



Indonesia: How Much Worse Will Things Get?

by Ralph A. Cossa

Jakarta: Everyone I talk to here in Indonesia believes that things will get much worse before they get better. Much more difficult to find is anyone who thinks things will start getting better anytime soon. The perception is that “the old man” – a reference to President Suharto that used to be a term of endearment and now is used more derisively – just “doesn’t get it”; that he is not willing to take the current economic crisis seriously and do what’s required to restore domestic and international confidence in his nation.

The President’s apparent choice of State Minister of Research and Technology B.J. Habibie as his new vice president – a decision which will not be formally confirmed until the People’s Consultative Assembly meets at the beginning of March to re-elect Suharto, but which seems 99% certain – increases this sense of hopelessness and despair both domestically and in the region. Habibie is not known for his fiscal responsibility.

No less than Singaporean Senior Minister Lee Kuan Yew, in a pointed reference to Habibie’s apparent selection, has offered the unsolicited advice that the next vice president must be someone who inspires confidence in the international financial community, something Habibie clearly does not do. Every time Habibie’s name is mentioned, the rupiah sinks significantly. The apparent confirmation of his selection, combined with news of continued riots on the countryside, once again drove the rupiah past the 10,000 Ru to the US dollar mark on Monday (2/16).

The President’s apparent solution, the institution of a Currency Board System (CBS) which will reportedly peg the rupiah at an unrealistic 5,000 Ru to one US dollar rate has merely compounded the problem. The word in Jakarta is that the President’s new economic advisor, American economist Steve Hanke – who is strongly urging the creation of a CBS, contrary to the advise of the International Monetary Fund (and just about everyone else, reportedly to include the Indonesian economic policy committee he is supposedly advising) – was introduced to the President by his children. This raises the suspicion that the currency board idea is merely another family ploy to make money by setting an unrealistic peg and then immediately cashing in assets and rupiah for dollars.

Even if this is not the intention – and there are others, apparently including the President, who genuinely believe that the peg is desperately needed to ensure currency stability as a prerequisite to economic recovery and reform – an unrealistic peg is likely to cause a run on dollars beyond anything the nation’s dwindling foreign exchange reserves can handle. In addition, IMF Managing Director Michel Camdessus has warned that establishing a CBS will compel him to recommend against a continuation of the current IMF bailout

program. This puts next month’s scheduled \$3 billion IMF disbursement to Indonesia at risk (which will further strain foreign exchange reserves).

[All this has caused the South China Morning Post, in a recent editorial, to opine that if Suharto establishes a CBS before stability is restored to Indonesia’s economy, “he is likely to find himself exchanging crisis for disaster.” This Hong Kong commentary also notes that “such an action would affect the whole region, and could deal a crippling blow to the fragile recovery now under way.” It is the regional consequences (an economic “domino effect”?) that has prompted leaders like Lee Kuan Yew to violate ASEAN’s own non-interference rules and warn against destabilizing actions.]

Flaunting the IMF (not to mention ignoring a direct appeal from the President of the United States) is not seen as an ideal way of inspiring international investor confidence. To his credit, State Minister of National Development Planning Ginandjar Kartasmita has announced that the government will consult with the IMF over the CBS proposal, which he identified as “one of several alternatives being considered to shore up the rupiah.” However, the government’s track record on accepting the IMF’s advice (or on following it even if it is accepted) provides little cause for optimism at present.

Meanwhile, continuing and increasingly more intense riots throughout the country are just the tip of iceberg. Thus far, the peoples’ anger has been directed largely against the Chinese merchant community. Some are concerned that the government, while not encouraging the disturbances, sees them as a potentially useful safety valve, allowing people to blow off steam directed at the focal point of their frustration (rising food and commodity costs) rather than at its root cause. But, the merchants have only two options in the face of growing acquisition and transportation charges: raise prices or board up their shops and stay home. Once the latter begins to occur, hunger rather than frustration will begin driving the rioters and their anger will become more directed at the source.

The Army has sworn to keep order and few question it’s willingness or ability to do so, at least in the near term. During his swearing in this week as Indonesia’s new Armed Forces (ABRI) Commander, General Wiranto noted that “the Indonesian military’s next move is to take stern steps against anyone who tries to pull an unconstitutional act or any act which endangers the country.” ABRI in general and Wiranto in particular remain highly loyal to the President – the highly competent Wiranto, at age 50, becomes the youngest officer to hold the top ABRI leadership position, a reflection of the degree of trust and confidence Suharto feels toward his former adjutant.

But, ABRI has traditionally placed its loyalty first and foremost to the nation. Suharto has instructed the military to take whatever actions are necessary to maintain national stability and integrity. What if they conclude that this can only be accomplished by a change of leadership? What if they conclude that a failure to take the necessary steps to improve the economy and remove the source of people's frustration and anger, the elevation of the generally unpopular Habibie, the institution of a destabilizing CBS, and the general failure of the president to lead the nation through these difficult economic times, together constitutes "an act which endangers the country?"

The likelihood of this happening today, thankfully, remains slim and no one wants to see things come to this. But it is not outside the realm of possibility, especially if the riots continue to worsen and spread and the president seems unwilling or unable to lead the country out of its increasingly more self-inflicted crisis.

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