

Indonesia

Briefing paper

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Indonesia

Nominal GDP: US\$270 bn (market exchange rate)
US\$864 bn (purchasing power parity)

Ranking: 23rd largest MER basis; 15th largest PPP basis

Population: 242 mn (July 2005)

Age structure: 0-14 yrs 29.1%
15-64 years 65.7%
65+ years 5.2%

Median age: 26.5 years

Life expectancy at birth: 69.6 years

Languages: Bahasa Indonesia
English
Dutch
Local dialects (eg. Javanese)

Literacy: 87.9%

Land size: 1.8 mn sq kilometres

Capital: Jakarta

Administrative divisions: 30 provinces; 2 special regions;
1 special capital city district

Independence: 17 August 1945

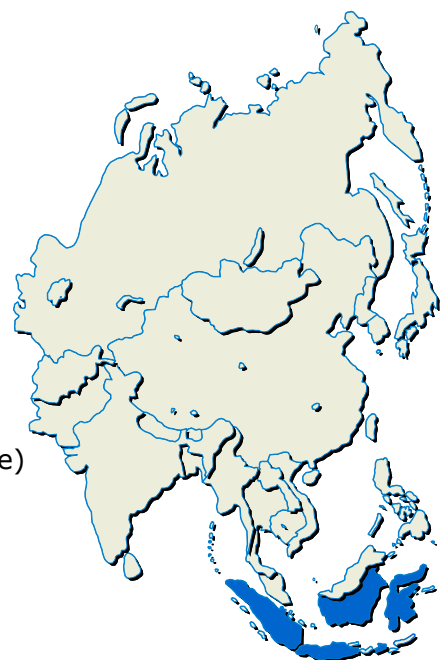
Chief of State and Head of Government: President Susilo Bambang
YUDHOYONO (since 20 October 2004)

Vice President: Muhammad Yusuf KALLA (since 20 October 2004)

Elections: President and Vice President elected by direct vote for five-
year terms (next election September 2009);

National Legislature: The Peoples Consultative Assembly (MPR) consists
of the 550-member House of Peoples Representatives (DPR) plus 128
regional representatives (DPD)

Elections: Parliamentary elections due in 2009



The structure of Indonesia's economy

The structure of the Indonesian economy has shifted away from the agriculture, forestry & fishing sector which, in 1980, accounted for a quarter of GDP and today represents around 15% of GDP. Indonesia has a rich mineral resource base and the mining & quarrying sector accounted for around 9% of GDP in 2004. Crude petroleum & products and LNG are Indonesia's major exports. The manufacturing sector has gained in importance, with its share of GDP growing from 12% in 1980 to 26% in 2004. Manufacturing has mainly been concentrated in labour-intensive industries such as textiles & garments, which is a major export item, as well as resource-based industries (eg. pulp & paper, cement, iron & steel). On an expenditure basis, household consumption has been the mainstay of the economy, currently accounting for close to 70% of GDP. Fixed investment, which was close to 30% of GDP in the early 1990s plunged to less than 25% in the aftermath of the Asian crisis. The low rates of investment in recent years have impeded a return to the strong rates of economic growth experienced prior to the crisis.

The crisis years were also characterized by an escalation foreign debt levels and deterioration in the fiscal balance. The current administration has, however, since made serious inroads into improving the external debt and fiscal profiles. Foreign currency debt to GDP, which reached exceeded 140% of GDP in 1998, dropped to close to 50% in 2005 and the fiscal deficit is forecast to be maintained at under 1% of GDP over the next few years.

Composition of GDP – output (% of total)				
	1980	1990	2000	2004
Agriculture, forestry & fishing	25.3	19.4	16.0	15.1
Mining, Manufacturing & Utilities	29.9	33.5	40.0	38.6
Construction & Services	44.8	47.1	44.0	46.3

Source: UN Statistics Division

Composition of GDP – expenditure (% of total)				
	1980	1990	2000	2004
Household consumption	55.3	56.8	68.1	68.0
Government consumption	9.8	8.8	6.3	7.4
Gross fixed capital formation	23.1	28.3	24.1	23.5
Exports of goods & services	35.9	25.3	31.6	31.1
Imports of goods & services	28.4	23.7	26.0	29.0

Source: UN Statistics Division

Politics

President Yudhoyono (SBY), leader of the newly formed Democratic Party, won a convincing victory in the country's first direct presidential elections in 2004. The relatively smooth election process, with parliamentary elections in April, presidential polls in July and the run-off on 20 September underscored significant democratic progress in Indonesia. President SBY's party, however, only secured 10% of the seats in parliament and relies on Golkar, which is led by VP Jusuf Kalla and has the largest single-party representation, to achieve a majority in parliament.

President SBY has four more years at the helm before his term ends in 2009. The investment mood in Indonesia has become more optimistic with a December 2005 cabinet reshuffle that installed the well-regarded economic team of Coordinating Minister of Economic Affairs Boediono, Finance Minister Sri Mulyani Indrawati, and incumbent Trade Minister, Mari Pangestu. The immediate focus

has been to address structural issues such as fuel and electricity price controls, and to resolve regulatory issues that impeded investment in infrastructure.

While President SBY's popularity has slipped following the implementation of difficult reform, in particular the dismantling of fuel subsidies, he still retains broad support compared with previous Presidents. This provides scope for further reform to be carried out, albeit gradually, without the occurrence of substantive protests that would be disruptive to economic activity.

External relations have improved markedly under the leadership of President SBY. Relations with China have improved considerably with both Presidents making bilateral visits in 2005. Indonesia continues to maintain strong ties with Japan and relations with the US have gradually improved with military links being restored late last year. Serious efforts to address corruption and capture high-level terrorism suspects have contributed toward rising international goodwill toward Indonesia.

Relations with Australia

Bilateral relations between Indonesia and Australia continue to improve. In April 2005, President SBY and PM Howard signed a Joint Declaration for a Comprehensive Partnership, underscoring efforts to further strengthen bilateral commercial ties. This was followed, in September 2005, with the signing of the Trade and Investment Framework by trade ministers from both countries.

Total trade between Australia and Indonesia was recorded at A\$6.7 bn in FY2004/05 (year ending June 2005), compared with A\$6.4 bn in FY2000/01. Indonesia ranked as the 10th largest export market for Australia and 14th most important source of imports. Australia generally records a deficit with Indonesia but registered a small surplus of A\$92 mn in FY2004/05. In terms of services trade, total trade between Australia and Indonesia amounted to A\$1.7 bn in FY2004/05 accounting for 2.4% of total services trade with Indonesia ranked as the 10th most important partner.

According to the Australian Bureau of Statistics, Australia's stock of investment in Indonesia was A\$2.3 bn as at December 2004, making Indonesia the 16th largest investment market.

Australia's Merchandise Trade with Indonesia				
FY2004/05	A\$ bn	% share of total	Rank	5-year trend growth
Exports to Indonesia	3.41	2.7	10	4.4
Imports from Indonesia	3.32	2.2	14	4.5
Total Trade	6.73	2.4	13	
Trade Balance	0.09			

Source: DFAT, Composition of Trade Australia

Australia's Merchandise Trade with Indonesia			
Main Australian Exports*	A\$ mn (% of total)	Main Australian Imports*	A\$ mn
Crude Petroleum	474 (13.9%)	Crude Petroleum	1,309 (39.5%)
Cotton	255 (7.5%)	Non-monetary gold	202 (6.1%)
Live animals	215 (6.3%)	Paper & Paperboard	120 (3.6%)
Aluminium	203 (5.9%)	Refined Petroleum	104 (3.1%)
Copper	147 (4.3%)	Wood	103 (3.1%)

*: includes confidential items which accounted for 26% of exports and 5.4% of imports

Source: DFAT, Composition of Trade Australia

Forecasts

In the period since the Asian crisis, Indonesia has been growing at a rate of 4¼% pa. (1999-05), driven largely by private consumption and more recently by investment. Growth slowed in the second half of 2005 due largely to the impact of accelerating inflation and interest rates on consumption and investment. The substantial reduction in fuel subsidies and the decline of the Indonesian rupiah prompted a jump in annual inflation, which averaged 17.8% in Q4 2005 compared with 7.8% in Q1 2005 while the central bank's key policy rate climbed to 12.75% in December 2005 from 7.4% at the start of the year. However, full-year growth was recorded at a relatively healthy 5.6%, up from 5.1% in 2004.

The economy is likely to expand at a slower pace of around 4¾% in 2006 against a higher interest rate and inflation environment but is expected to bounce back to grow by more than 6% in 2007. The government's decision to cut fuel subsidies in March and October 2005, while contributing to an acceleration in the inflation rate, has boosted the government's economic credentials. The expectation of electricity tariff hikes and further fuel subsidy reductions during the year will keep prices elevated.

Ratings agencies have made successive upgrades on Indonesia's debt ratings since 2002 in recognition of a relatively stable political and economic backdrop, commitment towards fiscal consolidation and a marked improvement in its external debt profile. Moody's Investors Service announced, in February 2006, that it has put Indonesia's foreign and domestic currency ratings on review for a possible upgrade. An upgrade to B1 is anticipated during Q2 2006.

Key economic indicators				
	2004	2005e	2006f	2007f
Real GDP growth (%)	5.1	5.6	4.8	6.1
Nominal GDP (US\$ bn)	257.6	300	345	390
CPI (% , year average)	6.1	10.4	10.2	7.5
Fiscal balance (% GDP)	-1.6	-0.7	-0.8	-0.3
Current account (% GDP)	1.2	0.5	1.2	1.6
Foreign exchange reserves (US\$ bn)	34.9	32.9	35	40
USD/IDR, eop	9,270	9,830	8,750	8,580
AUD/IDR, eop	7,233	7,203	6,125	6,006
Policy rate (% pa)	7.4	12.75	10.25	7.25

Source: Economics@ANZ

Issues in the economy

- The government has made efforts to pursue reform and streamline business operations. However, the bureaucracy remains the main obstacle to the pace of change. Concerns over corporate governance, judicial reform, entrenched vested interests and security will continue to emerge as risks to investment.
- Growing competition, especially from China, will pose a serious challenge for Indonesia's manufacturing sector. Nevertheless, Indonesia stands to benefit from strong mineral demand and the potential for investment in this sector is significant provided that the regulatory environment improves.
- More frequent threats of terrorism will also remain an impediment to large-scale investment. Nevertheless, the government's quick response to the Bali 2 attack reflects better crisis management by the current administration.

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