta No.SE-002/BEJ/012001

Date	Regulation/Policy	Number
February		
7	The Government issued a regulation concerning income tax on interest earned from time/saving deposits and SBI holdings.	Finance Minister Decree No.51/KMK.04/2001
9	The Government issued a regulation concerning tax on export of palm oil, CPO, and its derivative products.	Finance Minister Decree No.66/KMK.17/2001
	The Government issued a regulation concerning the article 21 income tax proceeds sharing between the central and local governments.	Finance Minister Decree No.6/KMK.04/2001
14	In order to support the debt restructuring program, the Government enacted a regulation designed to reduce the burden of tax payers, who are joining the corporate debt restructuring program through a special institution designated by the government.	Government Regulation No.7, 2001
	The Government issued a regulation concerning the calculation of interest earnings for tax payers.	Circular Letter of Tax No.SE-03/PJ.33/2001
	The Government issued a regulation concerning the 2001 quotas for listed textile exporters and textile small scale businesses and cooperatives.	Industry and Trade Minister Decree No.51/MPP/Kep/2/2001
19	The Government issued a regulation concerning the crash program on the settlement of 2nd banking claims on government.	Finance Minister Decree No.81/KMK.01/2001
20	The Goverment issued a regulation concerning the authorization granted to the Head of Financial Information	Finance Minister Decree No.88/KMK.03/2001

Date	Regulation/Policy	Number
	and Technology Institute to sign a decree or letter regarding the provision of exports facilities.	
March		
8	The Stock Market Supervisory Agent issued a regulation which restricts transfer of the shares issued prior to the public offer.	Capital Market Decree Kep-06/PM/2001
15	The Government issued a regulation concerning treatment on tax deductible item i.e. food and beverage, compensation and fringe benefit for employee.	Tax General Director Decree No.KEP-213/PJ/2001
16	The Government issued a regulation concerning the procedure to earn tax waiver on interest earned from demand and saving deposits or SBI holdings by individuals or pension fund institution established with Finance Minister's legalization.	Tax General Director Decree No.KEP-217/PJ/2001
22	The Government issued a regulation concerning imports and strategic goods that are exempted from Value Added Tax.	Bank Indonesia Regulation No.3/6/PBI/2001
23	The Stock Market Supervisory Agency issued a regulation on right to reserve shares. If a company has undertaken a public offering or a listed company intends to increase its shares equity, including through a warrant issuance or share conversion, every shareholder of the company shall be given the right to reserve the new share equivalent to the percentage of his ownership.	Capital Market Decree Kep-07/PM/2001 Government Regulation No.12, 2001

Date	Regulation/Policy	Number
27	The Government issued a regulation concerning the application of the tax agreement between the Republic of Indonesia and Venezuela.	Circular Letter of Tax General Director No.SE-02/PJ.10/2001
28	The Government issued a regulation concerning the debt write off.	Circular Letter of Tax General Director No. KEP-238/PJ/2001
	The Government issued a regulation on taxation in Intergrated Economic Zone (Kapet).	Circular Letter of Tax General Director No.KEP-229/PJ/2001
29	The Government issued a regulation on domestic retail price of fuels.	Presidential Decree No.45, 2001
April		
11	The Government issued a regulation concerning the policies to improve banking soundness and corporate debt restructuring based on the Financial Sector Policy Comittee decision on April 11, 2001.	Financial Sector Commitee Decree No.Kep-01/K.KKSK/04/ 2001
16	The Government issued a regulation on tax reduction on imports of raw material, additive materials, and parts components of machines and rotating motor assemblies.	Finance Minister Decree No.190/KMK.01/2001
30	The Government issued a regulation on the Value Added Tax of imported goods waived from import duty.	Finance Minister Decree No.231/KMK.03/2001
May		
17	The Government issued a regulation on importing machines and used machinery equipments.	Industry and Trade Minister Decree

Date	Regulation/Policy	Number
18	The government issued the third amendment of the regulation on import duty, additional import duty, value added tax, sales tax on luxury goods and income tax related to the implementation of the grant/foreign loan funded government projects in order to accelerate the economic recovery.	No.172/MPP/Kep/5/2001 Government Regulation No.25, 2001
28	The Government issued a regulation on the revision of government regulation No.42, 2000 concerning income tax payment on individual traveling overseas.	Government Regulation No.41, 2001
June		
8	The Government issued the fourth amendment of the Government Regulation Number 17 of 1999 concerning the Indonesian Banking Restructuring Agency (IBRA). The regulation stipulates that a bank with the status of Bank Under Rehabilitation but has finished the recovery program shall undergo a surveillance period conducted by IBRA, at least 6 months since the Bank Under Recovery has met the requirements before being transferred back to Bank Indonesia.	Government Regulation No.47, 2001
15	The Government issued a regulation on domestic retail fuel prices.	Presidential Decree No.73, 2001
July		
9	The Minister of Finance issued a regulation regarding divestment of government bonds related to temporary equity investment by IBRA.	Finance Minister Decree No. 401/KMK.01/2001
23	The Government issued a regulation on contingency funds to assist regional government who record a marginal surplus after the transfer of personnels, equipments, financing and documents.	Finance Minister Decree No.190/KMK.01/2001

Date	Regulation/Policy	Number
August		
1	The Government issued a regulation on patent and brand names following government ratification on international convention on patent right and brand names.	Law No.14, 2001
6	The Government issued regulation concerning foundation activities. A foundation is allowed to execute activities to support its mission in the areas of social, religion and humanity by establishing a corporation and or by participating in a corporation. A foundation is prohibited to transfer its assets directly or indirectly to its founders, managers, supervisors and employees or any other parties who has interest in the foundation.	Law No.16, 2001
September		
13	The Government issued a regulation concerning the transfer of status, duty, and authority of Finance Minister on IBRA to State Minister on SOE's Affairs.	Government Regulation No.63, 2001
24	The General Directorate of Tax issued a guideline on freezing and confiscating of the tax payer's assets in the bank in tax collection effort. The assets must be frozen before it is confiscated. To have the assets frozen, the Chief of the Tax Service Office or Land and Building Tax Service Office must submit a request letter attached by a copy of "Surat Paksa" (force letter) and the Letter of Instruction to Confiscate. Subsequently, the chief of the bank is obliged to freeze the assets and signs a Legal Report.	Tax General Director Decree No.KEP-627/PJ/2001
27	The Government issued a regulation concerning the export goods waived from import tax or duties, VAT, and luxurious goods sales tax.	Circular Letter of Excise Tax and Duties General Director No.SE-31/BC/2001

Date	Regulation/Policy	Number
October		
24	The Government issued a regulation concerning the establishment of a task force to monitor price and anticipate procurement and distribution of basic needs in conjunction with the religious festivities in 2001/2002.	Industry and Trade Minister Decree No.300/MPP/Kep/10/2001
30	The Government issued a regulation regarding quotas on textile and textile products.	Industry and Trade Minister Decree No.311/MPP/Kep/10/2001
31	Governor of of Metropolitan Jakarta issued a decree concerning the minimum provincial wage Year 2002 for the DKI Jakarta Province of Rp591.266,- per month.	Jakarta's Governor Decree No.3052, 2001
November		
14	The Government set up the 2002 State Budget which is expected to record a deficit and will be financed by deficit spending from domestic and foreign sources.	Law No.19, 2001
23	The Government issued a regulation on oil and gas.	Government Regulation No.22, 2001
December		
7	The State sold out its shares in PT Telekomunikasi Indonesia Tbk, PT Socfin Indonesia and PT Wisma Nusantara Internasional.	Government Regulation No.78, 2001 Government Regulation No.79, 2001 Government Regulation No.80, 2001
11	The Government issued a regulation on sound banking policy and corporate debt restructuring based on the decision made	Financial Sector Committee Decree

Date	Regulation/Policy	Number
	by the Financial Sector Policy Committee, on December, 11 2001.	No.Kep-01/K.KKSK/12/2001
12	The Minister of Finance issued a regulation to postpone the implementation of Government Regulation Number 107 of 2000 concerning the Province Loan. It was stipulated that the Provinces can make use of loan as a source to finance the province development by considering its ability to repay the loan. Nevertheless with the new the regulation, any loan agreement is deferred until the end of budget year 2002.	Finance Minister Decree No.625/KMK.01/2001
14	The Government issued a regulation on business field reserved for small scale business. The field are still open for medium-large scale enterprises with compulsion to cooperate with small scale business.	Government Regulation No.127, 2001
19	The government issued a regulation concerning Amandment to Government Regulation No.20,1994 on share ownership in Foreign Direct Investment scheme.	Government Regulation No.83, 2001

Table 1
Gross Domestic Product by Expenditure
(billions of rupiah)

Type of expenditure	1997	1998	1999	2000*	2001**
	Constant 1993 market prices				
Consumption	308,816.9	286,850.6	299,084.5	310,725.2	329,841.7
Private	277,116.1	260,022.7	272,070.2	281,957.4	298,703.6
Government	31,700.8	26,827.9	27,014.3	28,767.8	31,138.1
Gross domestic fixed capital formation	139,725.6	93,604.7	76,572.9	93,360.2	97,057.7
Change in stock	3,341.7	-6,386.9	-9,622.1	-27,232.6	-31,371.6
Exports of goods and services	121,157.9	134,707.2	91,863.6	116,193.6	118,377.0
less Import of goods and services	139,796.1	132,400.7	78,546.4	95,112.1	102,772.7
Gross Domestic Product	**433,246.0**	**376,374.7**	**379,352.5**	**397,934.3**	**411,132.1**
Net factor income from abroad	-15,462.9	-27,965.4	-22,145.1	-25,391.1	-17,399.1
Gross National Product	**417,783.1**	**348,409.5**	**357,207.4**	**372,543.2**	**393,733.0**
less Net Indirect tax	26,100.1	1,858.9	6,181.9	-11,687.3	8,815.8
less Depreciation	21,662.4	18,818.8	18,967.6	19,896.7	20,556.6
National Income	**370,020.6**	**327,731.8**	**332,057.9**	**364,333.7**	**364,360.6**
	Current market prices				
Consumption	430,122.7	702,239.5	885,814.6	958,776.8	1,110,103.0
Private	387,170.7	647,823.6	813,183.3	867,997.1	999,266.3
Government	42,952.0	54,415.9	72,631.3	90,779.7	110,836.7
Gross domestic fixed capital formation	177,686.1	243,043.4	221,472.3	268,669.4	310,908.7
Change in stock	21,615.1	-82,716.1	-96,461.4	-81,384.6	-56,820.0
Exports of goods and services	174,871.3	506,244.8	390,560.1	542,992.4	612,482.2
less Imports of goods and services	176,599.8	413,058.1	301,654.0	407,036.4	485,699.7
Gross Domestic Product	**627,695.4**	**955,753.5**	**1,099,731.6**	**1,282,017.6**	**1,490,974.2**
Net factor income from abroad	-18,355.0	-53,893.7	-83,764.2	-92,161.8	-58,079.0
Gross National Product	**609,340.4**	**901,859.8**	**1,015,967.4**	**1,189,855.8**	**1,432,895.2**
less Net Indirec tax	37,828.7	6,480.5	17,950.1	-37,820.3	31,425.7
less Depreciation	31,384.8	47,787.7	54,986.6	64,100.9	74,548.7
National income	**540,126.9**	**847,591.6**	**943,030.7**	**1,163,575.2**	**1,326,920.8**
Memorandum items:					
Per capita Gross Domestic Product 1)					
in thousands of rupiah	3,205.5	4,814.7	5,489.7	6,301.2	
in dollars	1,118.3	491.1	696.5	777.3	
Per capita Gross National Product 1)					
in thousands of rupiah	3,111.8	4,543.2	5,071.5	5,848.2	
in dollars	1,085.6	463.4	643.5	721.4	
Per capita National Income 1)					
in thousands of rupiah	2,758.3	4,269.8	4,707.5	5,719.1	
in dollars	962.3	435.5	597.3	705.4	

1) At Market Price
Source : BPS-Statistics Indonesia

Table 2
Gross Domestic Product by Sector
(billions of rupiah)

Sector	Constant 1993 market prices					Current market prices				
	1997	1998	1999	2000*	2001**	1997	1998	1999	2000*	2001**
Agriculture, livestock, forestry, and fishery	**64,468.0**	**63,609.5**	**64,985.3**	**66,088.3**	**66,503.8**	**101,009.4**	**172,827.6**	**215,686.7**	**218,301.3**	**244,381.0**
Food crops	32,688.4	33,350.4	34,012.4	34,312.2	33,932.1	52,189.4	91,346.0	116,222.5	111,886.5	124,287.7
Non-food crops	10,496.6	10,501.8	10,702.0	10,870.7	11,096.3	16,447.3	33,289.6	35,966.5	33,993.8	38,434.8
Livestock and products	7,483.1	6,439.7	6,836.9	7,051.6	7,322.4	11,688.2	15,743.6	23,761.2	28,087.5	31,575.1
Forestry	7,189.8	6,580.7	6,288.1	6,364.4	6,431.5	6,806.5	11,700.5	13,803.8	14,861.8	15,406.2
Fishery	6,610.1	6,736.9	7,145.8	7,489.4	7,721.6	10,878.0	20,747.9	25,932.8	29,471.7	34,677.2
Mining and quarrying	**38,538.2**	**37,474.0**	**36,865.8**	**38,730.2**	**38,483.3**	**55,561.9**	**120,328.5**	**109,925.4**	**176,639.9**	**202,680.1**
Crude petroleum and natural gas	23,919.8	23,340.1	22,136.8	22,658.3	21,706.9	34,036.7	74,883.7	72,424.9	131,079.4	143,063.4
Mining (excl. oil and gas)	7,645.6	9,678.0	10,357.7	11,459.3	11,966.1	11,192.4	35,459.9	27,696.1	34,031.6	45,558.1
Quarrying	6,972.8	4,455.9	4,371.2	4,612.6	4,810.3	10,332.8	9,984.9	9,804.3	11,528.8	14,058.6
Manufacturing	**107,629.7**	**95,320.6**	**99,058.5**	**105,102.5**	**109,641.3**	**168,178.0**	**238,897.1**	**385,873.9**	**335,339.4**	**389,320.9**
Oil and gas	10,650.3	11,042.2	11,797.2	11,599.9	11,271.5	15,621.9	33,172.4	35,127.6	53,167.6	61,878.0
Petrollum and refinery	5,925.5	6,310.0	6,606.6	6,843.1	6,964.5	8,116.1	15,092.2	16,320.8	22,500.1	28,604.9
LNG	4,724.8	4,732.3	5,190.6	4,756.9	4,307.0	7,505.8	18,080.2	18,806.8	30,667.4	33,273.1
Non-oil and gas	96,979.4	84,278.4	87,261.3	93,502.6	98,369.8	152,556.1	205,724.7	250,746.3	282,171.8	327,443.0
Electricity, gas, and water supply	**5,479.9**	**5,646.1**	**6,112.9**	**6,649.5**	**7,210.0**	**7,832.4**	**11,283.1**	**13,429.0**	**15,072.4**	**17,285.6**
Construction	**35,346.4**	**22,465.3**	**22,035.6**	**23,246.9**	**24,168.0**	**46,678.8**	**61,761.6**	**67,616.2**	**76,090.8**	**84,045.3**
Trade, hotels, and restaurants	**73,523.8**	**60,130.7**	**60,093.7**	**63,448.8**	**66,691.8**	**99,581.9**	**146,740.1**	**175,835.4**	**194,910.1**	**239,959.2**
Wholesale and retail trade	58,842.3	47,845.9	47,574.5	50,284.3	52,859.0	77,543.3	116,688.5	140,588.7	155,184.4	193,692.6
Hotels and restaurants	14,681.6	12,284.8	12,519.2	13,164.5	13,832.7	22,038.6	30,051.6	35,246.7	39,725.7	46,266.6
Transportation and Communication	**31,782.5**	**26,975.1**	**26,772.1**	**29,284.0**	**31,483.0**	**38,530.9**	**51,937.2**	**55,189.6**	**64,550.1**	**79,824.8**
Transportation	25,609.1	20,503.8	19,737.6	21,430.5	22,746.9	31,497.6	41,837.2	42,735.7	49,336.7	62,274.4
Comminication	6,173.4	6,471.3	7,034.5	7,853.5	8,736.1	7,033.3	10,100.0	12,453.9	15,213.4	17,550.4
Financial, rental, and business services	**38,543.0**	**28,278.7**	**26,244.6**	**27,382.7**	**28,201.1**	**54,360.3**	**69,891.7**	**71,220.2**	**79,476.8**	**92,459.4**
Banks 1)	19,956.0	13,173.0	11,861.7	12,429.5	12,899.0	25,205.2	31,710.2	31,088.6	35,404.8	42,234.2
Rental and business services	18,587.0	15,105.7	14,382.8	14,953.1	15,302.2	29,155.1	38,181.5	40,131.6	44,072.1	50,225.2
Services	**37,934.5**	**36,475.0**	**37,184.0**	**38,001.5**	**38,749.9**	**55,962.0**	**82,102.5**	**104,955.3**	**121,636.9**	**141,017.8**
Public administration	23,616.5	21,887.5	22,250.6	22,555.1	22,795.4	32,127.9	40,641.0	59,745.0	69,460.2	81,850.9
Private	14,318.0	14,587.5	14,933.4	15,446.4	15,954.5	23,834.1	41,445.8	48,210.3	52,176.7	59,166.9
Gross Domestic Product	**433,245.9**	**376,374.9**	**379,352.5**	**397,934.3**	**411,132.1**	**627,695.6**	**989,611.6**	**1,099,731.6**	**1,282,017.6**	**1,490,974.2**
Non-oil and gas	**398,675.8**	**341,992.5**	**345,418.5**	**363,676.1**	**378,153.8**	**578,037.0**	**881,555.5**	**992,179.1**	**1,097,770.6**	**1,286,032.8**
Oil and gas	**34,570.1**	**34,382.4**	**33,934.0**	**34,258.2**	**32,978.3**	**49,658.6**	**108,056.1**	**107,552.5**	**184,247.0**	**204,941.4**

1) Including non-bank financial institutions and financial supporting services.

Source : BPS-Statistics Indonesia

Table 3
Terms of Trade Effect on Gross domestic Product
(billions of rupiah)

I t e m	1997	1998	1999	2000*	2001**
1. Exports of goods and services at current market prices	174,871.3	506,244.8	390,560.1	542,992.4	612,482.2
2. Exports of goods and services at constant market prices	121,157.9	134,707.2	91,863.6	116,193.6	118,377.0
3. Export deflator (1:2) x 100)	144.3	375.8	425.2	467.3	517.4
4. Imports of goods and services at current market prices	176,599.8	413,058.1	301,654.0	407,036.4	485,699.7
5. Imports of goods and services at constant market prices	139,796.1	132,400.7	78,546.4	95,112.1	102,772.7
6. Import deflator (4:5) x 100)	126.3	312.0	384.0	428.0	472.6
7. Terms of trade index (3:6) x 100)	114.3	120.5	110.7	109.2	109.5
8. Changes in terms of trade index (%)	7.89	5.43	-8.10	-1.36	0.26
9. Real Import capacity of export (1:6) x 100)	138,427.8	162,270.6	101,696.3	126,880.9	129,599.5
10. Terms of trade effect (9 - 2)	17,269.9	27,563.4	9,832.7	10,687.3	11,222.5
11. Changes in terms of trade effect (%)	160.33	59.60	-64.33	8.69	5.01
12. GDP at constant 1993 market prices	433,246.0	376,374.7	379,352.5	397,934.3	411,132.1
13. Changes in GDP at constant 1993 market prices (%)	4.70	-13.13	0.79	4.90	3.32
14. Gross Domesti Income (10 - 12)	-415,976.1	-348,811.3	-369,519.8	-387,247.0	-399,909.6
15. Changes in Gross Domestic Income (%)	2.16	-16.15	5.94	4.80	3.27

Source : BPS-Statistics Indonesia (processed)

Table 4
Selected Agricultural Products
(thousands of tonnes)

Product	1997	1998	1999	2000	2001
Food crops					
Paddy	49,377.1	49,236.7	50,866.4	51,898.9	50,096.5 [1]
Corn	8,770.9	10,169.4	9,204.0	9,676.9	9,121.4 [1]
Cassava	15,134.0	14,696.2	16,458.5	16,089.0	-
Sweet potatoes	1,847.5	1,935.0	1,665.5	1,827.7	-
Peanuts	688.3	692.4	659.6	736.5	695.8 [1]
Soybeans	1,356.9	1,305.6	1,382.8	1,017.6	862.6 [1]
Mung beans	261.7	306.1	265.1	289.9	286.5 [1]
Estate crops					
Dry Rubber	309.8	330.9	303.7	336.2	138.3 [2]
Palm Oil	2,980.9	3,855.4	4,024.8	4,094.0	1,466.5 [2]
Palm Kernel	708.3	778.3	914.6	930.6	333.3 [2]
Chocolate	59.7	83.0	59.0	59.7	23.6 [2]
Coffee	23.0	24.1	27.3	29.5	2.6 [2]
T e a	99.9	157.2	132.2	127.8	56.2 [2]
Kina	0.1	0.4	0.4	0.6	0.1 [2]
Sugarcane	2,166.7	2,065.3	1,907.5	1,896.3	224.4 [2]
Tobacco	8.1	17.8	28.1	14.8	0.3 [2]
Forestry					
Logs [3]	29,520.3	19,026.9	20,619.9	-	-
Sawn Timber [3]	2,613.5	2,707.2	2,060.2	-	-
Plywood [3]	6,709.8	7,154.7	4,611.9	-	-
Livestock					
Meat	1,555.1	1,228.5	1,193.5	1,445.2	1,450.7 [4]
Eggs	768.6	529.8	640.4	783.3	793.8 [4]
Milk (millions of litres)	423.7	375.4	436.0	495.7	505.0 [4]
Fisherry					
Sea	3,613.0	3,837.0	3,950.0	-	-
Inland	966.5	1,000.0	1,020.0	-	-

1) Projection figures of Quarter III-2001
2) Data up to July 2001
3) Fiscal year, In thousands of cubic matres
4) Projection figures
Sources : - Ministry of Agrculture
- Ministry of Forestry and Plantation
- BPS-Statistics Indonesa

Table 5
Production, Harvested Area, and Production of Food Crops

Description	1997	1998	1999	2000	2001[1)]
Production (thousands of ton)					
Paddy	49,377.1	49,236.7	50,866.4	51,898.9	50,096.5
Corn	8,770.9	10,169.4	9,204.0	9,676.9	9,121.4
Cassava	15,134.0	14,696.2	16,458.5	16,089.0	-
Sweet potatoes	1,847.5	1.935.0	1,665.5	1,827.7	-
Peanuts	688.3	692.4	659.6	736.5	695.8
Soybeans	1,356.9	1,305.6	1,382.8	1,017.6	862.6
Mung beans	261.7	306.1	265.1	289.9	286.5
Harvested area (thousands of hectares)					
Paddy	11,140.6	11,730.3	11,963.2	11,793.5	11,412.0
Corn	3,355.2	3,847.8	3,456.4	3,500.3	3,305.1
Cassava	1,243.4	1,205.4	1,350.0	1,284.0	1,279.9
Sweet potatoes	195.4	202.1	172.2	194.3	167.1
Peanuts	628.1	651.1	625.0	683.6	650.7
Soybeans	1,119.1	1,095.1	1,151.1	824.5	723.0
Mung beans	294.2	339.2	298.1	131.3	319.6
Production (quintal per hectare)					
Paddy	44.3	42.0	42.5	44.0	43.9
Corn	26.1	26.4	26.6	27.6	27.6
Cassava	121.7	121.9	121.9	125.3	-
Sweet potatoes	94.5	95.8	96.7	94.1	-
Peanuts	11.0	10.6	10.6	10.8	10.7
Soybeans	12.1	11.9	12.0	12.3	11.9
Mung beans	8.9	9.0	8.9	22.1	9.0

1)Projection figures of Quarter III 2001

Source : Ministry of Agriculture

Table 6
Selected Mining and Quarrying Products

Product	Units	1997	1998	1999	2000	2001
Oil and gas Mining						
Crude oil [1]	Millions of barrels	576.4	569.2	545.7	507.3	448.7 [2]
LNG	Thousands of ton	27,136.7	27,179.9	29,812.4	27,203.0	10,727.2 [3]
LPG	Thousands of ton	2,805.1	2,312.2	2,249.8	2,047.3	892.2 [3]
Non oil and gas Mining						
C o a l	Thousands of ton	52,074.3	60,320.8	69,357.6	76,820.2	52,406.8 [4]
Nickel	Thousands of ton	2,829.9	2,734.0	3,245.3	3,349.3	2,079.5 [4]
Copper [1]	Thousands of ton	1,840.7	2,640.0	2,645.2	3,193.5	2,241.8 [4]
T i n	Thousands of ton	55.2	54.0	47.8	50.2	48.7 [4]
Bauxite	Thousands of ton	808.7	1,055.6	1,142.5	1,175.4	926.8 [4]
Iron sand	Thousands of ton	487.4	561.0	562.3	538.9	341.9 [4]
Gold	Thousands of kilograms	90.0	124.0	129.0	117.6	99.3 [4]
Silver	Thousands of kilograms	270.4	350.0	292.3	334.6	154.6 [4]

1) Including Condenser
2) Data up to November 2001
3) Data up to May 2001
4) Data up to September 2001
Sources : - Ministry of Miining and Energy
- Directorate General of Mining and Energy
- BPS-Statistics Indonesia

Table 7
PLN Electric Power Distributions
(millions of KWH)[1]

Y e a r	1997	1998	1999	2000	2001[1]
Total	**64,314.5**	**64,383.3**	**71,337.7**	**79,050.3**	**69,964.5**
Social	1,396.3	1,425.8	1,488.7	1,667.1	1,508.0
Household	22,642.4	24,391.0	26,859.2	30,506.0	27,381.8
Business	8,660.4	8,507.5	9,332.2	10.224.4	9,002.1
Industry	29,358.1	27,779.1	31,338.5	33,994.4	29,876.3
Public	2,257.3	2,280.0	1,341.6	2,096.7	1,990.9
Multipurpose	-	-	977.3	561.7	205.4

1) Data up to October 2001
Source : State Electricity Corporation (PLN)

Table 8
Regional Daily Minimum Wage by Province
(rupiah)

Province	1997	1998	1999	2000	2001
Aceh	4,270	4,900	5,700	8,833	10,000
North Sumatera	5,030	5,800	7,000	8,467	11,350
West Sumatera	3,970	4,567	5,333	6,667	8,333
Riau	5,050	5,800	7,267	10,000	14,050
Batam	7,830	9,000	9,667	14,167	17,000
Jambi	3,980	4,583	5,000	5,767	8,167
South Sumatera	4,250	5,183	5,850	6,533	8,500
Bengkulu	4,250	4,883	5,000	5,777	8,000
Lampung	4,200	4,833	5,333	6,400	8,000
Jakarta	5,750	6,617	7,700	11,475	14,208
West Java	5,120	5,892	6,958	7,667	8,167
Central Java	3,770	4,333	5,100	6,167	8,167
Yogyakarta	3,550	4,083	4,333	6,483	7,917
East Java	4,150	4,767	5,683	0	8,355
Bali	4,720	5,417	5,883	6,343	10,325
West Nusa Tenggara	3,600	4,133	4,833	6,000	8,000
East Nusa Tenggara	3,550	4,083	4,767	6,133	9,167
East Timor	4,600	5,283	6,100	0	n,a,
West Kalimantan	4,220	4,850	5,833	7,600	10,150
Central Kalimantan	4,600	5,283	6,500	9,500	12,067
South Kalimantan	4,170	4,800	5,533	6,667	9,833
East Kalimantan	5,100	5,867	6,467	7,767	10,000
Sulawesi	3,930	4,517	5,167	6,200	12,400
Sulawesi	3,550	4,083	5,000	6,767	8,167
Sulawesi	3,750	4,317	4,933	6,667	10,000
Sulawesi	4,030	4,633	5,333	7,000	9,167
Maluku	4,530	5,217	6,000	6,000	7,667
Irian Jaya	5,670	6,517	7,500	10,500	13,333
Average [1]	4,347	5,009	5,782	7,053	9,750
Average [2]	4,471	5,151	5,921	7,316	10,018
Changes (%) [3]	10	15	15	22	38

1) Excluding Batam
2) Including Batam
3) Excluding Batam
Source : Ministry of Manpower and Transmigration (processed)

Table 9
Approved Domestic Investment Projects by Sector
(billions of rupiah)

Sector	1997	1998	1999	2000	2001 2)	Total 1) 1968 to July 2000 Value a)	Project b)
Agriculture, Forestry, and Fishery	**14,807.7**	**5,315.1**	**2,408.3**	**1,578.7**	**1,331.0**	**88,020.7**	**1,711**
Agriculture	13,737.5	4,757.9	1,614.8	1,408.3	731.0	70,944.4	1,094
Forestry	165.5	542.9	749.3	35.0	445.9	6,608.7	301
Fishery	904.7	14.3	44.2	135.4	154.1	10,467.6	316
Mining	**126.3**	**116.3**	**174.0**	**36.4**	**1,198.2**	**5,974.4**	**172**
Manufacturing	**79,334.3**	**44,908.0**	**46,747.5**	**81,976.1**	**41,609.1**	**580,991.0**	**6,561**
Food	13,048.6	6,711.8	12,729.9	8,547.6	8,957.0	153,704.9	990
Textile	6,831.3	1,137.6	2,561.5	2,386.4	2,217.4	56,017.6	1,358
Wood	762.2	1,971.9	1,229.0	168.8	546.5	19,342.0	816
Paper	11,841.9	12,754.1	20,244.1	8,174.2	4,771.0	101,120.1	423
Chemical and pharmaceutical	22,497.2	15,583.2	2,480.9	56,435.9	22,236.2	122,656.5	1,350
Non-metal mineral	11,638.7	3,469.0	70.4	3,523.0	596.5	63,561.2	436
Basic metal	8,021.5	1,786.3	6,354.2	274.3	287.0	33,437.8	211
Metal products	4,683.9	960.9	1,070.7	2,465.9	0.0	30,024.3	873
Others	9.0	533.2	6.8	0.0	1,997.5	1,126.6	104
Construction	**877.0**	**1,992.0**	**395.1**	**843.6**	**2,006.8**	**9,569.2**	**170**
Hotel	**2,587.9**	**1,150.4**	**1,379.9**	**153.5**	**2,459.0**	**32,676.8**	**717**
Tranportation	**4,649.4**	**3,260.5**	**225.3**	**1,801.6**	**1,416.4**	**26,151.8**	**1,004**
Real estate and office buildings	**4,300.5**	**1,547.5**	**995.5**	**292.6**	**4,540.9**	**37,540.0**	**369**
Other services	**13,189.8**	**2,459.5**	**1,226.3**	**1,611.9**	**1,635.1**	**28,715.4**	**387**
Total	**119,872.9**	**60,749.3**	**53,551.9**	**88,294.4**	**56,196.5**	**809,639.3**	**11,091**

1) a. Investment cumulative data from 1968 is the sum of new investments, including extensions, status shiftings, changes, and combinations less cancellation
b. Project cumulative data from 1968 is the sum of new projects, including status shiftings and combinations less cancellation
Investment and project cumulative data from 1968 is only available up to July 2000
2) at the end of December 2001
Source : Investment Coordination Board (BKPM)

Table 10
Approved Distribution of Domestic Investment Projects by Province
(billions of rupiah)

Province	1997	1998	1999	2000	2001[2]	Total[1] 1968 to July 2000 Value [a]	Project [b]
Java and Madura	**63,680.8**	**18,871.5**	**22,126.8**	**17,314.0**	**20,272.4**	**401,423.9**	**7,419**
Jakarta	8,553.5	4,289.7	1,260.5	3,521.8	7,845.4	71,339.3	1,841
West Java	37,423.5	8,117.1	18,393.9	9,742.2	7,024.7 [3]	221,414.4	3,434
Central Java	5,764.2	2,574.9	849.6	1,019.5	2,174.3	36,884.6	758
Yogyakarta	235.6	6.0	34.6	119.9	105.5	2,053.4	127
East Java	11,704.0	3,883.8	1,588.2	2,910.6	3,122.5	69,732.2	1,259
Sumatera	**33,561.7**	**10,669.4**	**14,746.3**	**35,584.3**	**8,677.3**	**239,389.2**	**1,677**
Aceh	1,114.1	1,297.3	94.2	89.6	64.4	9,435.6	135
North Sumatera	3,395.5	1,101.5	1,079.4	363.8	981.6	15,841.5	356
West Sumatera	522.6	336.8	597.6	575.5	1.0	90,401.7	137
Riau	11,862.4	4,925.1	9,091.5	33,285.1	5,584.5	61,807.6	470
Jambi	9,793.5	1,429.4	3,001.7	882.2	771.5	28,618.3	90
South Sumatera	5,391.4	882.7	149.3	67.7	625.6	19,123.8	251
Bengkulu	630.7	4.0	121.4	22.5	0.0	3,013.6	58
Lampung	851.5	692.6	611.2	297.9	648.7	11,147.1	180
Kalimantan	**13,935.7**	**11,966.6**	**5,359.5**	**4,277.7**	**3,776.9**	**77,561.5**	**845**
West Kalimantan	3,825.9	416.9	222.6	21.1	10.1	20,110.6	253
Central Kalimantan	1,688.0	9,093.4	3,561.4	331.5	164.3	20,243.0	145
South Kalimantan	4,300.1	640.6	410.5	3,064.8	188.4	12,899.4	166
East Kalimantan	4,121.7	1,815.7	1,165.0	860.3	3,414.1	24,308.5	281
Sulawesi	**3,849.9**	**13,022.9**	**1,795.8**	**30,297.3**	**20,191.3**	**39,054.2**	**475**
North Sulawesi	277.8	1,132.4	51.8	1,487.5	2,241.6 [4]	6,062.4	91
Central Sulawesi	725.5	630.7	543.9	262.5	1,067.8	6,389.0	74
South Sulawesi	1,880.0	11,168.7	696.2	28,380.4	16,581.5	22,443.0	268
Southeast Sulawesi	966.6	91.1	503.9	166.9	300.4	4,159.8	42
Nusa Tenggara	**1,222.5**	**1,289.0**	**35.2**	**757.0**	**1,600.6**	**5,237.3**	**131**
West Nusa Tenggara	352.5	638.5	14.9	755.5	519.7	2,821.1	78
East Nusa Tenggara	870.0	650.5	20.3	1.5	1,080.9	2,416.2	53
Bali	**850.7**	**804.6**	**1,002.7**	**21.6**	**540.2**	**10,979.2**	**316**
East Timor	**0.0**	**2,802.6**	**47.8**	**0.0**	**0.0**	**3,359.4**	**8**
Maluku	**1,060.0**	**44.5**	**20.0**	**0.0**	**0.0**	**7,688.7**	**133**
Irian Jaya	**1,711.6**	**1,278.7**	**8,416.0**	**42.5**	**1,137.8**	**24,945.9**	**87**
Total	**119,872.9**	**60,749.8**	**53,550.1**	**88,294.4**	**56,196.5**	**809,639.3**	**11,091**

1) a. Investment cumulative data from 1968 is the sum of new investments, including extensions, status shiftings, changes, and combinations less cancellation
b. Project cumulative data from 1968 is the sum of new projects, including status shiftings and combinations less cancellation
Investment and project cumulative data from 1968 is only available up to July 2000
2) At the end of December 2001
3) Including Banten
4) Including Gorontalo
Source : - Investment Coordination Board (BKPM)

Table 11
Approved Foreign Direct Investment Projects by Sector
(millions of $)

Sector	1997	1998	1999	2000	2001 2)	Total 1) 1967 to July 2000 Value a)	Total 1) 1967 to July 2000 Project b)
Agriculture, forestry, and fishery	**463.7**	**998.2**	**482.4**	**443.5**	**387.3**	**8,063.6**	**380**
Agriculture	436.6	965.2	412.7	388.9	281.3	6,686.6	240
Forestry	0.0	0.0	0.0	5.0	100.5	653.1	28
Fishery	27.1	33.0	69.7	49.6	5.5	723.9	112
Mining	**1.6**	**0.3**	**14.2**	**1.1**	**112.4**	**9,925.3**	**207**
Manufacturing	**23,017.3**	**8,388.2**	**6,929.2**	**10,633.7**	**5,097.7**	**146,967.7**	**4,376**
Food	572.8	342.0	680.9	701.3	278.8	7,276.6	352
Textile	372.6	216.9	240.2	400.3	328.0	7,730.4	800
Wood	69.7	70.8	113.2	157.0	19.9	2,369.2	391
Paper	5,353.3	40.8	1,411.8	88.0	741.2	24,809.9	130
Chemical and pharmaceutical	12,376.4	6,178.8	3,268.2	7,406.4	2,309.7	68,478.9	928
Non- metal mineral	1,457.3	237.1	110.4	9.6	105.0	7,068.8	166
Basic metal	357.0	394.4	501.3	830.7	651.0	9,786.2	136
Metal products	2,331.7	890.5	593.0	1,005.5	0.0	18,801.2	1,337
Others	126.5	16.9	10.2	34.9	664.1	646.5	136
Construction	**306.8**	**197.8**	**153.4**	**125.3**	**47.6**	**2,049.0**	**376**
Hotel	**462.6**	**451.1**	**228.6**	**257.0**	**891.6**	**11,327.4**	**331**
Transportation	**5,900.0**	**79.0**	**102.7**	**1,217.3**	**378.0**	**13,529.6**	**279**
Real estate and office buildings	**1,397.6**	**1,270.9**	**171.1**	**301.5**	**177.4**	**12,697.6**	**221**
Other services	**2,282.9**	**2,177.6**	**2,800.2**	**2,303.4**	**1,887.6**	**23,922.3**	**2,278**
Total	**33,832.5**	**13,563.1**	**10,881.8**	**15,282.8**	**8,979.6**	**228,482.5**	**8,448**

1) a. Investment cumulative data from 1967 is the sum of new investments, including extensions, status shiftings, changes, and combinations less cancellation
b. Project cumulative data from 1967 is the sum of new projects, including status shiftings and combinations less cancellation
Investment and project cumulative data from 1967 is only available up to July 2000
2) At the end of December 2001
Source : - Investment Coordination Board (BKPM)

Table 12
Approved Distribution of Foreign Direct Investment Projects by Province
(millions of $)

Province	1997	1998	1999	2000	2001 2)	Total 1) 1967 to July 2000 Value a)	Project b)
Java and Madura	**20,535.0**	**10,840.4**	**2,635.9**	**10,539.9**	**5,718.9**	**144,536.6**	**6,345**
Jakarta	6,136.1	1,700.1	783.8	3,270.5	1,145.0	34,897.1	2.754
West Java	7,973.3	5,504.1	1,498.2	3,138.0	2,771.9 3)	64,993.2	2.646
Central Java	2,195.7	3,066.7	69.7	3,013.8	116.0	13,837.6	267
Yogyakarta	14.3	6.0	10.5	4.0	10.0	309.9	45
East Java	4,215.6	563.5	273.7	1,113.6	1,676.0	30,498.8	633
Sumatera	**11,163.9**	**1,415.7**	**7,652.6**	**2,945.6**	**2,325.5**	**49,753.1**	**1,061**
Aceh	771.9	6.2	51.8	1,811.1	6.0	2,549.5	44
North Sumatera	3,514.6	229.6	102.7	193.3	82.3	9,978.0	203
West Sumatera	7.1	175.8	344.9	18.5	37.3	1,036.2	52
Riau	6,743.0	537.1	6,956.9	418.0	2,093.9	24,801.8	607
Jambi	0.0	201.9	42.0	252.7	5.6	4,407.8	19
South Sumatera	73.2	129.3	39.7	215.5	44.6	5,147.4	61
Bengkulu	0.0	37.7	18.4	0.2	1.9	258.1	23
Lampung	54.1	98.1	96.2	36.3	53.9	1,574.3	52
Kalimantan	**1,056.1**	**722.7**	**226.8**	**137.0**	**235.0**	**11,513.7**	**267**
West Kalimantan	28.2	251.2	102.0	3.3	21.8	1,225.6	73
Central Kalimantan	6.0	0.4	50.3	74.8	11.8	547.4	55
North Kalimantan	438.7	73.4	30.3	3.1	9.7	3,279.0	49
East Kalimantan	583.2	397.7	44.2	55.8	191.7	6,461.7	90
Sulawesi	**426.1**	**192.7**	**141.8**	**68.5**	**70.8**	**8,916.0**	**170**
North Sulawesi	358.8	157.4	24.1	22.2	1.1	1,117.9	68
Central Sulawesi	5.5	6.9	2.7	1.8	0.5	172.2	21
South Sulawesi	58.3	27.8	12.5	36.5	68.7	7,373.8	60
Southeast Sulawesi	3.5	0.6	102.5	8.0	0.5	252.1	21
Nusa Tenggara	**14.6**	**57.2**	**15.0**	**1,413.5**	**5.7**	**3,936.8**	**77**
West Nusa Tenggara	0.6	34.6	13.6	1,408.5	5.0	3,774.3	59
East Nusa Tenggara	14.0	22.6	1.4	5.0	0.7	162.5	18
Bali	**114.7**	**308.5**	**193.8**	**125.8**	**518.9**	**3,381.7**	**441**
East Timor	**0.0**	**12.4**	**0.0**	**0.0**	**0.0**	**45.2**	**2**
Maluku	**17.8**	**4.9**	**1.7**	**0.1**	**9.3**	**395.5**	**28**
Irian Jaya	**504.4**	**8.6**	**23.2**	**52.4**	**95.5**	**6,003.9**	**57**
Total	**33,832.6**	**13,563.1**	**10,890.8**	**15,282.8**	**8,979.6**	**228,482.5**	**8,448**

1) a. Investment cumulative data from 1967 is the sum of new investments, including extensions, status shiftings, changes, and combinations less cancellation
b. Project cumulative data from 1967 is the sum of new projects, including status shiftings and combinations less cancellation
Investment and project cumulative data from 1967 is only available up to July 2000
2) At the end of December 2001
3) Including Banten
Source : - Investment Coordination Board (BKPM)

Table 13
Approved Foreign Direct Investment Projects by Country of Origin
(millions of $)

Country of Origin	1997	1998	1999	2000	2001 2)	Total 1) 1967 to July 2000 Value a)	Total 1) 1967 to July 2000 Project b)
Europe	**11,740.2**	**5,311.0**	**730.2**	**5,864.8**	**920.4**	**41,250.8**	**1,254**
Netherlands	319.5	411.8	48.7	1,159.2	88.0	6,228.8	267
Belgium	16.5	11.5	9.8	5.7	0.2	367.3	50
United Kingdom	5,473.6	4,745.3	507.0	3,574.0	722.6	21,163.5	390
Germany	4,467.8	71.0	87.1	958.6	42.7	8,329.1	192
France	456.6	7.5	22.7	64.4	14.4	1,219.8	107
Switzerland	73.5	35.1	42.1	42.2	11.7	1,083.1	74
Others	932.7	28.8	12.8	60.7	40.8	2,859.2	174
America	**1,112.8**	**699.6**	**144.2**	**254.3**	**81.3**	**11,642.4**	**550**
United States	1,017.7	568.3	136.7	243.1	72.6	10,449.2	397
Canada	6.2	8.1	3.2	3.6	8.4	156.7	109
Others	88.9	123.2	4.3	7.6	0.3	1,036.5	44
Asia	**15,169.6**	**4,673.8**	**6,486.1**	**3,824.0**	**6,154.0**	**110,509.6**	**5,103**
Hongkong	251.0	549.1	76.9	106.2	39.4	14,594.4	404
Japan	5,421.3	1,330.7	644.3	1,961.1	759.7	36,586.1	1,179
South Korea	1,409.9	202.4	263.0	688.4	357.2	9,490.0	936
Malaysia	2,289.3	1,060.2	186.1	167.7	2,226.3	7,035.3	366
Philippines	0.0	62.5	4.9	7.4	1.8	165.2	26
Singapore	2,298.6	1,267.4	731.1	535.0	1,129.5	19,190.2	1,094
Taiwan	3,419.4	165.4	1,489.3	131.0	72.1	16,100.7	809
Thailand	19.1	2.8	8.4	6.8	3.0	1,781.8	38
Others	61.0	33.3	3,082.1	220.4	1,565.0	5,565.9	251
Australia	**187.5**	**85.1**	**2,458.5**	**58.6**	**255.2**	**9,501.0**	**456**
Africa	**93.5**	**75.2**	**65.6**	**466.5**	**560.1**	**1,440.1**	**47**
Joint countries	**5,528.9**	**2,718.4**	**1,006.0**	**4,814.6**	**1,008.6**	**54,138.6**	**1,038**
T o t a l	**33,832.5**	**13,563.1**	**10,890.6**	**15,282.8**	**8,979.6**	**228,482.5**	**8,448**

1) a. Investment cumulative data from 1967 is the sum of new investments, including extensions, status shiftings, changes, and combinations less cancellation
b. Project cumulative data from 1967 is the sum of new projects, including status shiftings and combinations less cancellation
Investment and project cumulative data from 1967 is only available up to July 2000
2) At the end of December 2001
Source : - Investment Coordination Board (BKPM)

Table 14
Consumer Price Index

End period[1]	Food-stuffs	Prepared food, beverages, cigaretes and tobacco	Housing	Clothing	Medical care	Education, rekreation and sport	Transpor-tation and Communi-cation	General Index	Change in General Index (%)
1994 [2]	156.97	-	178.57	147.53	161.69	-	-	163.17	9.24
1995	179.14	-	188.93	157.42	173.33	-	-	177.83	8.64
1996	189.99	-	198.00	166.76	190.72	-	-	189.62	6.47
1997	227.88	-	210.36	179.96	206.72	-	-	211.62	11.05
1998	263.22	211.58	159.03	219.71	212.54	161.84	163.70	198.64	1.23
January - March	166.71	142.23	128.61	161.39	155.88	134.74	119.74	142.15	27.11
April - June [3]	196.39	167.92	139.17	195.29	171.97	140.84	150.38	163.89	15.29
July - September	261.00	207.21	155.92	225.22	204.49	162.17	163.18	196.23	19.73
October - December	163.22	211.58	159.03	219.71	212.54	161.84	163.70	198.64	1.23
1999	-	-	-	-	-	-	-	-	**2.01**
January	281.09	213.80	160.62	232.11	214.07	161.40	164.95	204.54	2.97
February	287.60	216.87	162.06	234.23	214.12	161.89	164.29	207.12	1.26
March	281.65	216.34	162.92	234.71	215.80	162.05	169.16	206.75	-0.18
April	275.09	215.52	164.04	233.58	216.57	162.04	169.07	205.34	-0.68
May	271.38	215.20	164.91	231.18	217.60	162.59	170.06	204.76	-0.28
June	268.25	215.16	165.34	228.32	218.22	163.06	170.23	204.07	-0.34
July	258.96	214.87	166.06	224.69	219.48	163.87	169.94	201.93	-1.05
August	248.54	215.33	165.87	226.56	220.98	166.48	169.68	200.05	-0.93
September	239.06	216.26	166.12	229.63	220.00	169.52	169.94	198.68	-0.68
October [4]	237.24	216.13	166.45	232.23	220.06	170.17	171.31	198.79	0.06
November	240.00	216.51	165.93	228.38	219.97	170.42	171.56	199.00	0.25
December	249.54	219.20	166.77	233.21	220.37	170.44	172.20	202.45	1.73
2000	-	-	-	-	-	-	-	-	**9.35**
January	256.85	220.00	167.56	237.47	220.87	170.43	173.68	205.12	1.32
Februay	256.00	220.17	168.34	239.79	221.85	170.23	173.45	205.27	0.07
March	250.16	219.97	169.05	240.09	222.43	171.83	174.01	204.34	-0.45
April	246.16	225.28	171.03	240.50	224.87	173.50	176.83	205.48	0.56
May	246.08	225.07	174.18	242.55	225.76	174.91	181.19	207.21	0.84
June	246.47	227.25	174.87	244.54	226.50	175.41	182.54	208.24	0.50
July	251.39	229.45	176.06	248.54	229.42	178.51	183.37	210.91	1.28
August	246.68	231.43	176.71	247.01	230.43	195.70	184.69	211.99	0.51
September	240.76	232.73	177.93	247.12	236.19	198.02	186.65	211.87	-0.06
October	241.37	237.42	180.60	248.68	238.16	199.24	191.19	214.33	1.16
November	246.96	241.62	182.93	249.95	240.47	199.50	191.78	217.15	1.32
December	259.53	243.49	183.61	256.98	241.46	200.28	194.00	221.37	1.94
2001	-	-	-	-	-	-	-	-	**12.55**
January	258.68	245.87	184.74	259.03	242.26	200.61	193.21	222.10	0.33
February	263.04	247.59	185.96	258.88	244.77	201.38	194.29	224.04	0.87
March	265.51	250.49	188.19	260.70	247.97	202.17	195.00	226.04	0.89
April	262.89	252.77	190.09	264.85	252.17	203.41	196.06	227.07	0.46
May	266.84	255.28	191.63	270.08	254.79	203.89	197.42	229.63	1.13
June	270.43	261.35	194.72	271.94	257.03	204.61	204.14	233.46	1.67
July	274.88	266.46	197.93	272.10	259.74	209.40	218.09	238.52	2.12
August	268.42	267.54	199.69	264.80	260.26	218.08	218.12	237.92	-0.21
September	266.45	269.14	203.04	266.57	260.62	222.74	219.75	239.44	0.64
October	269.53	270.38	203.89	271.77	261.32	223.38	219.99	241.06	0.68
November	282.50	272.38	206.05	274.81	262.26	223.57	220.14	245.18	1.71
Dec ember	290.74	278.75	208.57	277.90	262.99	224.12	221.47	249.15	1.62

1) Figures at the end of period (year/quarter)
2) From April 1998 to March 1998 = 100 with 4 categories, column (1) refers to food; colum (6) refers to miscellanous
3) From January 1996 to December 1996 = 100, CPI was calculated based on survey in 44 cities and comodities were classified into 7 categories
4) Since October 1999, CPI is calculated based on survey in 43 cities (excl. Dili)

Source : Ministry of Manpower and Transmigration

Table 15
Wholesale Price Index[1)]

Group	1997	1998	1999	2000	2001	Changes 2001- 2000 (%)
Agriculture	445	750	410	459	567	24
Mining and quarry	318	396	214	236	275	17
Manufacturing	275	455	268	278	309	11
Imports	260	598	289	316	356	13
Exports	238	592	366	461	669	45
Oil and gas	204	474	355	393	462	18
Non-oil and gas	353	994	370	634	521	-18
General Index	282	568	314	353	403	14

1) Annual figure is the average of monthly index over the year
From 1996 - 1998 using constant 1983 market price (1983=100)
From 1999 - 2001 using constant 1993 market price (1993=100)
Source : BPS-Statistics Indonesia

Table 16
Inflation Rates in 43 Cities
(percent)

City	1997	1998 [1]	1999 [2]	2000	2001
Lhokseumawe	8.44	79.66	6.61	8.73	11.67
Banda Aceh	9.90	79.01	5.57	10.57	16.60
Padang Sidempuan	16.84	85.72	-0.14	3.95	9.84
Sibolga	14.60	85.01	1.65	6.95	8.66
Pematang Siantar	15.14	80.23	-0.54	4.67	13.55
Medan	13.10	83.81	1.68	5.90	15.50
Padang	10.72	87.20	4.23	10.99	9.86
Pekanbaru	11.05	75.86	4.35	10.34	14.65
Batam	17.13	52.89	-0.28	9.00	12.64
Jambi	9.89	72.31	0.49	8.40	10.11
Palembang	13.58	89.18	-1.01	8.49	15.15
Bengkulu	9.21	84.10	0.47	8.21	10.58
Bandar Lampung	9.70	85.22	3.34	10.18	12.94
Jakarta	11.70	74.42	1.77	10.29	11.52
Tasikmalaya	10.44	73.55	1.58	4.57	16.71
Serang/Celegon	12.45	65.43	-0.04	7.03	12.75
Bandung	9.95	72.59	4.29	8.52	11.91
Cirebon	10.74	62.23	4.75	6.52	12.93
Purwokerto	9.38	80.93	0.99	10.02	11.76
Surakarta	9.07	66.38	0.46	7.89	15.58
Semarang	10.88	67.19	1.51	8.73	13.98
Tegal	10.44	67.73	1.11	7.85	11.26
Yogyakarta	10.72	77.46	2.51	7.32	12.56
Jember	9.89	84.95	3.16	10.35	13.92
Kediri	12.75	77.08	-0.64	7.05	15.91
Malang	7.38	93.16	1.49	10.62	12.45
Surabaya	9.11	95.21	0.24	10.46	14.13
Denpasar	9.75	75.11	4.39	9.81	11.52
Mataram	8.66	90.50	0.59	5.19	14.76
Kupang	7.71	62.58	10.65	10.62	12.34
Pontianak	12.29	78.85	4.49	8.34	10.60
Sampit	15.79	75.94	-4.98	11.87	14.69
Palangkaraya	13.03	74.65	-0.13	8.57	13.35
Banjarmasin	12.98	74.43	1.47	7.57	8.36
Balikpapan	13.28	75.10	3.01	10.67	10.82
Samarinda	10.93	68.31	3.69	11.91	10.21
Manado	13.66	74.24	7.41	11.41	13.30
Palu	9.70	95.18	3.58	8.41	18.73
Makasar	8.20	80.86	1.64	9.73	11.77
Kendari	8.42	97.79	1.29	11.25	12.56
Ternate	16.77	72.98	0.38	14.51	13.71
Ambon	7.99	75.82	8.26	8.52	14.12
Jayapura	10.35	61.83	3.49	10.23	14.00
National Inflation	**11.05**	**77.63**	**2.01**	**9.35**	**12.55**

Notes :
1) Calculated based on survey in 44 cities and classified into 7 categories, 1996 = 100 — 2)
2) Calculated based on survey in 43 cities (excl. Dili) and classified into 7 categories, 1996 = 100
Source : BPS-Statistics Indonesia

Table 17
Balance of Payments
(millions of $)

Item	1997	1998	1999	2000	2001*
A. Current Account	**-5,001**	**4,096**	**5,783**	**7,992**	**4,977**
1. Merchandise	**10,074**	**18,428**	**20,644**	**25,042**	**21,647**
a. Export f.o.b	56,297	50,370	51,243	65,407	58,689
- Non-oil and gas	44,576	42,951	40,988	50,341	45,816
- Oil and gas	11,721	7,419	10,255	15,066	12,873
b. Import f.o.b	-46,223	-31,942	-30,599	-40,366	-37,042
- Non-oil and gas	-41,447	-29,087	-26,632	-34,378	-31,448
- Oil and gas	-4,776	-2,855	-3,967	-5,988	-5,594
2. Services (net)	**-15,075**	**-14,332**	**-14,861**	**-17,050**	**-16,670**
- Non-oil and gas	-10,525	-11,420	-11,660	-12,500	-12,361
- Oil and gas	-4,550	-2,911	-3,201	-4,550	-4,309
B. Capital Account	**2,542**	**-3,836**	**-4,571**	**-6,772**	**-8,915**
1. Official capital movement (net)	**2,880**	**10,009**	**5,352**	**3,217**	**-290**
a. Inflows	7,594	13,213	7,932	4,986	3,329
- Program aid	0	1,821	3,870	1,361	458
- Food aid	0	160	273	76	0
- IGGI/CGI	4,538	2,788	2,408	2,420	2,470
- Non-IGGI/CGI 1)	3,056	8,444	1,381	1,130	401
b. Debt repayments 2)	-4,714	-3,204	-2,581	-1,769	-3,619
2. Private capital movement (net)	**-338**	**-13,845**	**-9,923**	**-9,989**	**-8,625**
a. Direct investment (net)	4,677	-355	-2,745	-4,550	-5,912
b. Others (net)	-5,015	-13,491	-7,178	-5,439	-2,713
C. Total (A+B)	**-2,459**	**260**	**1,212**	**1,220**	**-3,938**
D. Errors and Omissions (net)	**-1,651**	**2,084**	**2,080**	**3,822**	**2,560**
E. Monetary Movements 3)	**4,110**	**-2,344**	**-3,292**	**-5,042**	**1,378**

1) Including borrowing from IMF
2) taking into account the rescheduling & payment to IMF
3) Minus (-) : Surplus ; Since 2000 based on International Reserve and Foreign Currency Liquidity (IRFCL) concept, replacing Gross Foreign Assets (GFA) concept.

Table 18
Export Value of Non-oil and gas by Commodity
(millions of $)

Item	1997	1998	1999	2000	2001[1)]
Total Exports	**44,577**	**42,951**	**40,987**	**50,341**	**45,816**
Agriculture	**5,166**	**5,091**	**4,179**	**4,152**	**4,015**
Wood	64	53	86	97	128
Rubber	1,505	1,006	854	883	980
Coffe	583	602	465	327	181
Tea	152	169	102	115	107
Pepper	165	195	183	227	98
Tobacco	124	139	108	80	120
Tapioca	23	21	23	11	13
Animal and animal products	1,789	1,779	1,574	1,622	1,685
- Shrimps	1,047	1,041	886	971	994
Skins	56	72	74	94	101
Others	706	1,056	710	695	601
Mining	**4,353**	**4,703**	**4,130**	**5,566**	**5,113**
Tin	277	260	242	234	222
Copper	1,548	1,792	1,441	2,272	2,265
Nickel	233	165	219	360	292
Aluminum	280	202	138	260	207
Coal	1,638	1,669	1,665	1,635	1,662
Others	377	614	425	805	466
Manufacturing	**35,057**	**33,157**	**32,678**	**40,623**	**36,688**
Textiles & textile products	7,614	7,034	6,291	7,317	7,047
- Garments	4,186	3,769	3,450	4,067	4,038
Handicrafts	1,031	2,089	569	548	581
Wood and wood products	5,704	4,245	4,526	4,495	4,094
- Plywoods	3,482	2,328	2,259	1,996	1,854
Rattan products	204	39	255	296	285
Palm Oil	1,662	888	1,369	1,265	1,076
Copra oil-cake	86	51	47	62	41
Chemical product	1,746	2,098	1,835	2,259	2,338
Metal products	1,140	1,387	1,078	1,217	1,197
Electrical appliances	3,264	2,813	3,365	6,366	6,446
Cement	37	87	143	141	176
Paper	1,957	2,471	2,645	3,046	2,473
Rubber products	406	415	374	440	432
Glass and glassware	272	269	279	349	299
Footwear	2,219	1,583	1,519	1,620	1,533
Plastic products	787	935	860	1,216	1,045
Machinery and mechanical	1,415	1,478	1,853	3,783	2,894
Others	5,515	5,275	5,670	6,205	4,731

1) Projection figures

Table 19
Export Volume of Non-oil and gas by Commodity
(thousands of tonnes)

Item	1997		1998		1999		2000		2001 1)	
	Volume	Share (%)	Volume	Share (%)	Volume	Share (%)	Volume	Share (%)	Volume	Share (%)
Total Exports	**251,845**	**100.0**	**199,771**	**100.0**	**175,610**	**100.0**	**176,535**	**100.0**	**246,148**	**100.0**
Agriculture	**4,731**	**1.9**	**5,936**	**3.0**	**5,395**	**3.1**	**4,649**	**2.6**	**5,329**	2.2
Wood	708	0.3	489	0.2	679	0.4	685	0.4	740	0.3
Rubber	1,483	0.6	1,584	0.8	1,544	0.9	1,410	0.8	1,565	0.6
Coffe	356	0.1	411	0.2	362	0.2	363	0.2	422	0.2
Tea	96	0.0	113	0.1	107	0.1	109	0.1	114	0.0
Pepper	33	0.0	45	0.0	35	0.0	67	0.0	110	0.0
Tobacco	56	0.0	114	0.1	78	0.0	32	0.0	36	0.0
Tapioca	244	0.1	211	0.1	300	0.2	161	0.1	166	0.1
Animal and animal products	704	0.3	949	0.5	819	0.5	664	0.4	632	0.3
- Shrimps	141	0.1	165	0.1	164	0.1	182	0.1	156	0.1
Skins	1	0.0	13	0.0	38	0.0	11	0.0	12	0.0
Others	1,050	0.4	2,007	1.0	1,433	0.8	965	0.5	1,131	0.5
Mining	**217,018**	**86.2**	**154,226**	**77.2**	**116,809**	**66.5**	**125,015**	**70.8**	**179,395**	72.9
Tin	50	0.0	49	0.0	47	0.0	46	0.0	58	0.0
Copper	1,932	0.8	2,946	1.5	2,261	1.3	3,144	1.8	2,860	1.2
Nickel	2,224	0.9	1,409	0.7	2,008	1.1	1,918	1.1	2,138	0.9
Aluminum	1,081	0.4	1,076	0.5	1,125	0.6	1,204	0.7	1,467	0.6
Coal	45,822	18.2	52,411	26.2	53,899	30.7	59,742	33.8	58,149	23.6
Others	165,909	65.9	96,335	48.2	57,469	32.7	58,961	33.4	172,651	70.1
Manufacturing	**30,096**	**12.0**	**39,609**	**19.8**	**49,307**	**28.1**	**46,871**	**26.6**	**61,425**	25.0
Textiles and textile products	1,369	0.5	1,635	0.8	1,525	0.9	1,677	0.9	1,827	0.7
- Garments	318	0.1	414	0.2	333	0.2	351	0.2	370	0.2
Handicraft	183	0.1	223	0.1	196	0.1	205	0.1	202	0.1
Wood and wood products	6,914	2.7	7,302	3.7	6,791	3.9	6,770	3.8	7,327	3.0
- Plywood	5,087	2.0	5,157	2.6	4,302	2.4	3,970	2.2	4,365	1.8
Rattan products	52	0.0	14	0.0	114	0.1	130	0.1	124	0.1
Palm Oil	3,245	1.3	1,700	0.9	3,600	2.0	4,521	2.6	6,107	2.5
Copra oil-cake	1,090	0.4	984	0.5	983	0.6	1,225	0.7	1,927	0.8
Chemical products	4,206	1.7	6,883	3.4	5,378	3.1	5,916	3.4	5,728	2.3
Metal products	1,090	0.4	3,391	1.7	3,191	1.8	1,515	0.9	1,955	0.8
Electrical appliances	356	0.1	381	0.2	437	0.2	692	0.4	715	0.3
Cement	794	0.3	3,736	1.9	7,383	4.2	7,292	4.1	9,808	4.0
Paper	3,768	1.5	5,585	2.8	9,048	5.2	5,048	2.9	5,314	2.2
Rubber products	167	0.1	203	0.1	209	0.1	279	0.2	292	0.1
Glass and glassware	643	0.3	957	0.5	1,555	0.9	960	0.5	962	0.4
Footwear	193	0.1	173	0.1	165	0.1	157	0.1	170	0.1
Plastics products	720	0.3	1,244	0.6	1,045	0.6	1,195	0.7	1,285	0.5
Machinery and mechanical	114	0.0	763	0.4	166	0.1	288	0.2	377	0.2
Others	5,192	2.1	4,435	2.2	7,156	4.1	4,680	2.7	10,446	4.2

1) Projection figures

Table 20
Export Value of Non-oil and gas by Country of Destination
(millions of $)

Continent/Country	1997		1998		1999		2000		2001 [1]	
	Value	Share (%)	Value	Share (%)	Value	Share (%)	Value	Share (%)	Value	Share (%)
Africa	**777**	**1.7**	**904**	**2.1**	**1,032**	**2.5**	**1,157**	**2.3**	**1,110**	**2.4**
America	**8,286**	**18.6**	**7,815**	**18.2**	**7,679**	**18.7**	**9,993**	**19.9**	**9,505**	**20.7**
United States of America	6,701	15.0	6,383	14.9	6,297	15.4	8,463	16.8	8,094	17.7
Latin America	875	2.0	459	1.1	429	1.0	626	1.2	576	1.3
Canada	397	0.9	409	1.0	346	0.8	446	0.9	414	0.9
Others	314	0.7	564	1.3	607	1.5	458	0.9	420	0.9
Asia	**25,350**	**56.9**	**24,831**	**57.8**	**23,573**	**57.5**	**28,579**	**56.8**	**25,535**	**55.7**
ASEAN	**7,723**	**17.3**	**8,723**	**20.3**	**7,982**	**19.5**	**9,748**	**19.4**	**8,622**	**18.8**
Brunei	47	0.1	43	0.1	26	0.1	24	0.0	32	0.1
Malaysia	1,343	3.0	1,358	3.2	1,388	3.4	1,861	3.7	1,710	3.7
Philippines	734	1.6	608	1.4	646	1.6	861	1.7	798	1.7
Singapore	4,913	11.0	5,798	13.5	4,998	12.2	6,073	12.1	5,130	11.2
Thailand	686	1.5	916	2.1	923	2.3	928	1.8	952	2.1
Hong Kong	2,053	4.6	2,037	4.7	1,400	3.4	1,574	3.1	1,288	2.8
India	597	1.3	782	1.8	807	2.0	1,088	2.2	956	2.1
Iraq	19	0.0	45	0.1	63	0.2	95	0.2	106	0.2
Japan	7,015	15.7	5,964	13.9	5,791	14.1	7,844	15.6	7,208	15.7
South Korea	1,297	2.9	1,166	2.7	1,287	3.1	1,710	3.4	1,564	3.4
Myanmar	159	0.4	175	0.4	101	0.2	64	0.1	76	0.2
Pakistan	170	0.4	152	0.4	151	0.4	148	0.3	155	0.3
People's Republic of China	1,387	3.1	1,320	3.1	1,486	3.6	1,828	3.6	1,559	3.4
Saudi Arabia	627	1.4	476	1.1	428	1.0	535	1.1	476	1.0
Taiwan	1,330	3.0	1,288	3.0	1,234	3.0	1,487	3.0	1,358	3.0
Others	2,975	6.7	2,702	6.3	2,846	6.9	2,458	4.9	2,166	4.7
Australia/Oceania	**783**	**1.8**	**910**	**2.1**	**1,058**	**2.6**	**1,080**	**2.1**	**950**	**2.1**
Europe	**9,379**	**21.0**	**8,491**	**19.8**	**7,645**	**18.7**	**9,532**	**18.9**	**8,716**	**19.0**
European Community	**8,408**	**18.9**	**7,474**	**17.4**	**6,744**	**16.5**	**8,774**	**17.4**	**7,785**	**17.0**
Netherlands	1,825	4.1	1,488	3.5	1,464	3.6	1,895	3.8	1,570	3.4
Belgium dan Luxembourg	804	1.8	773	1.8	687	1.7	892	1.8	758	1.7
United Kingdom	1,263	2.8	1,120	2.6	1,175	2.9	1,575	3.1	1,550	3.4
Italy	636	1.4	729	1.7	605	1.5	708	1.4	686	1.5
Germany	1,502	3.4	1,458	3.4	1,217	3.0	1,435	2.9	1,329	2.9
France	527	1.2	545	1.3	506	1.2	730	1.5	627	1.4
Others	1,851	4.2	1,360	3.2	1,090	2.7	1,540	3.1	1,.265	2.8
Former Soviet Union	120	0.3	67	0.2	49	0.1	81	0.2	52	0.1
Other Eastern Europe	196	0.4	310	0.7	232	0.6	243	0.5	251	0.5
Others	656	1.5	640	1.5	621	1.5	433	0.9	629	1.4
T o t a l	**44,576**	**100.0**	**42,951**	**100.0**	**40,987**	**100.0**	**50,341**	**100.0**	**45,816**	**100.0**

1) Projection figures

Table 21
Import Value of Non-oil and gas by Country of origin (FOB)
(millions of $)

Continent/country	1997		1998		1999		2000		2001 1)	
	Value	Share (%)	Value	Share (%)	Value	Share (%)	Value	Share (%)	Value	Share (%)
Africa	**422**	**1.0**	**362**	**1.2**	**449**	**1.7**	**460**	**1.3**	**602**	**1.9**
America	**7,374**	**17.8**	**5,285**	**18.2**	**4,973**	**18.7**	**5,641**	**16.4**	**4,940**	**15.7**
United States of America	4,765	11.5	3,150	10.8	2,541	9.5	4,044	11.8	3,917	12.5
Latin America	733	1.8	420	1.4	507	1.9	670	1.9	454	1.4
Canada	609	1.3	422	1.5	360	1.4	804	2.3	495	1.6
Others	1,267	3.1	1,294	4.4	1,566	5.9	124	0.4	73	0.2
Asia	**20,495**	**49.4**	**14,354**	**49.3**	**13,810**	**51.9**	**19,463**	**56.6**	**17,599**	**56.0**
ASEAN	**3,494**	**8.4**	**2,396**	**8.2**	**2,730**	**10.2**	**4,706**	**13.7**	**4,610**	**14.7**
Brunei	4	0.0	2	0.0	1	0.0	2	0.0	2	0.0
Malaysia	619	1.5	344	1.2	424	1.6	840	2.4	883	2.8
Philippines	108	0.3	71	0.2	48	0.2	147	0.4	123	0.4
Singapore	1,788	4.3	1,195	4.1	1,433	5.4	2,422	7.0	2,359	7.5
Thailand	974	2.3	785	2.7	824	3.1	1,295	3.8	1,243	4.0
Hong Kong	269	0.6	236	0.8	212	0.8	452	1.3	324	1.0
India	630	1.5	256	0.9	231	0.9	582	1.7	595	1.9
Iraq	3	0.0	3	0.0	0.0	0.0	0	0.0	0	0.0
Jepang	7,517	18.1	4,202	14.4	2,541	9.5	6,576	19.1	5,298	16.8
South Korea	1,973	4.8	1,228	4.2	1,064	4.0	2,293	6.7	2,374	7.5
Myanmar	19	0.0	10	0.0	17	0.1	27	0.1	27	0.1
Pakistan	42	0.1	128	0.4	98	0.4	68	0.2	106	0.3
People's Republic of China	1,167	2.8	887	3.0	1,039	3.9	2,238	6.5	2,053	6.5
Saudi Arab	115	0.3	105	0.4	120	0.5	279	0.8	287	0.9
Taiwan	1,360	3.3	882	3.0	695	2.6	1,592	4.6	1,438	4.6
Others	3,907	9.4	4,022	13.8	5,062	19.0	649	1.9	487	1.5
Australia/Oceania	**2,181**	**5.3**	**1,614**	**5.5**	**2,021**	**7.6**	**2,371**	**6.9**	**2,507**	**8.0**
Europe	**10,974**	**26.5**	**7,472**	**25.7**	**5,378**	**20.2**	**6,443**	**18.7**	**5,800**	**18.4**
European Community	**7,686**	**18.5**	**4,938**	**17.0**	**3,027**	**11.4**	**4,871**	**14.2**	**4,604**	**14.6**
Netherlands	474	1.1	316	1.1	314	1.2	566	1.6	433	1.4
Belgium dan Luxembourg	292	0.7	232	0.8	143	0.5	366	1.1	286	0.9
United Kingdom	1,082	2.6	779	2.7	500	1.9	866	2.5	702	2.2
Italy	931	2.2	476	1.6	232	0.9	421	1.2	541	1.7
Germany	2,410	5.8	2,399	8.2	1,232	4.6	1,601	4.7	1,704	5.4
France	1,929	4.7	513	1.8	328	1.2	600	1.7	511	1.6
Others	570	1.4	224	0.8	277	1.0	449	1.3	426	1.4
Former Soviet Union	312	0.8	151	0.5	102	0.4	295	0.9	169	0.5
Other Eastern Europe	124	0.3	68	0.2	44	0.2	60	0.2	65	0.2
Others	2,853	6.9	2,316	8.0	2,204	8.3	1,217	3.5	963	3.1
Total	**41,447**	**100.0**	**29,087**	**100.0**	**26,632**	**100.0**	**34,378**	**100.0**	**31,448**	**100.0**

1) Projection figures

Table 22
Exports of Oil and Gas 1)

Item	1997	1998	1999	2000	2001 1)
Export Value 2)					
Oil and oil products	6,771	4,141	5,680	7,954	7,166
Gas					
- LNG	4,432	3,046	4,207	6,756	5,355
- LPG	518	233	369	356	352
Total	**11,721**	**7,420**	**10,256**	**15,066**	**12,873**
Export Volume					
Oil and oil products (millions of barrel)	362	340	336	291	300
Gas					
- LNG (millions of MMBTU) 3)	1,387	1,384	1,511	1,400	1,336
- LPG (millions of Mton)	2,233	1,620	1,865	1,215	1,251

1) The f.o.b. value classification system changed into H.S (Harmonized Commodity Description and Coding System) so that groups of export items changed.
2) Consists of crude oil and oil products.
3) MMBTU : Million British Thermal Unit

Table 23
Money Supply
(billions of rupiah)

End of period	M1 1) Outstanding	M1 1) Share (%)	Quasi Money 2) Outstanding	Quasi Money 2) Share (%)	M2 3) Outstanding	M2 3) Change (%) Annual	M2 3) Change (%) Quarterly
1997	78,343	22.0	277,300	78.0	355,643	23.2	8.1
1997/1998	98,270	21.8	351,554	78.2	449,824	52.7	26.5
1998	101,197	17.5	476,184	82.5	577,381	62.3	4.9
1998/1999	105,705	17.5	497,620	82.5	603,325	34.1	4.5
1999 4)	124,633	19.3	521,572	80.7	646,205	11.9	-0.9
2000							
March	124,663	19.0	531,788	81.0	656,451	8.8	1.6
June	133,832	19.6	550,503	80.4	684,335	11.2	4.2
September r	135,430	19.7	551,023	80.3	686,453	5.2	0.3
December r	162,186	21.7	584,842	78.3	747,028	15.6	8.8
2001							
January	145,345	19.7	593,386	80.3	738,731	13.5	
February	149,879	19.8	606,019	80.2	755,898	15.7	
March	148,375	19.3	618,437	80.7	766,812	16.8	2.6
April	154,297	19.5	637,930	80.5	792,227	19.0	
May	155,791	19.8	632,529	80.2	788,320	15.3	
June	160,142	20.1	636,298	79.9	796,440	16.4	3.9
July	162,154	21.0	608,981	79.0	771,135	11.8	
August	166,851	21.6	607,186	78.4	774,037	12.9	
September	164,237	21.0	618,867	79.0	783,104	14.1	-1.7
October	169,963	21.0	638,551	79.0	808,514	14.3	
November	171,383	20.9	650,308	79.1	821,691	14.1	
December	177,731	21.1	666,323	78.9	844,054	13.0	7.8

1) Consists of currency and demand deposits.
2) Consists of time and saving deposits in rupiah and foreign currency, and demand deposits in foreign currency held by residents.
3) Consists of narrow money (M1) and quasi money
4) excluding frozen banks data (7 banks since April 1998, 3 banks since August 1998, and 38 banks since March 1999)

Table 24
Changes in Money Supply and its Affecting factors
(billions of rupiah)

Rincian	1997r	1998	1999r	2000r	2001	2001 I	2001 II	2001 III	2001 IV
Money Supply									
M2	67,011	221,738	68,824	100,823	97,026	19,784	29,629	-13,337	60,950
M1	14,254	22,854	23,436	37,553	15,545	-13,811	11,768	4,094	13,494
Currency	5,937	12,970	16,959	14,018	3,971	-12,257	6,087	2,846	7,295
Demand deposits	8,317	9,884	6,477	23,535	11,574	-1,554	5,681	1,248	6,199
Quasi money 1)	52,757	198,884	45,388	63,270	81,481	33,595	17,861	-17,431	47,456
Affecting factors :									
Net foreign assets	17,344	73,692	-12,581	81,637	23,242	37,521	44,969	-89,552	30,304
Net claims on central government	-16,486	17,513	425,287	123,060	9,389	870	-18,679	963	26,235
Net claims on IBRA	-	29,693	-29,693	-	-	-	-	-	-
Claims on business sector	137,062	99,421	-299,689	42,347	34,233	14,348	21,338	-2,996	1,544
Claims on official entities/ state enterprises	5,031	6,389	-8,139	-4,505	3,910	-291	973	-770	3,998
Claims on private enterprises and individuals	132,031	93,032	-291,550	46,852	30,323	14,639	20,365	-2,226	-2,454
Net other items	-70,909	1,419	-14,500	-146,221	30,162	-32,955	-17,999	78,248	2,867

1) Consists of time and saving deposits in rupiah and foreign currency, and demand deposits in foreign currency held by residents.

Table 25
Interest Rates on Time Deposits by Denomination and Group of Banks[1)]
(percent per annum)

Maturity	December 1997		December 1998		December 1999		December 2000		December 2001	
	Rupiah	Foreign Currency	Rupiah	Foreign Currency	Rupiah	Foreign Currency	Rupiah	Foreign Currency	Rupiah	Foreign Currency
State banks										
1-month	19.74	7.31	41.24	13.23	12.52	5.44	12.05	6.37	16.59	4.95
3-month	19.88	7.41	48.69	13.70	13.19	5.45	13.33	6.59	17.47	5.36
6-month	15.66	7.49	35.17	8.14	14.44	7.94	13.42	6.17	16.55	5.67
12-month	15.19	7.81	28.75	12.61	23.14	8.91	12.48	6.24	15.81	5.95
24-month	15.32	7.23	16.01	14.87	18.53	14.87	14.32	10.23	18.06	6.34
Private national banks										
1-month	27.68	8.77	41.88	12.72	12.14	5.34	12.05	6.07	15.83	4.05
3-month	27.76	8.40	50.24	10.64	12.66	5.68	13.20	6.43	16.94	4.90
6-month	19.17	7.81	33.34	10.21	13.55	7.98	13.16	6.23	15.58	5.32
12-month	17.43	7.99	26.16	11.49	17.07	16.63	11.50	11.39	14.74	5.70
24-month	16.79	7.76	22.85	14.91	17.59	8.02	14.22	8.14	17.22	6.27
Regional government banks										
1-month	21.10	6.23	42.05	12.99	12.20	5.09	11.39	4.97	15.04	5.05
3-month	20.62	6.76	45.35	10.99	12.51	6.19	12.92	4.56	15.98	4.71
6-month	14.16	7.15	29.46	10.43	13.46	5.18	12.94	5.13	15.61	5.48
12-month	16.65	7.2	23.91	12.94	16.17	5.67	11.43	5.05	14.99	5.37
24-month	14.58	-	14.03	-	13.73	-	13.44	-	17.42	-
Foreign banks and joint banks										
1-month	17.70	5.19	33.07	4.71	9.46	4.08	9.73	4.61	12.96	1.92
3-month	18.03	5.99	40.84	4.71	9.24	4.03	11.21	4.81	12.35	2.00
6-month	13.99	5.71	44.42	5.15	9.05	4.31	8.13	4.12	11.63	2.58
12-month	13.64	5.92	31.74	5.17	13.46	4.67	8.51	5.09	12.99	3.40
24-month	15.48	3.57	15.57	3.59	11.67	4.00	13.00	6.05	8.72	2.53
Commercial banks										
1-month	25.39	7.97	41.42	12.11	12.24	5.15	11.96	5.94	16.07	4.18
3-month	23.92	7.77	49.23	10.73	12.95	5.24	13.24	6.11	17.24	4.35
6-month	16.96	7.53	36.78	8.22	14.25	7.85	13.31	5.72	16.18	5.12
12-month	15.92	7.73	28.29	11.66	22.35	9.11	12.17	7.86	15.48	5.62
24-month	15.46	6.47	16.61	14.71	18.38	14.63	14.32	9.47	18.05	6.32

1) Weighted average at the end of period

Table 26
Inter-bank Money Market in Jakarta

End of period		Value of transaction (billions of rupiah)	Weighted average interest rate (percent per annum)
1997	January - December	784,368	26.98
1998	January - December r	2,104,924	63.14
1999	January - December	595,362	23.79
2000	January - December	8,915	10.46
1997	January - March	138,121	12.08
	April - June	157,529	13.45
	July - September	210,670	42.70
	October - December	278,048	39.68
1998	January - March	526,347	57.36
	April - June	500,713	66.38
	July - September	625,331	74.13
	October - December	452,533	54.68
1999	January - March	173,045	39.57
	April - June	160,470	29.70
	July - September	127,906	13.44
	October - December	133,941	12.43
2000	January - March	1,712	9.50
	April - June	1,907	10.03
	July - September	2,486	10.89
	October - December	2,810	11.43
2001 1)	January	2,542	11.74
	February	3,286	12.65
	March	3,562	13.75
	January - March	3,130	12.71
	April	3,076	14.32
	May	2,912	14.29
	June	3,324	14.73
	April - June	3,104	14.45
	July	3,240	15.34
	August	2,912	14.29
	September	3,059	15.82
	July - September	3,070	15.15
	October	3,166	15.92
	November	3,070	15.78
	December	3,266	16.09
	October - December	3,167	15.93

1) Daily average figures

Table 27
Discount Rates on Rupiah Certificate of Deposits by Group of Banks [1)]
(percent per annum)

Maturity	1998		1999	2000				2001			
	March	December	December	March	June	September	December	March	June	September	Desember
State banks											
1-month	18.05	43.95	37.96	10.59	10.23	11.48	12.04	13.26	15.33	16.22	16.48
3-month	23.71	55.30	36.94	11.81	10.67	11.86	12.95	13.05	14.99	16.26	17.51
6-month	23.42	32.18	28.13	11.56	11.51	11.55	11.62	11.36	14.84	15.15	14.25
12-month	14.21	23.86	23.60	15.36	13.93	11.68	11.66	12.04	14.89	15.88	16.03
24-month	14.01	12.90	14.22	-	-	-	11.50	13.70	16.30	16.28	16.28
Private national banks											
1-month	29.41	44.26	38.77	11.34	11.20	12.29	12.59	14.20	14.50	16.76	17.28
3-month	30.29	48.62	39.53	11.36	11.09	11.51	11.81	12.93	14.35	15.49	16.81
6-month	22.11	38.35	32.62	10.28	11.74	12.13	13.24	14.16	14.81	15.34	15.77
12-month	15.63	49.89	52.40	16.02	10.44	10.40	12.12	12.73	12.81	17.19	17.62
24-month	17.47	15.93	30.00	-	-	-	-	-	-	-	-
Regional government banks											
1-month	22.49	40.49	31.90	11.52	10.33	12.32	11.26	11.98	13.95	14.69	15.85
3-month	20.85	52.57	35.48	12.62	12.10	13.40	13.88	15.62	15.78	17.24	18.19
6-month	15.71	22.00	26.26	12.00	12.00	12.00	12.00	12.00	12.49	12.50	-
12-month	18.04	21.20	25.21	12.50	12.10	12.08	13.81	13.83	14.60	14.54	13.00
24-month	13.86	14.50	14.50	-	-	-	-	-	-	-	-
Foreign banks and joint banks											
1-month	13.02	58.46	48.41	-	-	9.07	9.43	10.05	10.63	10.93	11.90
3-month	20.41	39.91	34.00	9.54	10.25	9.26	9.70	10.06	11.43	12.43	13.78
6-month	19.08	-	35.50	-	-	7.98	8.28	8.64	8.70	9.00	10.24
12-month	-	-	-	12.00	12.00	7.98	7.90	8.20	8.33	8.38	8.40
24-month	-	-	-	-	-	-	-	-	-	-	-
Commercial banks											
1-month	28.80	45.94	39.57	11.31	11.15	12.13	12.47	14.09	14.60	16.55	16.81
3-month	27.56	49.99	38.68	11.31	11.07	11.49	11.83	12.89	14.40	15.58	16.97
6-month	22.40	35.50	30.89	10.87	11.68	11.91	12.00	12.00	14.81	15.18	14.65
12-month	15.58	41.51	28.77	14.41	12.41	10.97	12.11	12.65	13.97	16.39	16.50
24-month	16.95	14.56	14.53	-	-	-	11.50	13.70	16.30	16.28	16.28

1) Weighted average at the end of period

Table 28
Issuance, Repayment, and Outstanding of Bank Indonesia Certificates (SBIs)
(billions of rupiah)

End of periode	Issuance	Repayment	Outstanding[1)]
January - December 1997	176,452	187,969	7,034
January - December 1998	735,844	700,182	42,765
January - December 1999	711,542	691,408	62,899
January - December 2000	928,944	937,212	59,781
2001			
January	83,318	55,915	87,184
February	84,500	82,504	89,180
March	100,791	121,362	68,609
April	65,798	62,867	71,539
May	91,906	88,874	74,570
June	76,941	74,103	77,408
July	77,083	77,081	77,410
August	96,017	94,933	78,494
September	87,452	94,978	70,967
October	68,023	65,461	73,530
November	89,172	86,925	75,777
December	49,379	69,696	55,460

Note :
SBI was introduced in February 1984. Since July 1988, the selling of SBIs was executed by Stop Out Rate (SOR) system auction
1) Ddaily average

Table 29
Discount Rates on Bank Indonesia Certificates (SBIs)[1)]
(percent per annum)

Period	7-day	14-day	28-day	90-day	180-day	360-day
1997						
March	7.61	8.70	11.07	11.88	-	-
June	7.29	8.50	10.50	11.25	12.00	12.50
September	18.35	20.06	22.00	-	-	-
December	16.00	18.00	20.00	-	-	-
1998						
March	29.24	-	27.75	-	-	-
June	-	52.81	58.00	-	-	-
September	-	-	68.76	-	-	-
December	-	-	38.44	39.00	-	-
1999						
March	-	-	37.84	38.00	-	-
June	-	-	22.05	23.75	-	-
September	-	-	13.02	13.25	-	-
December	-	-	12.51	12.75	-	-
2000						
March	-	-	11.03	11.00	-	-
June	-	-	11.74	11.09	-	-
September	-	-	13.62	13.32	-	-
December	-	-	14.53	14.31	-	-
2001						
January	-	-	14.79	14.79	-	-
February	-	-	14.79	14.84	-	-
March	-	-	15.16	14.94	-	-
April	-	-	15.91	15.80	-	-
May	-	-	16.27	15.80	-	-
June	-	-	16.52	16.28	-	-
July	-	-	16.98	16.96	-	-
August	-	-	17.37	17.03	-	-
September	-	-	17.65	17.56	-	-
October	-	-	17.58	17.61	-	-
November	-	-	17.59	17.62	-	-
December	-	-	17.62	17.63	-	-

1) Weighted average

Table 30
Money Market Securities (SBPUs) Transactions between Bank Indonesia and Banks
(billions of rupiah)

Period	Buying	Repayment	Outstanding
1997			
January - March	15,954	13,455	2,670
April - June	18,937	19,480	2,126
July - September	50,131	52,237	21
October - December	94,934	91,499	3,455
1998			
January - March	257,109	256,474	4,090
April - June	42,929	46,873	146
July - September	24,136	24,057	227
October - December	1,342	550	1,018
1999			
January - March	1,018	1,018	1,018
April - June	0	0	1,018
July - September	0	0	1,018
October - December	644	1,662	0
2000			
January - March	0	0	0
April - June	0	0	0
July - September	0	0	0
October - December	0	0	0
2001			
January	0	0	0
February	112	2	110
March	0	110	0
April	18	18	0
May	4	4	0
June	0	0	0
July	0	0	0
August	0	0	0
September	0	0	0
October	8	8	0
November	0	0	0
December	0	0	0

Table 31
Government Revenues & Expenditures
(billions of rupiah)

Items	1998/1999p	1999/2000p	2000[1]	2001 Budget[2]	2001 Realization[3]	2002 Budget[4]
Government Revenues and Grants	**156,470**	**187,819**	**204,942**	**286,006**	**299,851**	**301,874**
Domestic revenues	**156,409**	**187,819**	**204,942**	**286,006**	**299,842**	**301,874**
Tax Revenues	**102,395**	**125,951**	**115,788**	**185,260**	**184,737**	**219,627**
Domestic taxes	**95,459**	**120,915**	**108,787**	**174,255**	**174,189**	**207,029**
Income tax (PPh)	55,944	72,729	57,079	94,971	92,767	104,497
Non-oil and gas	55,944	59,683	38,427	69,246	69,696	88,815
Oil and gas	-	13,046	18,652	25,725	23,071	15,682
Value added tax (PPN)	27,803	33,087	35,042	53,457	55,841	70,100
Land and building tax (PBB)	3,043	3,504	3,545	5,094	4,800	5,924
Duties on land and building transfer	523	604	927	1,195	1,489	2,205
Excise duties	7,733	10,381	11,302	17,601	17,622	22,353
Other taxes	413	611	892	1,938	1,670	1,950
International trade taxes	**6,936**	**5,036**	**7,002**	**11,005**	**10,548**	**12,599**
Import duties	2,306	4,177	6,652	10,398	9,828	12,249
Export tax	4,630	859	349	607	720	350
Non-tax revenues	**54,014**	**61,868**	**89,154**	**100,746**	**115,105**	**82,247**
Natural Resource Revenues	41,368	45,435	76,017	79,446	86,658	63,195
Oil	25,957	-	51,003	57,857	60,038	44,013
Gas	15,411	-	15,658	17,369	21,647	14,524
Other natural resources [5]	-	-	9,356	4,220	4,974	4,658
Mining	-	-	556	928	1,827	1,340
Forestry	-	-	8,776	3,001	3,001	3,026
Fishery	-	-	24	292	146	292
Profit transfer from SOEs	3,428	5,430	3,868	9,000	10,440	10,351
Other non-tax revenues (PNBP)	9,217	11,002	9,269	12,300	18,007	8,700
Grants [6]	**62**	**-**	**-**	**-**	**10**	**-**
Government Expenditures	**172,669**	**231,879**	**219,935**	**340,326**	**354,578**	**344,009**
Central government expenditures	**146,020**	**201,943**	**187,058**	**258,849**	**272,178**	**246,040**
Routine expenditures	**103,261**	**156,756**	**161,369**	**213,388**	**232,796**	**193,741**
Personnel expenditures	**23,216**	**32,719**	**29,350**	**38,206**	**39,544**	**41,298**
Salaries and pensions	18,657	27,010	24,269	31,915	33,275	34,003
Rice allowances	1,245	1,822	1,524	1,281	1,259	1,412
Food allowances	1,547	2,567	1,800	2,114	2,114	2,832
Other domestic personnel expenditures	1,073	1,294	1,458	1,371	1,831	1,550
Overseas personnel expenditures	695	25	300	1,526	1,066	1,502
Material expenditures	**9,862**	**10,765**	**8,135**	**9,909**	**9,604**	**12,863**
Domestic	8,888	9,784	7,985	8,735	8,735	11,707
Overseas	974	980	150	1,174	869	1,156
Interest payment	**32,864**	**42,910**	**50,086**	**89,570**	**95,527**	**88,500**
Domestic debt	8,385	22,230	31,238	61,174	66,251	59,525
Foreign debt	24,480	20,679	18,848	28,395	29,277	28,975
Subsidies	**34,614**	**65,916**	**62,758**	**66,269**	**81,575**	**41,586**
Fuel	28,607	40,923	53,635	53,774	68,381	30,377
Non-fuel	6,008	24,993	9,123	12,495	13,194	11,209
Other routine expenditures	**2,703**	**4,446**	**11,039**	**9,433**	**6,546**	**9,494**
Development expenditures	**42,759**	**45,187**	**25,689**	**45,461**	**39,382**	**52,299**
Rupiah financing	16,578	20,804	9,370	21,712	19,712	26,469
Project aid	26,181	24,383	16,319	23,749	19,670	25,830
Regional expnditures	**26,650**	**29,936**	**32,878**	**81,477**	**82,400**	**97,969**
Regional balancing funds	**26,650**	**29,936**	**32,878**	**81,477**	**82,400**	**94,532**
Revenue sharing funds	3,703	3,993	4,251	20,259	21,183	24,600
General allocation funds [7]	22,947	25,943	28,626	60,517	60,517	69,114
Special allocation funds	-	-	-	701	701	817
Special autonomy and equalization funds	**-**	**-**	**-**	**-**	**-**	**3,437**

p) PAN figures (audited state budget)
1) Realization, April 1 2000 up to December 31, 2000
2) State budget (revised)
3) State budget (provisional realization)
4) State budget (approved)
5) Implemented since year 2000
6) Grants from USAID and Japan's government
7) up to year 2000, consists of regional routine and development funds
Source : Ministry of Finance

Table 32
Budget Deficit Financing
(billions of rupiah)

Items	1998/1999p	1999/2000p	2000[1]	2001		2002
				Budget[2]	Realization[3]	Budget[4]
I. Domestic financing	**-4,799**	**14,672**	**5,439**	**34,387**	**44,189**	**23,501**
1. Domestic banks (SILPA/SIKPA) [5]	-6,433	-1,941	-13,461	-	7,551	-
2. Non-domestic banks	1,634	16,613	18,900	34,387	36,638	23,501
a. Privatization	1,634	3,727	-	6,500	5,000	3,952
b. Asset recovery	-	12,886	18,900	27,000	30,980	19,549
c. Domestic bonds, net	-	-	-	887	658	-
i. Government bonds	-	-	-	887	658	3,931
ii. Domestic debt/bond amortization	-	-	-	-	-	-3,931
II. Foreign financing, net	**20,998**	**29,388**	**9,554**	**19,933**	**10,538**	**18,634**
1. Gross drawing	51,045	49,584	17,168	40,091	30,284	62,601
Program loan	24,926	25,201	849	16,341	10,624	36,771
Project loan	26,119	24,383	16,319	23,749	19,660	25,830
2. Amortization	-30,047	-20,196	-7,613	-20,158	-19,746	-43,967
Net financing	**16,199**	**44,060**	**14,993**	**54,320**	**54,727**	**42,135**

p) PAN figures (audited state budget)
1) Realization, April 1, 2000 up to December 31, 2000
2) State budget (revised)
3) State budget (provisional realization)
4) State budget (approved)
5) Budget financing excess (SILPA)/Budget financing shortage(SIKPA)
Source: Ministry of Finance

Table 33
Funds Mobilization by Commercial Banks 1)
(billions of rupiah)

End of period	Demand deposits			Time deposits			Saving deposits	Total
	Rupiah	Foreign Currency	Sub-total	Rupiah 2)	Foreign Currency	Sub-total		
1997	53,103	30,125	83,228	125,743	80,652	206,395	67,990	357,613
1997/1998	64,074	44,629	108,703	177,954	94,106	272,060	72,173	452,936
1998	58,067	39,351	97,418	303,016	103,782	406,798	69,308	573,524
1998/1999	60,002	47,244	107,246	303,022	109,778	412,800	79,453	599,499
1999	68,456	47,110	115,566	301,431	85,640	387,071	122,981	625,618
2000								
March	75,847	46,078	121,925	301,087	86,670	387,757	135,801	645,483
June	84,262	49,805	134,067	289,385	87,737	377,122	146,662	657,851
September r	94,575	56,820	151,395	286,844	83,943	370,787	148,665	670,847
December r	104,539	70,969	175,508	296,885	93,658	390,543	154,328	720,379
2001								
January	102,404	59,233	161,637	306,903	91,661	398,564	156,977	717,178
February	105,105	58,972	164,077	318,203	93,518	411,721	155,691	731,489
March	102,113	64,116	166,229	321,209	99,132	420,341	153,383	739,953
April	105,534	72,321	177,855	314,144	114,778	428,922	159,257	766,034
May	106,233	68,997	175,230	313,774	109,728	423,502	160,150	758,882
June	107,089	68,124	175,213	315,200	111,615	426,815	160,825	762,854
July	109,209	57,657	166,866	311,845	92,875	404,720	164,344	735,930
August	110,594	52,642	163,236	318,146	85,412	403,558	167,144	733,938
September	109,021	56,781	165,802	323,337	92,226	415,563	163,278	744,643
October	115,711	62,378	178,089	334,133	99,347	433,480	162,677	774,246
November	112,007	64,003	176,011	340,066	98,628	438,694	166,007	780,712
December	120,541	66,478	187,018	348,257	97,940	446,196	172,613	805,827

1) Including deposits owned by the Central Government and nonresident
2) Including certificates of deposits

Table 34
Commercial Banks' Demand Deposits in Rupiah and Foreign Currency by Group of Banks
(billions of rupiah)

End of periode	State banks			Private national banks			Regional government banks			Foreign banks & joint banks			Total		
	Rupiah rupiah	Foreign currency	Sub-total	Rupiah rupiah	Foreign currency	Sub-total	Rupiah rupiah	Foreign currency	Sub-total	Rupiah rupiah	Foreign currency	Sub-total	Rupiah rupiah	Foreign currency	Sub-total
1997	17,492	7,125	24,617	24,301	12,693	36,994	4,014	7	4,021	7,296	10,300	17,596	53,103	30,125	83,228
1997/1998	20,595	9,638	30,233	28,663	14,812	43,475	2,738	12	2,750	12,078	20,167	32,245	64,074	44,629	108,703
1998	24,751	8,476	33,227	23,151	13,447	36,598	4,895	13	4,908	5,270	17,415	22,685	58,067	39,351	97,418
1998/1999	28,271	11,624	39,895	21,921	14,255	36,176	4,374	12	4,386	5,436	21,353	26,789	60,002	47,244	107,246
1999	25,407	12,483	37,890	26,866	15,792	42,658	7,055	15	7,070	9,128	18,820	27,948	68,456	47,110	115,566
2000															
March	28,859	12,539	41,398	32,432	14,695	47,127	5,412	16	5,428	9,144	18,828	27,972	75,847	46,078	121,925
June	33,858	9,696	43,554	33,056	16,768	49,824	8,123	20	8,143	9,225	23,321	32,546	84,262	49,805	134,067
September [r]	40,390	14,888	55,278	33,638	17,963	51,601	10,277	23	10,300	10,270	23,946	34,216	94,575	56,820	151,395
December [r]	49,205	24,284	73,489	34,123	18,973	53,096	10,806	17	10,823	10,405	27,695	38,100	104,539	70,969	175,508
2001															
January	44,082	14,007	58,089	34,653	18,685	53,338	12,375	19	12,394	11,294	26,522	37,816	102,404	59,233	161,637
February	44,828	14,387	59,214	36,295	18,486	54,781	14,180	16	14,196	9,803	26,083	35,885	105,105	58,972	164,077
March	43,822	12,892	56,714	34,134	20,915	55,049	15,083	23	15,106	9,074	30,286	39,360	102,113	64,116	166,229
April	43,889	15,512	59,401	35,748	24,292	60,040	15,832	20	15,852	10,066	32,497	42,563	105,534	72,321	177,855
May	45,465	12,752	58,217	34,987	24,595	59,582	16,555	13	16,568	9,226	31,637	40,863	106,233	68,997	175,230
June	44,526	12,442	56,968	34,728	25,398	60,126	19,539	15	19,554	8,296	30,269	38,565	107,089	68,124	175,213
July	45,527	10,843	56,370	34,645	20,743	55,388	20,186	13	20,199	8,851	26,058	34,909	109,209	57,657	166,866
August	46,270	9,803	56,073	34,552	19,115	53,667	21,427	16	21,443	8,345	23,708	32,053	110,594	52,642	163,236
September	45,145	10,539	55,684	34,546	20,872	55,418	20,810	15	20,825	8,520	25,355	33,875	109,021	56,781	165,802
October	47,170	12,470	59,639	35,952	22,541	58,493	23,167	21	23,187	9,421	27,347	36,768	115,711	62,378	178,089
November	44,590	11,895	56,486	36,470	23,366	59,835	21,874	14	21,888	9,074	28,728	37,802	112,007	64,003	176,011
December	50,956	14,430	65,386	38,099	24,270	62,369	22,775	21	22,797	8,710	27,756	36,466	120,541	66,478	187,018

Table 35
Commercial Banks' Time Deposits in Rupiah and Foreign Currency by Maturity
(billions of rupiah)

End of period	24-month	12-month	6-month	3-month	1-month[1)]	Others	Total
1997	359	25,377	28,664	34,637	88,987	28,371	206,395
1997/1998	2,140	28,937	27,841	30,101	138,596	44,445	272,060
1998	610	21,039	17,151	50,352	266,585	51,061	406,798
1998/1999	502	15,449	19,414	24,840	307,610	44,984	412,799
1999	436	14,742	35,244	42,125	243,645	50,879	387,071
2000							
March	628	12,992	45,123	55,711	231,854	41,449	387,757
June	666	9,217	42,666	52,589	230,451	41,534	377,123
September	6,836	7,719	35,941	59,614	204,986	55,689	370,785
December	14,061	6,920	23,503	68,877	215,532	61,649	390,542
2001							
January	14,946	7,314	23,175	74,668	221,001	57,460	398,564
February	14,388	7,698	23,864	75,966	231,107	58,698	411,721
March	14,038	7,767	23,174	75,696	236,772	62,894	420,340
April	14,438	7,478	26,038	71,315	242,358	67,295	428,922
May	13,651	8,218	24,358	68,114	241,134	68,028	423,502
June	14,395	9,451	23,644	66,928	249,025	63,371	426,814
July	12,671	9,871	21,279	67,800	232,362	60,735	404,719
August	14,483	10,489	20,054	72,109	224,257	62,165	403,557
September	14,847	10,553	20,258	75,042	231,910	62,953	415,562
October	17,316	12,450	20,131	75,590	239,527	68,465	433,480
November	18,031	13,297	18,624	75,589	240,270	72,883	438,695
December	18,882	13,533	17,903	77,768	242,685	75,425	446,196

1) Including matured time deposits

Table 36
Commercial Bank' Time Deposits in Rupiah by Ownership
(billions of rupiah)

End of period	Residents										Non-residents	Total
	Govern-ment	Official entities	Insurance companies	State enterprises	Private enterprises	Social institutions	Coopera-tives	Indivi-duals	Others	Sub-total		
1997	5,363	1,786	6,323	6,540	26,512	12,784	282	56,856	9,031	125,477	266	125,743
1997/1998	6,124	1,882	6,845	11,470	35,877	13,344	420	94,053	7,500	177,515	439	177,954
1998	8,805	3,626	8,399	18,241	46,408	20,041	768	182,561	13,555	302,404	612	303,016
1998/1999	8,150	3,320	7,963	16,755	47,583	17,970	726	188,258	11,487	302,212	810	303,022
1999 r	11,268	4,713	11,916	20,463	46,883	20,188	953	173,785	10,165	300,334	1,097	301,431
2000												
March r	12,454	3,863	10,844	22,616	48,713	22,329	619	169,245	9,600	300,283	804	301,087
June r	7,595	4,023	12,011	23,603	48,049	19,435	604	162,654	10,598	288,572	813	289,385
September	4,206	4,846	24,420	19,843	41,948	21,207	1,041	162,539	4,579	284,628	2,215	286,843
December r	4,408	5,162	24,412	18,595	39,653	22,864	941	172,917	6,274	295,226	1,659	296,885
2001												
January	5,042	5,018	25,729	19,858	39,550	24,433	1,092	178,014	6,567	305,304	1,599	306,903
February	5,255	5,242	26,725	20,654	40,720	25,962	1,722	185,317	5,620	317,218	985	318,203
March	6,343	5,320	26,722	21,707	40,385	26,143	2,244	187,611	3,758	320,233	976	321,209
April	5,858	5,068	25,712	21,008	39,251	26,974	2,419	183,834	2,704	312,828	1,314	314,142
May	6,383	5,771	24,285	18,742	38,260	28,372	2,484	184,899	3,378	312,574	1,200	313,774
June	6,559	6,017	25,154	16,746	40,117	30,118	1,756	184,916	2,574	313,957	1,243	315,200
July	6,577	5,971	22,520	13,942	40,487	30,823	1,736	185,499	3,145	310,700	1,145	311,845
August	7,364	5,530	24,560	15,741	40,739	29,222	1,429	189,748	2,563	316,896	1,250	318,146
September	7,622	5,783	23,028	14,275	39,665	28,616	1,716	198,439	2,769	321,914	1,424	323,338
October	7,481	4,989	22,679	14,039	47,284	28,083	1,136	203,257	3,209	332,157	1,976	334,133
November	7,545	5,642	23,089	15,782	52,148	28,757	926	201,768	2,866	338,525	1,542	340,066
December	7,729	8,761	23,547	13,331	50,718	28,255	893	208,994	2,586	344,812	3,444	348,257

Table 37
Certificate of Deposits
(billions of rupiah)

End of period	State banks	Non-State banks	T o t al
1997	777	5,894	6,671
1997/1998	493	3,409	3,902
1998	1,792	5,004	6,796
1998/1999	829	2,825	3,654
1999	491	2,156	2,647
2000			
March	279	2,715	2,994
June	245	3,017	3,262
September	360	3,434	3,794
December	410	3,215	3,625
2001			
January	396	3,708	4,104
February	606	4,212	4,818
March	441	3,297	3,739
April	494	3,580	4,073
May	760	3,781	4,541
June	1,574	4,001	5,575
July	1,404	5,681	7,085
August	1,574	3,522	5,097
September	1,945	3,855	5,799
October	1,969	3,753	5,722
November	2,900	3,016	5,916
December	2,719	2,882	5,601

Table 38
Commercial Banks' Saving Deposits by Type of Deposits

End of period	Saving deposits withdrawnable anytime		Saving deposits		Other saving deposits		Total	
	Depositors (thousands)	Outstanding (billions of Rp)	Depositors (thousands)	Outstanding (billions of Rp)	Depositors (thousands)	Outstanding (billions of Rp)	Depositors (thousands)	Outstanding (billions of Rp)
1997	42,872	62,765	274	173	17,295	5,052	60,441	67,990
1997/1998	43,232	66,653	271	220	19,102	5,300	62,605	72,173
1998	46,292	62,506	307	1,908	18,890	4,894	65,489	69,308
1998/1999	45,442	72,328	222	2,047	18,549	5,078	64,213	79,453
1999	66,926	115,945	161	855	17,437	6,181	84,524	122,981
2000								
March	47,607	127,821	196	1,532	17,755	6,448	65,558	135,801
June	49,442	138,732	191	1,065	16,825	6,865	66,458	146,662
September	80,913	146,300	302	1,290	748	1,075	81,963	148,665
December	65,041	152,388	355	755	1,298	1,185	66,694	154,328
2001								
January	65,460	155,231	347	689	941	1,057	66,748	156,977
February	66,518	153,914	360	719	961	1,058	67,838	155,691
March	86,571	151,593	564	984	626	806	87,761	153,383
April	66,733	157,093	715	1,325	715	839	68,163	159,257
May	67,538	157,461	562	1,445	661	1,244	68,761	160,150
June	67,422	157,535	787	1,960	650	1,330	68,859	160,825
July	78,069	160,875	788	2,145	586	1,324	79,443	164,344
August	67,098	163,458	780	2,240	643	1,446	68,521	167,144
September	67,007	161,323	963	1,022	752	933	68,722	163,278
October	67,996	160,669	846	1,094	554	913	69,396	162,676
November	67,669	164,027	645	935	876	1,045	69,190	166,007
December	68,138	170,783	510	995	823	834	69,470	172,613

Table 39
Interest Rates on Rupiah Credits by Group of Banks [1)]
(percent)

End of Periode	State Banks		Regional Government Banks		Private National Banks		Foreign Banks & Joint Banks		Commercial Banks	
	Working Capital	Invesment	Working Capital	Invesment	Working Capital	Invesment	Working Capital	Invesment	Working Capital	Invesment
1997	20.41	16.12	23.04	15.49	28.22	27.31	26.76	25.22	25.40	18.94
1998	29.03	22.35	30.20	15.83	38.70	40.32	42.89	35.53	34.75	26.23
1999	21.61	17.48	21.81	13.43	19.57	20.61	18.28	22.70	20.68	17.80
2000										
March	20.36	16.48	20.23	11.64	17.62	18.28	16.37	16.81	18.93	16.46
June	18.99	15.79	19.42	18.98	17.65	17.85	15.96	15.20	18.14	16.21
September	18.62	16.19	21.58	18.00	17.88	18.00	15.32	14.88	17.99	16.62
December	18.40	16.53	21.11	18.11	17.55	17.59	15.42	15.49	17.65	16.86
2001										
January	18.48	16.37	20.78	18.04	17.86	17.61	15.80	15.73	17.85	16.77
February	18.44	16.43	20.81	18.00	17.77	17.77	15.89	16.07	17.80	16.88
March	18.47	16.31	20.87	18.02	17.84	17.95	16.28	16.30	17.90	16.86
April	18.52	16.16	20.63	18.00	17.88	18.06	17.48	16.43	18.13	16.80
May	18.62	16.21	20.82	18.05	18.13	18.08	17.11	16.73	18.21	16.85
June	18.64	16.41	20.84	18.07	18.28	17.94	18.05	16.69	18.45	17.04
July	18.73	16.17	20.94	18.02	18.47	17.91	18.64	17.22	18.68	16.90
August	18.82	16.26	20.93	17.97	18.83	18.16	18.80	17.86	18.89	17.08
September	18.91	16.44	20.84	17.73	18.96	18.22	19.24	17.98	19.06	17.22
October	19.10	16.61	20.79	17.81	19.10	18.38	19.17	17.90	19.18	17.38
November	19.15	16.83	20.74	17.77	19.15	18.89	19.28	17.98	19.23	17.64
December	19.15	17.11	20.48	17.76	19.16	19.02	19.09	18.55	19.19	17.90

1) Weighted average

Tabel 40
Commercial Banks' Credits in Rupiah and Foreign Currency by Economic Sector[1)]
(billions of rupiah)

Description	1997	1998	1999	2000	2001			
					Mar.	Jun.	Sep.	Dec.
Credit in rupiah	**261,534**	**313,118**	**140,527**	**152,482**	**158,023**	**171,984**	**187,953**	**202,618**
Agriculture	20,340	29,430	21,139	15,028	15,383	16,291	16,004	16,851
Mining	2,769	2,729	879	2,879	3,364	2,651	2,861	3,676
Manufacturing	56,123	85,594	35,561	35,697	35,802	41,752	47,012	50,434
Trade	57,471	59,830	29,687	30,601	30,555	33,827	36,374	38,491
Services	85,598	101,129	26,332	23,784	25,939	26,685	28,615	30,696
Others	39,233	34,406	26,929	44,493	46,980	50,778	57,087	62,470
Credit in foreign currency	**116,600**	**174,308**	**84,606**	**116,518**	**127,352**	**134,349**	**116,467**	**104,976**
Agriculture	5,662	9,878	2,638	4,475	5,629	6,475	5,724	4,012
Mining	2,547	3,180	2,818	3,801	4,323	2,232	1,775	3,764
Manufacturing	55,556	86,074	48,698	71,085	78,072	85,105	75,532	66,091
Trade	24,793	36,534	13,601	13,498	14,508	12,932	10,881	9,959
Services	27,971	37,995	16,829	20,532	22,313	23,828	20,258	18,365
Others	71	647	22	3,127	2,507	3,777	2,297	2,785
Total	**378,134**	**487,426**	**225,133**	**269,000**	**285,375**	**306,333**	**304,420**	**307,594**
Agriculture	26,002	39,308	23,777	19,503	21,012	22,766	21,728	20,863
Mining	5,316	5,909	3,697	6,680	7,687	4,883	4,636	7,440
Manufacturing	111,679	171,668	84,259	106,782	113,874	126,857	122,544	116,525
Trade	82,264	96,364	43,288	44,099	45,063	46,759	47,255	48,450
Services	113,569	139,124	43,161	44,316	48,252	50,513	48,873	49,061
Others	39,304	35,053	26,951	47,620	49,487	54,555	59,384	65,255

1) Excluding inter-bank loans, loans to the Central Government and non-residents, and aid counterpart funds

Table 41
Commercial Banks' Credits in Rupiah and Foreign Currency by Type of Credit and Economic Sector[1)]
(billions of rupiah)

Type/Sector	1997	1998	1999	2000	2001			
					Mar.	Jun.	Sep.	Dec.
Working capital credits	**277,399**	**345,962**	**167,442**	**203,724**	**213,278**	**221,410**	**220,755**	**234,128**
Agriculture	11,373	22,058	12,162	8,693	9,065	9,322	8,498	8,748
Mining	3,995	3,880	2,368	3,796	4,406	1,325	1,202	1,197
Manufacturing	76,585	121,867	61,278	80,572	85,535	89,877	83,957	88,208
Trade	64,336	72,065	36,181	36,318	36,751	37,716	38,625	40,360
Services	81,806	91,039	28,502	26,725	28,034	28,615	29,089	30,359
Others	39,304	35,053	26,951	47,620	49,487	54,555	59,384	65,255
Investment credits	**100,735**	**141,464**	**57,691**	**65,276**	**72,097**	**84,923**	**83,665**	**73,466**
Agriculture	14,629	17,250	11,615	10,810	11,947	13,444	13,230	12,115
Mining	1,321	2,029	1,329	2,884	3,281	3,558	3,434	6,243
Manufacturing	35,094	49,801	22,981	26,210	28,339	36,980	38,587	28,317
Trade	17,928	24,299	7,107	7,781	8,312	9,043	8,630	8,090
Services	31,763	48,085	14,659	17,591	20,218	21,898	19,784	18,701
Others	-	-	-	-	-	-	-	-
T o t a l	**378,134**	**487,426**	**225,133**	**269,000**	**285,375**	**306,333**	**304,420**	**307,594**
Agriculture	26,002	39,308	23,777	19,503	21,012	22,766	21,728	20,863
Mining	5,316	5,909	3,697	6,680	7,687	4,883	4,636	7,440
Manufacturing	111,679	171,668	84,259	106,782	113,874	126,857	122,544	116,525
Trade	82,264	96,364	43,288	44,099	45,063	46,759	47,255	48,450
Services	113,569	139,124	43,161	44,316	48,252	50,513	48,873	49,061
Others	39,304	35,053	26,951	47,620	49,487	54,555	59,384	65,255

1) Excluding inter-bank loans, loans to the Central Government and non-residents, and aid counterpart funds

Table 42
Commercial Banks' Credits in Rupiah and Foreign Currency by Group of Banks and Economic Sector[1)]
(billions of rupiah)

Group/Sector	1997	1998	1999	2000	2001			
					Mar.	Jun.	Sep.	Dec.
1. State banks	**153,266**	**220,747**	**112,288**	**102,061**	**106,542**	**112,726**	**113,577**	**117,104**
Agriculture	14,279	17,012	15,516	11,209	12,082	12,035	11,677	12,034
Mining	1,939	1,989	1,360	2,522	2,995	2,936	2,833	5,554
Manufacturing	46,868	84,510	38,489	34,878	36,652	39,239	40,949	40,099
Trade	32,970	43,601	21,958	16,431	16,597	17,985	17,512	17,973
Services	39,421	55,792	19,945	16,370	17,367	17,249	15,691	15,537
Others	17,789	17,843	15,020	20,651	20,849	23,282	24,915	25,907
2. Private national banks	**168,723**	**193,361**	**56,012**	**82,425**	**87,869**	**98,660**	**104,092**	**101,871**
Agriculture	10,185	20,272	5,740	4,987	5,524	6,865	6,674	6,050
Mining	2,500	2,414	371	863	808	745	720	838
Manufacturing	35,592	45,416	14,421	22,914	24,427	30,876	33,761	28,237
Trade	40,513	40,687	13,307	21,656	22,306	22,144	23,453	23,402
Services	63,716	72,058	15,605	17,500	19,274	21,461	20,859	22,160
Others	16,217	12,514	6,568	14,505	15,530	16,569	18,625	21,185
3. Regional government banks	**7,539**	**6,570**	**6,793**	**10,106**	**11,152**	**12,453**	**14,674**	**15,419**
Agriculture	267	354	853	527	512	498	526	536
Mining	21	19	18	65	71	84	147	188
Manufacturing	429	409	190	249	261	279	284	257
Trade	1,206	1,053	816	1,182	1,329	1,578	1,930	2,108
Services	2,386	1,820	1,376	1,260	1,308	1,262	1,752	1,411
Others	3,230	2,915	3,540	6,823	7,671	8,752	10,035	10,920
4. Foreign banks and joint banks	**48,606**	**66,748**	**50,040**	**74,408**	**79,812**	**82,494**	**72,077**	**73,199**
Agriculture	1,271	1,670	1,668	2,780	2,894	3,368	2,851	2,244
Mining	856	1,487	1,948	3,230	3,813	1,118	936	860
Manufacturing	28,790	41,333	31,159	48,741	52,534	56,463	47,550	47,932
Trade	7,575	11,023	7,207	4,830	4,831	5,052	4,360	4,968
Services	8,046	9,454	6,235	9,186	10,303	10,541	10,571	9,952
Others	2,068	1,781	1,823	5,641	5,437	5,952	5,809	7,243
5. Commercial banks (1 through 4)	**378,134**	**487,426**	**225,133**	**269,000**	**285,375**	**306,333**	**304,420**	**307,594**
Agriculture	26,002	39,308	23,777	19,503	21,012	22,766	21,728	20,863
Mining	5,316	5,909	3,697	6,680	7,687	4,883	4,636	7,440
Manufacturing	111,679	171,668	84,259	106,782	113,874	126,857	122,544	116,525
Trade	82,264	96,364	43,288	44,099	45,063	46,759	47,255	48,450
Services	113,569	139,124	43,161	44,316	48,252	50,513	48,873	49,061
Others	39,304	35,053	26,951	47,620	49,487	54,555	59,384	65,255

1) Excluding inter-bank loans, loans to the Central Government and non-residents, and aid counterpart funds

Table 43
Flow of Banknotes in Bank Indonesia Head Office and Regional Offices
(trillions of rupiah)

Office	1997		1998		1999		2000		2001	
	Inflow	Outlow	Inflow	Outlow	Inflow	Outlow	Inflow	Outlow	Inflow	Outlow
Jakarta	18.7	32.2	24.2	39.9	24.4	47.2	33.2	51.4	34.9	53.7
Bandung	14.1	9.1	17.9	14.7	22.2	17.1	28.0	20.4	37.6	23.7
Semarang	11.8	6.9	14.5	9.3	17.8	13.6	20.2	15.1	25.5	17.4
Surabaya	13.9	13.3	18.8	18.5	23.4	23.9	28.8	28.6	37.9	33.5
Medan	6.9	7.7	9.4	10.3	11.4	12.8	11.5	11.9	15.1	15.3
Padang	4.2	5.6	5.8	8.7	6.5	11.7	7.8	13.1	10.1	14.9
Makassar	4.7	5.4	7.3	8.8	8.7	10.0	10.4	12.4	13.8	14.9
Banjarmasin	3.6	4.9	4.8	7.2	6.1	9.0	7.8	11.2	10.1	13.4
Total	**77.9**	**85.1**	**102.7**	**117.4**	**120.5**	**145.3**	**147.7**	**164.1**	**185.0**	**186.8**

Table 44
Share of Currency Outflow by Denomination in Bank Indonesia Head Office and Regional Offices
(percent)

Office	Rp100,000.00	Rp50,000.00	Rp20,000.00	Rp10,000.00	Rp5,000.00	<= Rp1,000.00	Total
Jakarta	42	38	12	5	2	1	100
Bandung	51	33	11	3	1	1	100
Semarang	50	33	11	4	1	0	100
Surabaya	49	38	7	4	1	1	100
Medan	47	36	10	4	2	1	100
Padang	43	34	13	8	2	1	100
Makassar	44	35	14	4	2	1	100
Banjarmasin	47	34	12	5	2	1	100

Table 45
Flow of Coins in Bank Indonesia Head Office and Regional Offices
(billions of rupiah)

Office	1997		1998		1999		2000		2001	
	Inflow	Outlow	Inflow	Outlow	Inflow	Outlow	Inflow	Outlow	Inflow	Outlow
Jakarta	14.4	79.5	4.4	105.5	2.2	117.7	4.1	184.5	0.1	196.9
Bandung	17.3	8.7	10.8	12.9	11.1	14.8	15.2	21.0	16.5	28.5
Semarang	23.2	7.4	13.9	8.3	12.2	13.2	14.3	14.4	17.0	15.6
Surabaya	2.9	15.9	1.2	32.8	2.2	29.7	1.8	33.5	4.0	44.2
Medan	2.0	7.4	3.3	11.2	1.1	13.1	0.4	14.0	0.7	24.1
Padang	0.7	7.3	0.3	14.1	0.3	9.7	0.3	12.3	0.5	21.8
Makassar	1.0	7.4	0.5	12.6	0.6	11.2	1.1	10.9	0.5	20.8
Banjarmasin	0.7	6.1	0.7	15.5	0.6	11.4	1.4	11.0	0.8	15.6
Total	**62.2**	**139.7**	**35.1**	**212.9**	**30.3**	**220.8**	**38.6**	**301.6**	**40.1**	**367.5**

Tabel 46
World Economic Growth
(percent)

Country	1997	1998	1999r	2000r	2001*
World	**4.1**	**2.6**	**3.6**	**4.7**	**2.4**
Industrial countries	**3.4**	**2.4**	**3.3**	**3.9**	**1.1**
7 major industrial countries	3.2	2.5	3.0	3.5	1.0
United States	4.4	4.4	4.1	4.1	1.0
Japan	1.6	-2.5	0.7	2.2	-0.4
Germany	1.4	2.1	1.8	3.0	0.5
France	2.0	3.2	3.0	3.5	2.1
Italy	1.8	1.5	1.6	2.9	1.8
United Kingdom	3.5	2.6	2.1	2.9	2.3
Canada	4.4	3.3	5.1	4.4	1.4
Others	4.2	2.0	4.9	5.2	1.5
Developing countries	**5.7**	**3.5**	**3.9**	**5.8**	**4.0**
Africa	2.8	3.1	2.5	2.8	3.5
Middle East, Malta and Turkey	5.1	4.1	1.1	5.9	1.8
Latin America	5.4	2.2	0.1	4.1	1.0
Asia	6.5	4.1	5.9	6.7	5.6
NIEs Asia	5.8	-2.3	7.9	8.2	0.4
People's Republic of China	8.8	7.8	7.1	8.0	7.3
Indonesia	4.7	-13.2	0.8	4.8	3.2
Singapore	9.0	0.3	4.5	9.9	-2.9
Malaysia	7.7	-6.7	6.1	8.3	0.3
Thailand	-1.3	-9.4	4.3	4.4	1.5
Philippines	5.2	-0.5	3.4	4.0	2.9
Vietnam	8.2	3.5	4.2	5.5	4.7
Countries in transition 1)	**1.6**	**-0.8**	**3.6**	**6.3**	**4.9**
Central and Eastern Europe	2.1	2.0	2.0	3.8	3.0
Russia	0.9	-4.9	5.4	8.3	5.8
Transcaucasus dan Central Asia	2.6	2.5	4.6	5.3	-

1) Excl. Belarus and Ukraine
Sources: – IMF, *World Economic Outlook*, December 2001
– Bank Indonesia

Table 47
World Inflation Rate
(percent)

Country	1997	1998	1999^r	2000^r	2001 *
World	**4.2**	**2.5**	**3.0**	**-**	**-**
Industrial countries	**2.1**	**1.5**	**1.4**	**2.3**	**2.3**
7 major industrial countries	2.0	1.3	1.4	2.3	2.2
United states	2.3	1.6	2.2	3.4	2.9
Japan	1.7	0.6	-0.3	-0.8	-0.7
Germany	1.5	0.6	0.7	2.1	2.4
France	1.3	0.7	0.6	1.8	1.8
Italy	1.7	1.7	1.7	2.6	2.6
United Kingdom	2.8	2.7	2.3	2.1	2.3
Canada	1.4	1.0	1.7	2.7	2.8
Others	2.4	2.5	1.3	2.4	2.9
Developing Countries	**9.2**	**10.3**	**6.8**	**5.9**	**6.0**
Africa	11.1	8.7	11.8	13.5	12.8
Middle East, Malta and Turki	27.7	27.6	23.3	19.1	19.1
Latin America	13.2	10.6	9.3	8.1	6.3
Asia	4.8	8.0	2.4	1.9	2.8
NIEs Asia	3.4	4.4	0.3	1.2	2.0
People's Republic of China	2.8	-0.8	-1.5	0.4	1.0
Indonesia	11.1	77.6	2.01	3.8	11.5
Singapore	2.0	-0.3	0.2	1.4	1.0
Malaysia	2.7	5.3	3.0	1.5	1.5
Thailand	5.6	8.1	0.5	1.5	1.7
Philippines	6.0	9.7	8.5	4.3	6.1
Vietnam	3.2	7.7	7.6	-1.7	0.8
Countries in transition	**28.2**	**20.9**	**43.9**	**20.1**	**16.0**
Central and Eastern Europe	41.8	17.1	10.9	12.8	9.3
Russia	14.7	27.8	85.7	20.8	21.5
Transcaucasus and Central Asia	36.5	15.3	15.4	14.8	-

Sources :
– IMF, *World Economic Outlook*, December 2001
– Bank Indonesia
– BPS-Statistics indonesia

Table 48
Interest Rates (%) and Exchange Rates

Description	1997	1998	1999r	2000r	2001 *
Interest rates in industrial countries					
Short term	4.00	4.00	3.80	-	-
Long term	5.40	4.50	5.30	-	-
LIBOR 6 months					
USD	-	-	5.50	6.60	3.80
Yen	-	-	0.20	0.30	0.20
Euro	-	-	3.00	4.60	4.10
Exchange Rates					
Yen/USD	120.99	130.91	102.51	114.41	131.66
DM/USD	1.73	1.76	1.94	2.08	2.20
SD/GBP	1.64	1.66	1.62	1.49	1.45

Sources : – IMF, *World Economic Outlook*, December 2001
– IMF, *International Financial Statistics*, December 2001

Table 49
World Trade Volume and Price
(annual percent change)

Indicator	1997	1998	1999r	2000r	2001 *
Volume	**10.0**	**4.1**	**5.4**	**12.4**	**1.0**
Price					
Industrial goods	-7.8	-1.2	-1.8	-5.1	-1.7
Non-oil and gas primary commodities	-3.2	-14.7	-7.0	1.8	-5.5
Oil	-5.4	-32.1	37.5	56.9	-14.0

Source : – IMF, *World Economic Outlook*, December 2001

Table 50
Current Accounts in Industrial and Developing Countries
(percent of GDP)

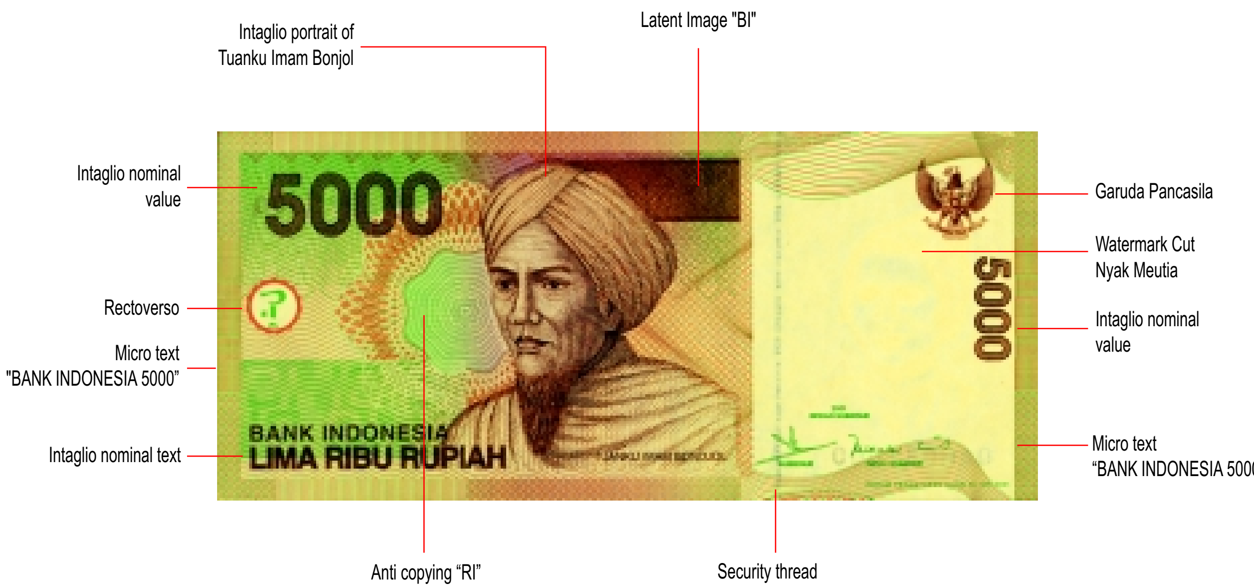
Country	1997	1998	1999[r]	2000[r]	2001*
7 major industrial countries					
United States	-1.7	-2.5	-3.5	-4.5	-4.8
Japan	2.2	3.2	2.4	2.5	2.2
Germany	-0.1	-0.2	-0.9	-1.0	-0.8
France	2.8	2.7	2.6	1.8	2.5
Italy	2.8	1.7	0.5	-0.5	-0.1
United Kingdom	0.8	-	-1.1	-1.7	-1.7
Canada	-1.6	-1.8	0.2	2.5	1.9
Developing Countries					
People's Republic of China	3.8	3.4	1.6	1.9	1.0
Indonesia	-2.3	4.3	4.10	5.2	3.4
Singapore	15.7	20.9	21.1	21.9	7.5
Malaysia	-5.1	12.9	15.9	9.4	7.5
Thailand	-2.0	12.8	10.2	7.5	4.7
Philippines	-5.3	2.0	10.0	12.1	4.9

Source : IMF, *World Economic Outlook*, December 2001

Appendix G

Banknote Specimen Issued 2001

Rp 5000 Denomination



Appendix H

List of Abbreviations

ADB	Asian Development Bank
APBN	State Budget
ARMA	Auto Regressive Moving Average
ASEAN	Association of of South East Asian Nations
BAPEPAM	Capital Market Supervisory Agency
BI-RTGS	Bank Indonesia -Real Time Gross Setlement
BIS	Bank for International Settlement
BNI	Bank Negara Indonesia (Commercial Bank)
BOTASUPAL	Coordinating Board for Eradication of Counterfit Money
BPD	Regional Development Bank
BPK	Supreme Audit Authority
BPKP	Finance and Development Supervisory Agency
BPRS	Sharia Rural Credit Bank
BPS	Central Statistical Agency
BRER	the Bilateral Real Exchange Rate
BRI	Bank Rakyat Indonesia (Commercial Bank)
BUMN	State Owned Enterprises (SOEs)
CAR	Capital Adequacy Ratio
CBS	Credit to Business Sector
CP	Core Principle
CPI	Consumer Price Index
DOC	Direct Observation of Capital
DPR	the House of Representative
DSR	Debt Service Ratio
DVP	Deliver versus Payment
EO	Exchange Offer
f.o.b	free on board
FAASM	Fixed Asset Accounting Simulation Model
FDI	Foreign Direct Investment

FRN	Floating-Rate Notes
GARCH	General Autoregressive Conditional Heteroscedasticity
GBHN	The State Long-Term Development Guidelines
GCS	the Gross Capital Stock
GDCF	Gross Domestic Fixed Capital Formation
GDP	Gross Domestic Product
GFA	Gross Foreign Assets
GFCF	Gross Fixed Capital Formation
GTZ	Gesellschaft fur Technische Zusammenarbeit
GWM	Giro Wajib minimum /Reserve Requierement
HDI	Human Development Index
IBD	Inter Bank Debt
IBI	Institut Bankir Indonesia
IBRA	Indonesian Banking Restructuring Agency
IBRD	International Bank for Reconstruction and Development
ICOR	Incremental Capital-Output Ratio
IMF	International Monetary Fund
IRFCL	International Reserves and Foreign Currency Liquidity
JBIC	Japan International Cooperation
JIBOR	Jakarta Interbak Offered Rate
JORR	Jakarta Outer Ring Road
KBI	Kantor Bank Indonesia/Bank Indonesia Regional Office
Kep	Keputusan/Decree
KLBI	Bank Indonesia Liquidity Support
KMK	Ministry of Finance Decree
LDR	Loan to Deposit Ratio
LEIs	Leading Economic Indicators
LNG	Liquified Natural Gas
LPG	Liquified Petroleum Gas
LPS	Lambaga Penjamin Simpanan/ Deposit Insurance Institution
MDH	the Mixture Distribution Hypothesis
MMBTU	Mile Mile British Thermal Unit

MoU	Memorandum of Understading
MPP	Ministry of Trade & Industry Decree
MPR	People's Consultative Assembly
MTN	Medium-Term Notes
NCG	Net Claim on the Central Government
NCS	Net Capital Stock
NDA	Net Domestic Assets
NFA	Net Foreign Assets
NIM	Net Interest Margin
NIR	Net International Reserve
NPLS	Non-Performing Loans
ODA	Official Development Assistance
OMO	Open Market Operation
OPEC	Organization of Petroleum Exporting Countries
PAPI	Indonesian Banking Accounting Guidelines
PAPSI	Accounting Guidelines for Sharia Banking in Indonesia
PBI	Bank Indonesia Regulation
PERC	Political & Economic Risk Consultancy
PIM	Perpetual Inventory Method
PSAK	Financial Accounting Standards
PSAKS	Accounting Princliples for Sharia Banking
PTTB	Pemberian Tanda Tidak Berharga/Unfit Banknotes
PUKM	Small-scale Business Development Program
REER	the Real Effective Exchange Rate
Rp	Rupiah
S&P	Standard & Poor's
SBI	Bank Indonesia Certificate
SD	Selected Default
SIABE	Information System for Export-Oriented Agroindustry
SIB	Information System for Baseline Economic Survey
SI-LMUK	Information System for Small Business Lending
SI-PMK	Information System for Procedures to Obtain Credit

SI-PUK	Integrated System for Small Business Development
SNA	System of National Accounts
SOECs	SOEs Coordinator
SOEs	State Owned Enterprises
SPK-UI	Supporting System for Investment Decisions
SWBIs	Bank Indonesia Wadiah Certificate
TMF	Trade Maintenance facility
UKM	Small-Scale Business
UNDP	The United Nation Development Program
US	United States
USAID	United States for International Development
VAT	Value Added tax
WTC	World Trade Centre