Committee on Balance-of-Payments Restrictions

DRAFT REPORT OF THE COMMITTEE ON BALANCE-OF-PAYMENTS
RESTRICTIONS ON THE CONSULTATION UNDER ARTICLE XVIII:12(b) WITH

INDONESIA

1. In accordance with its terms of reference, the Committee conducted the consultation with Indonesia under paragraph 12(b) of Article XVIII. The Committee had before it (a) a basic document (BOP/26/Rev.1) and (b) documents supplied by the International Monetary Fund as referred to in paragraph 3 below.

2. In conducting the consultation the Committee followed the Plan of Discussion for Consultations recommended by the CONTRACTING PARTIES. The consultation was completed on 18 June 1963. This report summarizes the main points discussed.

Consultation with the International Monetary Fund

3. Pursuant to the provisions of Article XV of the General Agreement, the CONTRACTING PARTIES had invited the International Monetary Fund to consult with them in connexion with this consultation with Indonesia. In accordance with the agreed procedure, the representative of the Fund was invited to make a statement supplementing the Fund's documentation concerning the position of Indonesia. The statement was made as follows:

"The International Monetary Fund has transmitted to the CONTRACTING PARTIES the Executive Board decision relating to the last consultation with Indonesia under Article XIV of the Fund Agreement and the background material prepared in connection with that consultation. The Fund has also provided a supplementary paper, dated May 29, 1963, to supply background information on recent developments.

"With respect to Part I of the Plan for Consultations, relating to balance of payments position and prospects, and with respect to Part III, relating to system and methods of the restrictions, attention is called to the Executive Board's decision of October 22, 1962, taken at the close of the Fund's latest Article XIV consultation with Indonesia. That decision
urged that certain steps should be taken in the fields of monetary, fiscal, and exchange policy, which would reduce the pressures on the balance of payments. Subsequently, on May 27, 1963, certain changes were made in Indonesia's exchange system. It is not possible at this time to assess the impact of these changes."

Opening statement by the representative of Indonesia

4. The representative of Indonesia recalled that at the time of his country's last consultation, in April 1961, its economic and payments positions appeared to be improving. In the previous two years there had been balance-of-payments surpluses and the exchange reserves thus accumulated had enabled an easing in the import restrictions. Government revenue was increasing and the budget deficit was being diminished. Finally export proceeds were showing encouraging signs of improvement as a result of higher world market prices and improved inter-insular transport. However, the years 1961 and 1962 had not in fact been favourable for the Indonesian economy generally and balance of payments in particular. First there arose two major political problems which had diverted financial and physical resources from more productive uses and secondly world commodity prices had declined.

5. The second half of 1962 had, however, seen the solution to the political problems and the Indonesian Government had turned its full attention to the economic and financial problems confronting the country. In March 1963 an Economic Declaration had been issued by the Government setting out both long and short-term economic policies and objectives. The long-term objectives of the economic policy of the Indonesian Government was to achieve sustained economic growth and higher living standards for the Indonesian people. For the two years immediately ahead there were two chief objectives viz: (1) the maintenance of a reasonable price level and (2) the rehabilitation of existing productive capacity to ensure its fullest use. The achievement of these two immediate objectives would be brought about by the creation of an adequate stock of rice and the ensuring of a sufficient supply of materials and parts for domestic industries.
Food production generally would be increased by expanding the area under cultivation; by intensifying agricultural yields by mechanization and improved techniques; by utilizing the armed forces in production; by accelerating the process of land reform; and by ensuring that projects directly related to the increase of food production were completed on schedule.

6. At the conclusion of his statement, the representative of Indonesia mentioned that, at the end of May 1963, the Indonesian Government had issued a new set of regulations covering exports, imports, domestic prices, and State enterprises. The Indonesian Government had also concluded lengthy negotiations with foreign-owned oil companies. The representative of Indonesia expressed his confidence that these and other measures taken would have a favourable impact on the Indonesian economy particularly in the field of exports.

Balance-of-payments position and prospects

7. The Committee discussed with the representative of Indonesia various factors affecting his country's balance of payments, particularly export earnings, diversification of exports, capital inflow and the burden of servicing her foreign debt.

8. A member of the Committee observed that in 1962 Indonesia's exports had dropped by 14 per cent in value as compared with 1961. The fall in exports had been accompanied by a 20 per cent drop in imports so that towards the end of 1962 Indonesia's foreign exchange reserves were starting to increase but the early months of 1963 had seen a further decline in their level. The representative of Indonesia was asked about prospects for Indonesia's exports in 1963. He stated that to a very large extent the value of Indonesia's exports depended upon international commodity price levels beyond her control. At the moment the position as regards rubber, for instance, was not very encouraging. However, there was no doubt that the continuous increases in domestic prices had adversely affected the competitive position of Indonesian exports in the world markets. Not only had these price increases pushed up production costs
but the degree of inflation had been such as to encourage producers to hold on to physical stocks, including export items, as a hoarding measure. It was hoped that the new measures, introduced in May 1963, would lead to a stabilization of prices which in itself should encourage exports by restraining costs. Moreover, the Indonesian Government was attempting to provide positive incentives for exporters in the form of favourable rupiah/foreign currency exchange rates. Although it was calculated that, on the basis of internal costs, Indonesian exporters should receive 270 rupiahs per dollar, the established exchange rate for exports was now 315 rupiahs per dollar. Moreover, exporters were permitted to retain part of their export earnings for their own use. (Further details of the retention scheme are contained in paragraph below.) It was not expected that Indonesia would diversify her exports very considerably in the immediate future since the primary objective of the Government was to restore normal exports of traditional items and to enable producing units, which had recently, for lack of imported materials and spare parts, been working very much below capacity, to achieve economic output rates.

9. In reply to a question, the representative of Indonesia commented on the likely effects on the imports of increased food production within Indonesia. The Government was encouraging rice production by raising producer prices. The multi-purpose project at Djatiluhur would enable three rice harvests per year instead of the present two on an area of 270 hectares. Food production would also be enhanced by the completion of the Palembang fertilizer project. Increases in rice and new fertilizer production would enable Indonesia to make considerable savings on imports.

10. A member of the Committee asked what arrangements Indonesia was making as regards the rescheduling of foreign debt repayments. The representative of Indonesia pointed out that debt servicing which, in 1963, would, in the normal course of events, amount to $200 million, was an extremely heavy burden on Indonesia's balance of payments. It was therefore the objective of his
Government to cut foreign debt servicing payments by 50 per cent, by means of a rescheduling of repayments. It was hoped that after 1965 the Indonesian economy and reserves position would be strong enough to resume repayments at normal rates.

11. A member asked what steps the Indonesian Government was now taking to encourage inflow of foreign private capital since, he observed, the policy of the Indonesian Government had, in the past, not perhaps been over generous as regards private capital. In this latter connexion he instanced the "production sharing scheme" which, he considered, could not be very attractive for foreign investors. The representative of Indonesia replied that his Government was not in favour of accepting foreign investment on traditional terms. It sought private investment under conditions which would be mutually beneficial to both Indonesia and the investor and for this reason encouraged production-sharing schemes. A National Private Consultative Council was in the process of formation and its chief purpose would be to foster private investment in the Indonesian economy. The means by which it would achieve this end were not yet known.

12. The representative of Indonesia stated that if Indonesia succeeded in her efforts to reschedule repayments of foreign debts and was able to obtain the $500 million of foreign aid it was seeking, then it was likely that her foreign transaction would be in balance in 1963.

Alternative measures to restore equilibrium

13. Members of the Committee emphasized that, in their view, the crux of the problem confronting Indonesia in the balance-of-payments field lay in the rapid inflation which had afflicted the economy in recent years. A member of the Committee noted that the Djakarta index of retail prices of nineteen foodstuffs had increased by 150 per cent in 1962 and by a further 41 per cent in the first quarter of 1963, and if rice were excluded, the respective figures were 210 per cent and 50 per cent. Members expressed the view that the
Indonesian Government should introduce fiscal and monetary measures aimed at curbing price increases. A member of the Committee asked when the Indonesian Government's budget was likely to move into a position of approximate balance. The representative of Indonesia replied that his Government was fully aware of the dangers of inflation and it was its aim to increase Government revenue. It was unlikely, however, that Government expenditure could be cut more than marginally. There were considerable difficulties in the way of increasing revenue from the taxation of a population which at present enjoyed only low standards of living. However, it was hoped that receipts from the taxation of imports would increase and that it would in due course prove possible to balance the budget.

14. The representative of Indonesia stated that, with the introduction of the May 1965 measures, it was not expected that there would be any further increase in price levels and it was thought that domestic prices would settle down at a foreign exchange equivalent of about 500 rupiah to the dollar.

System and methods of restrictions

15. The Committee noted that the information contained in the "basic document" (BOP/26/Rev.1) had been superseded by new measures introduced at the end of May 1963. Members of the Committee asked that details of the new measures should be circulated to contracting parties and this was agreed by the representative of Indonesia. The representative of Indonesia stated that, as a result of the new measures having been introduced so recently, he was not cognizant of their full details.
16. In reply to questions, the representative of Indonesia explained that there were now three exchange rates for imports. The rate of 315 rupiah per dollar (category I) was applied to certain essential imports viz: rice, materials for the textile industry, pharmaceuticals, fertilizers, newsprint and books. A rate of 810 rupiah per dollar (category III) was applied for imports of scheduled luxury items. The rate for all remaining imports was 540 rupiah per dollar (category II). The exchange rate for exports was 315 rupiah per dollar (see paragraph 8 above).

17. The representative of Indonesia explained the export proceed retention facilities open to exporters. Exporters could use an initial 5 per cent foreign exchange retention either to accumulate balances abroad or to import goods falling in any of the three categories of imports listed above. The additional 10 and 15 per cent retentions (the latter for producers exporting direct) could only be used to import items falling within categories I and II. Expenditure on imports from retentions could be made without the prior obtaining of a permit, as control, in this connexion was vested in the banks.

18. A member of the Committee stated that, from information he had received, he understood that new import duties had been imposed with nil duties for category I items, 50 per cent duties for category II items and 100 per cent duties for category III or luxury items. He understood that items bound under the GATT whilst not being subjected to the new import duties, as such, would be liable to a tax the equivalent of the duty. He asked what action Indonesia was contemplating in relation to its GATT obligations, if in fact this were the case. The representative of Indonesia replied that he was not in a position to give details of the new duties but stated that he was sure that GATT bindings would have been taken into consideration by his Government. The representative of Indonesia confirmed that, over and above the duties, there was a "revenue tax" termed "hasil perdagangan negara" which was applied to category II and category III items.

19. The representative of Indonesia confirmed that his Government was retaining the import licensing system which could be regarded as restrictive control on imports. There remained, moreover, a list of prohibited items which could not be imported into Indonesia because local production was sufficient to supply the needs of the domestic market. It was still necessary, moreover, for individual importers to obtain a licence to enable them to import at all.
20. Members of the Committee commented that an import control régime which incorporated multiple exchange rates, special retentions for exporters, quantitative restrictions by licensing, duties, revenue taxes and specific certificates for importers, must be regarded as exceedingly complex. The representative of Indonesia pointed out that the new measures adopted in May had simplified procedures somewhat in that there were now only three import exchange rates instead of, as previously, nine and one export exchange rate instead of two. Moreover, the Indonesian Government had abolished the "price component levy" or "siva retribution" and the special 1 per cent fee charge on applications for exchange.

21. Members of the Committee noted that a large sector of Indonesia's export trade was in the hands of State-trading establishments which, moreover, for certain items, enjoyed an import monopoly. They asked whether, particularly in view of the existence of bilateral agreements with certain countries, the State-trading establishments conformed fully to the requirements of Article XVII. The representative of Indonesia explained that State monopolies had come into existence for historical reasons. They conformed to the requirements of Article XVII in that all their purchases were made on purely commercial grounds. It was the intention of the Indonesian Government to enable private firms to compete with State enterprises in the importation of certain items where the latter presently enjoyed the monopoly so that competition could act as a brake on prices.

Effects of the restrictions

22. Members of the Committee commented that it was, as yet, too early to assess the impact on imports of the recent measures adopted by the Government of Indonesia. They pointed out, however, that the previous import régime had had considerable detrimental effects on the volume of imports made by Indonesia. Members of the Committee recalled the view, which had been repeatedly expressed by the Committee, that the restriction of imports aimed at the preservation of Indonesia's foreign exchange reserves might give impetus to the establishment and development of inefficient industries. In particular, they drew attention to the dangers inherent in the complete exclusion of imports of items contained in the "Prohibition List".
General

23. Members of the Committee expressed their understanding of the problems confronting Indonesia in the fields of exports, terms of trade, internal prices and exchange reserves. They wished the Indonesian Government success in the attainment of its objectives in the economic and payments spheres. They expressed the hope, however, that the Indonesian Government would find it possible to simplify the present complex system of restrictions and that it would be constantly on the watch for opportunities to extend liberalization.

24. Members of the Committee expressed appreciation for the full and comprehensive manner in which the representative of Indonesia had answered the various questions posed. In their view the consultation had been most useful in contributing to a better understanding of the import control policy and system in Indonesia. The representative of Indonesia stated that he had listened with interest to the suggestions made by members of the Committee, which he would communicate to Djakarta where they would receive serious consideration.