



OUTLOOK INDONESIA

MONTHLY UPDATE- MAY 2019

FROM THE AMERICAN INDOONESIAN CHAMBER OF COMMERCE

HIGHLIGHTS

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UPCOMING/RECENT EVENTS

May 1

Indonesia: The World's 3rd Largest Democracy Votes

Held in Conjunction with Asia Society

featuring:

Wayne Forrest
Cameron Hume
Anne Marie Murphy
Robert Heffner
Mari Elka Pangestu

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INDICATORS

US\$= 14,338
JSX= 6198.8 (last)
BI Rate: 6%
Inflation: 2.83%
Reserves: \$124.294 billion

(source: Bank Indonesia)
JSX= Jakarta Stock Exchange

THIS WEEK IN INDOONESIAN HISTORY

1954

Indonesia receives the first of 8 Convair commercial planes from General Dynamics

❖ ISSUE TO WATCH: APRIL POST ELECTION VISIT

Commentary by Wayne Forrest

I spent 9 days in Indonesia recently, April 20-30, and had very productive meetings in Jakarta and Banda Aceh. The run up to the recent Presidential Election was much hyped by the international media as a serious threat to Indonesia's pluralist state. To me, it was much ado about nothing. Indonesia is no more going to become an Islamic state than it ever has since its founding 70 years ago. I'll get to that but first let me lend my "unscientific" observations based on my conversations with local and international business people, sitting Ministers, political party supporters, state-owned companies, a sprinkling of taxi drivers, hawkers, students, and of course, our members with in-country operations.

The Election

Current Election Count: 70% of Votes Counted

Jokowi: 56%
Prabowo: 44%

Jakarta was quite calm and many people I spoke with did not take seriously the threatening public statements from Prabowo, who has yet to concede and believes the count was fraudulent. Jokowi supported reported that the President is disappointed he did not reach the 60% target which was the margin President Yudhoyono won in his reelection in 2009. PDI-P also thought it would significantly increase its seats in Parliament, but the direction of the count so far indicates otherwise. Based on the results so far here are a few conclusions:

- Compared to 2014 the President's margin of victory will widen by almost a factor of two from 8 to 15 million votes
- Parties with more of an Islamic affiliation are stuck at around 30%, similar to where they were in the 1950's. Secular parties have become more Islamic and it's a bit of an analytical conundrum to determine who may be co-opting who. Indonesia politics is highly consensual with no history of true opposition parties. Rumors are that Prabowo's young running mate Sandi Uno may be seeking a future benefit for helping to broker peace.
- If Indonesia had an Electoral College, Prabowo may have done much better, or perhaps won as he captured 18 of 34 provinces.
- As usual the election was won on the populous island of Java, especially central and east Java, which voted overwhelming for Jokowi.
- Voters there may have been positively influenced by the messaging of NU (a large and popular moderate Muslim social organization) for a unified Indonesia based on the secular, pluralist Pancasila ideology and an Islam tolerant of all religions. NU pinned this more on Jokowi rather than Prabowo (also a secularist) who courted more of the Islamist, Wahabbist right wing.
- The election may have proven that Indonesia is moving even further from the notion of a religious-based state. Democracy is prevailing and consolidating. The fly in the ointment is growing religious intolerance and gender discrimination, spread through certain mosques and on social media.
- Aceh, where I spoke at an international business conference AICC helped organize, voted overwhelmingly for Prabowo (80%). This region is the only area allowed to have sharia laws and would naturally candidates who stand up for Islam. However, many I spoke with voted for Prabowo not because of sense that he was the better Muslim but because they were not happy with Jokowi's performance.

Economy

Both local and foreign businessmen reacted well to Jokowi's victory, believing his administration continues to have an overall positive impact on business. State sector expansion (crowding out private sector), lack of coordination of policy between ministries, and the lack of competency and capacity within government remain at the top of the list of concerns. He is viewed as hard working, honest, but not necessarily surrounded by the "right people".

The Jokowi government remains committed to an economy less reliant on foreign management of natural resources, where local production is encouraged and sometimes mandated. These imperatives currently inhibit rather than enhance GDP growth predicted to stay in the 5% range for the next several years. Assuming Jokowi is named the winner, the consensus expectation is that he will continue to expand the role of state enterprises, bring further efficiencies to government, but not embark on major reforms. Several long-term foreign residents in Jakarta dispelled the notion that now reelected, Jokowi will be "unfettered" and can now pursue the types of reforms that bring 6-7% growth. Current ministers I spoke with, off the record, told me to expect more professionals in the next Cabinet, a continued emphasis on building infrastructure, and a major new priority to upgrade "human capital".

Indonesia is looking for investors in education, especially vocational training. It is expected that an early move will be to open the education sector to foreign universities, but they would have to do so in special economic zones. No real talk of opening the health sector to foreign investment or changing work rules for professionals, allowing, for example, foreign educated doctors to practice. No one I met believes there will be a serious revision to the 2002 labor law, long an impediment to labor intensive manufacturing investment. Nor is anyone predicted the same for the 2009 Mining Law, which remains an impediment to foreign investment. In fact several energy executives I met do not believe the President wants foreign investment in the sector at all. Furthermore, no one I met with expected any fundamental change to how judges are chosen, and how the court system operates. Regarding implementing the sweeping 2016 Halal Law, no one I spoke with had confidence the government had a solid plan to really implement it as written, given the lack of bureaucratic readiness and the realization of how costly creating the thousands of new certificates would be. If Indonesia believes it can steal from Vietnam's FDI, most executives I met say "think again". That said, these same people acknowledge the country's size, solid macroeconomic management, and young demographic will remain attractive for many investors, especially capital market players.

President Jokowi remains highly influenced by the Minister for State Owned Enterprises, Rini Soemarno, and the Minister of Finance, Sri Mulyani. Expect more consolidation among the SOEs into holding companies that can be utilized to reform the behavior of the private sector. This isn't necessarily new for Indonesia which has always practiced state-driven capitalism. But, in the late Suharto era there was an impulse (now dormant) to privatize SOE's. But viewing the arc of Indonesia economic policymaking for the past 50 years it may be surprising to some how strong the paternalist state has persisted even as the private sector has grown. When asked about this, the director of one state owned enterprise I met with told me his job was to "bring a more profit-oriented and efficient management" to his company. He advised foreign firms trying to enter Indonesia to voluntarily consider seeking a partnership with an SOE, something they wouldn't normally do. I take his remark seriously as a sign of Indonesia's future direction. Other key comments I heard:

- Most firms still experience modest sales growth, but profit margins are shrinking
- The Indonesian government has limited capacity, it remains difficult to raise money in domestic currency do limited hedging.
- Surveys of foreign business: business conditions have not changed much in last few years; no one believes regulatory conditions are getting better.
- The service sector is doing well as it is not under burdensome regulation
- Manufacturing competitiveness remains problematic.
- Cabinet shuffle could occur as early as June.
- Jokowi values stability over reform and would likely support a \$50 million local investment to create 500 jobs then a \$500 million foreign investment in the same sector that would create 5000.

The business sector (both local and foreign) laud the Jokowi's government accomplishments:

- Protecting secularism while integrating populist Islam
- Continued support of anti-corruption efforts via the KPK not just the police.
- Maintaining a low inflation environment
- Initial removal of energy subsidies, since reinstated but expected to be modified again
- Infrastructure performance: strong with road building, less well with ports and electricity

(The writer's opinions do not necessarily reflect those of the American Indonesian Chamber of Commerce or its members)

❖ ECONOMY AND BUSINESS:

• Shell Withdraws From Masela LNG Project

In 2016 Indonesia switched the Masela LNG project to an on-shore processing facility over the objections of its international partners, Shell and Inpex. Its inexperienced President believed he would be created more local jobs and the firms would go along. At the time, many resisted this notion and now we know they were correct. (Editor's Note).

(Reuters) Royal Dutch Shell is moving to sell its stake in Indonesia's \$15 billion Abadi liquefied natural gas (LNG) project, industry and banking sources said, following on from an asset disposal program that has raised more than \$30 billion. Shell, the world's largest buyer and seller of LNG, is raising cash to

help pay for its \$54 billion purchase of BG Group in 2015 and hopes to raise around \$1 billion from the sale of its 35 percent stake in the project, the sources said.

Shell's decision to sell out of the Abadi project in the Masela block, operated by Japanese oil and gas firm Inpex Corp which holds the remaining stake, highlights the difficulty Southeast Asia's largest economy has in attracting energy investment.

Shell, Inpex and an official with Indonesia's Energy and Mineral Resources all declined to comment.

Construction was due to start in 2018, but in 2016 was delayed until at least 2020 after Indonesian authorities instructed a switch from an offshore to an onshore facility.

• Unemployment Reaches New Low

Indonesia has recorded its lowest unemployment rate in more than a decade this year, though a wide gender wage gap has proved to be harder to shift. The unemployment rate dropped to 5.01 percent in February from 5.13 percent in the same month last year, according to new Central Statistics Agency (BPS) data released on Monday. In numbers, 6.82 million Indonesians out of a total working population of 136 million remained unemployed in February, compared to 6.87 million a year ago, the data showed. BPS head Suhariyanto said unemployment rate has continued to decline in the past four years, despite millions of new workers entering the job market each year. (*Jakarta Globe*)

• Plan to Move The Capital

President Jokowi made headlines when he revived a plan to move the nation's capital out of Java, perhaps to Kalimantan. The plan makes some sense as it could ease congestion and help the city cope with the a rising water table that combined with predicted sea level rises could flood large sections of Ja-

karta. Before everyone gets too excited its good to hear from the agency tasked to pay for it. (*Editor's Note*)

The Finance Ministry has announced that a plan to move the capital from Jakarta was still in its early phases as the ministry was currently waiting for further details from the National Development Planning Agency (Bappenas).

According to Finance Minister Sri Mulyani, discussions in the Cabinet have not reached the point of measuring how long it would take to build the new capital, but they have instead focused on why such a plan was needed and the various criteria the city must meet. The relocation plan is intended to turn Jakarta into a more livable city and ensure equal economic growth across Indonesia. "Bappenas needs to finalize the details, and then we will talk about planning and budgeting [...] We currently still do not know the engineering details and the exact location [for the new capital]," Sri Mulyani on the sidelines of the 52nd Asian Development Bank (ADB) annual meeting held in Fiji on Saturday. She conceded that the budget needed to build a new capital would be huge.

❖ POLITICS AND SECURITY:

• Police Declare Prabowo Supporter a Treason Suspect

Political activist and attorney Eggi Sudjana has been declared a treason suspect, a police spokesman said on Thursday. Investigators interrogated Eggi for several hours as a witness in April after a member of the public filed a police report against him over a statement he allegedly made on April 17, encouraging supporters of presidential candidate Prabowo Subianto and his running mate Sandiaga Uno to embark on "people power" to overturn the result of last month's presidential election. Eggi said: "[Therefore,] as our guru, Mr. Amien Rais, has said, we must embark on people power. Do you agree? Are you brave

[to do it]? When people power is implemented, we don't need to follow [legal] steps, because it will be the people's sovereignty," Eggi allegedly said at the time. "This is maybe the way of Allah for Mr. Prabowo to be inaugurated [as president]. We don't need to wait until Oct. 20," he added, amid chants of "Allahu akbar!" ("God is greatest") from the crowd. Eggi faces multiple charges, including under articles 107 and 110 of the Criminal Code on treason, which carry a maximum penalty of 20 years' imprisonment. In a separate case, former Army general Kivlan Zein was also reported for treason in a separate case. (*Jakarta Globe*)

❖ FOREIGN AFFAIRS/US INDONESIA RELATIONS:

• Tangle in the Natuna Sea

Indonesia's Foreign Affairs Ministry has summoned Vietnam's ambassador to Indonesia Pham Vinh Quang to explain an incident involving an Indonesian Navy war ship and two Vietnamese coastguard boats in the Natuna Sea last weekend, the ministry said on Monday. On April 28th Indonesian Navy war ship KRI Tjiptadi-381 was involved in a tense skirmish with two Vietnamese coastguard vessels in North Natuna Sea. According to a statement by the Indonesian Navy, the war ship had captured a Vietnamese fishing boat operating illegally on Indonesian

waters. The two Vietnamese coastguard boats, identified as KN 264 and KN 213, belonged to Vietnam's Fisheries Department.

When KRI Tjiptadi-381 started towing the fishing boat, the Vietnamese coastguard vessel KN 264 hit the war ship, while KN 213 bumped the fishing boat to sink it into the water. Vietnam claimed the skirmish happened on its territorial waters. The Indonesian Navy did not retaliate to the Vietnamese coastguards' provocations. "The Vietnamese boat crew were taken to the Ranai Naval Base. They will face a legal process," Admiral Yudo said in a statement.

❖ SOCIAL/CULTURE/EDUCATION:

• Religious Intolerance Survey: Disturbing Results

Indonesia is set to enjoy the benefits of a "demographic bonus" – a large productive population – until 2030, but it has its work cut out to prevent radicalism and intolerance from spreading among its young people. If the government fails with this project, it is feared that the much-hyped bonus can quickly turn into a huge disadvantage. Ubaid Matraji, a coordinator for the Network for Indonesian Education Watch (JPPI), said a survey released by Syarif Hidayatullah State Islamic University's Center for the Study of Islam and Society (PPIM) showed intolerance and radicalism remain serious threats for Indonesia's youth. The respondents for the survey were Muslim teachers and students. Results showed that around 63 percent of the Muslim teachers and 57 percent of the Muslim students were intolerant of other religions. Ubaid said if the government fails to pay

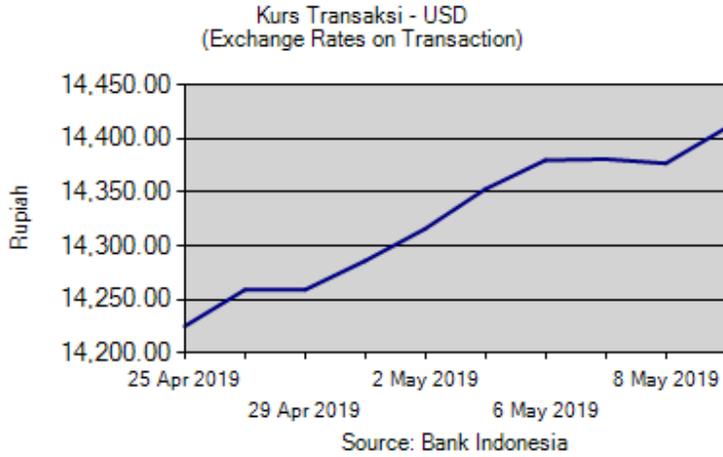
serious attention to the problems of intolerance and radicalism, Indonesia can soon say goodbye to its demographic bonus. "Worse than intolerance, the survey also showed nearly half of the Muslim teachers have opinions that can be considered as radical," Ubaid told Suara Pembaruan, Jakarta Globe's sister publication. (*Jakarta Globe*)



Reject Radicalism

CHARTS:

Dollar in Rupiah



Jakarta Stock Exchange Index



Inflation

