

Indonesia: the Wirjawan question

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Summary

Late last month, Indonesian Trade minister Gita Wirjawan stood down to concentrate on his long-anticipated campaign for the Indonesian Presidency. Wirjawan has set the tone for Indonesian inward investment and trade policy for half a decade, and that tone has been a pragmatic mix of openness and intervention. Under Wirjawan, Jakarta has taken a series of measures designed in large part to force change in Indonesia's trade profile - substituting a higher level of value-added production for a heavy dependence on raw commodity exports. Handicapped by a party ticket in free fall and in a potential contest with Indonesia's rising political superstar Joko Widodo, Wirjawan is very unlikely to win the Indonesian Presidency. But his political and policy style is likely to outlast him.

Late last month, Gita Wirjawan resigned as Indonesia's Trade Minister to free himself to run for the candidacy of the Democratic Party for Indonesian President to replace Susilo Yudhoyono in July. Wirjawan's decision was not a surprise: the radio adverts and t-shirts extolling his leadership credentials have spoken of his Presidential ambitions for some time. Wirjawan has stepped down from office early to give himself plenty of time to campaign for the Democratic Party's candidacy. He will need it if he is to build up the popular support and momentum to displace Yudhoyono's instinctive support for his brother-in-law, Pramono Edhie Wibowo - blood being generally thicker than water in Indonesian politics.

Wirjawan's odds of winning the Indonesian Presidency are a lot longer, if not prohibitive (Fig 1). Despite a strong period of economic growth, support for the governing Democratic Party has collapsed since 2009. Having run on an anti-graft platform, Yudhoyono's

government has been dogged by a succession of corruption scandals, as has major opposition party Golkar. Although popular Jakarta governor Joko Widodo ('Jokowi') has yet to declare his own candidacy, he is already being treated as the presumptive favourite. All Indonesian political polling needs to be handled with care, but some recent polls suggest that if PDIP leader Megawati Sukarnoputri (daughter of former President Sukarno) were to place Jokowi's candidacy over her own ambitions for the Presidency he would be a formidable frontrunner.

Wirjawan's own presidential ambitions are grounded in the calculation that he can claim some of the credit for a strong economic performance, while using a reputation for personal probity to sidestep his party's corruption problem. With growth averaging around 6% over the last five years and a booming equity market, Indonesia has been a portfolio investor favourite, although taper-

related exchange rate wobbles and persistent concerns about infrastructure and economic management have lingered.

There is no doubt that Wirjawan himself has played an important role in setting the tone for inward investment and trade policy in Indonesia over the last five years. A US-educated former investment banker and technocrat, he led Indonesia's investment promotion body from 2009 to 2011 before being moved to the Trade Ministry by President Yudhoyono in 2011. Wirjawan earned good reviews for his handling of Indonesia's hosting role of both the 2013 APEC summit and the Bali WTO Ministerial in December 2013. At the latter, his desire to see Indonesia bring home a successful outcome seems to have trumped Jakarta's more conventional instincts to side with Delhi on questions of food security. With the Bali deal ultimately avoiding any difficult questions of new market access for imports, it was a lot easier for Jakarta to be constructive.

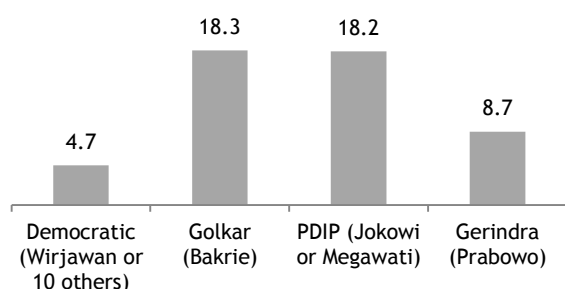


Fig 1: Support for main Indonesian political groupings
Source: LSI, February 2014. No defined Presidential candidate considered.

Wirjawan's time as Indonesian Trade Minister and his instincts in the job are worth reflecting on. In Canberra and Beijing in particular, Wirjawan and the Yudhoyono government have developed a reputation for economic nationalism and a strong streak of interventionism in trade. Both charges are fair, to a degree. It is an important question

to ask how the Wirjawan worldview carries over into the next Presidency, even if he himself is not President.

The Wirjawan worldview

Two things have stood out about Indonesian trade policy under Wirjawan and Yudhoyono. The first is the way it has been forced to respond to an important shift in US ambitions in the Asia Pacific region. Washington's refocusing on APEC after the stalling of the WTO multilateral agenda in 2008 caught Jakarta off guard. Jakarta, along with Manila and Seoul, was initially dismissive of the US-led Trans-Pacific Partnership (TPP) as a insubstantial piece of regional diplomacy intended chiefly to put pressure on China. But if sensitivity about US regional leadership and its own relationship with Beijing prompted a measure of aloofness, realism has begun to creep in. With 12 of the 20 APEC members now involved in the TPP negotiation and Japan having joined in 2012, the tone in Jakarta has changed markedly. While Indonesia stays outside TPP for now, the next administration will have big choices to make about its attitude to Washington's regional agenda.

The second feature has been interventionism, especially in export restrictions designed to encourage a reduced dependence on raw commodity exports. The most recent of these is a ban on exports of a range of raw minerals including bauxite ore and nickel that has been brewing since 2009 and finally came into force on January 12. The ban was strongly contested by Indonesian miners, and US firms Freeport and Newmont both obtained last minute temporary relaxations in the ban for 'semi-processed' concentrates until 2017. The logic of these bans and earlier similar measures has been that they will encourage domestic smelting and processing of minerals,

and therefore a greater degree of value-added before export.

This focus on forcing change in Indonesia's trade profile is driven both by an anxiety and a measure of confidence. The anxiety is the fear that while commodity exports have driven the strong growth of the last decade, Indonesia is not extracting full value from its natural or human resources. Unlike China, Indonesia is not a huge exporter of manufactured or finished goods. Its export profile is overwhelmingly dominated by raw materials - timber pulp, coal, bauxite, minerals and palm oil (Fig 2). Large volumes of this go to China for processing or consumption.



Fig 2: Evolution of Indonesia's export mix (LH % of total export income) and Chinese share of Indonesia's export market since 2006 (RH %)

Source: WTO

The upside of the global commodity boom has been the funding of strong domestic demand, a local services industry and a middle class that is now the same size as India's - approaching 150 million people. Domestic consumption accounts for 56% of Indonesian GDP, more than one and a half times the level in China. During Wirjawan's tenure, Jakarta's

calculation has been two-fold. First, that high commodity prices created an incentive to invest in new processing capacity in Indonesia. Second, that resilient domestic demand created a backstop for any short term fall in commodity exports provoked by export restrictions. The result has been a string of incentives for domestic processing of commodities like palm oil, or heavier requirements for raw commodity exports to promote their refining in Indonesia. Jakarta has irritated Beijing by using export restrictions to encourage bauxite ore processing in Indonesia and Canberra with restrictions on the import of Australian cattle to encourage the local beef industry.

Whether this policy will be sustainable will depend on a range of factors. Falling commodity prices have begun to change the economics of making large investments in smelting and processing that the policy is premised on. But the government's case for new inward investors is based on the promise of a captive market. Without the processing capabilities to transform their raw materials, domestic miners will be hit twice by the export bans: unable to export and with no domestic refining market to sell to. Pressure on the government to reverse the measures is strong. The political success of the policy largely depends on the investment decisions taken by nickel and bauxite processors over the next few months.

The Jokowi question

Gita Wirjawan is hardly alone among policymakers in the emerging economies in being willing to take a pragmatic line on intervening in trade in an attempt to guarantee a domestic supply of commodities or reshape their economy's export profile. Economic nationalism may still attract formal disapproval in Washington and Brussels but for

many emerging economy trade ministries it is a question of degree. The Wirjawan worldview in any case is capable of seeing export restrictions and a relatively open approach to inward fixed investment as perfectly compatible. Indeed, part of the point of export restrictions is to encourage Chinese inward investment in Indonesian refining. The bans have prompted 28 approved smelter projects in Indonesia, although only three of these are expected to come on line this year.

A new Presidency in 2014 is unlikely to change this basic outlook in Indonesia. Economic nationalism is a political perennial in Jakarta and all the large mainstream parties combine elements of economic liberalism and nationalism - often in a way that reflects the mix of vested interests that result from the close interweaving of Indonesia's political and business elites. Wirjawan's own personal instincts do at least reflect a thesis about development and Indonesia's place in global value chains. He has spoken about export restrictions and the policy of driving up value-added in Indonesian trade as a question of generational equity. Whether Jakarta can hold this line in the face of short-term pressures remains to be seen.

Assuming that he runs and wins, Jokowi's own views on Indonesia's international commercial policy remain largely unknown. He is governor of the closest thing Indonesia has to a global city, and he is well aware of the appetite of foreign services businesses for better and more legally secure access to Indonesia's domestic markets. He is widely regarded as a pragmatic businessman, and is likely to be pragmatic on questions of foreign fixed investment and trade. His background as a Javan furniture manufacturer before local and national politics has left him with a very clear

sense of Indonesia's global trading reach. But it has also given him a particular insight into the way that trade policy initiatives like the EU's new anti-illegal logging rules can squeeze Indonesian SMEs, no matter how well intentioned.

Jokowi has built his political career on a very sure popular touch on social justice issues - most recently being pictured standing in a flood drain to illustrate his commitment to resolving Jakarta's terrible infrastructure. He is likely to favour a Wirjawan-style mix of trade and investment promotion and pragmatic intervention to promote diversification. But his political style suggests a strong sensitivity to appearing to put the interests of foreign investors over local commercial interests - especially small businesses. In this respect, a Jokowi Indonesia may look a lot more like regional India for potential foreign investors or operators.

In terms of regional politics, Jokowi is even more of an unknown. With ASEAN in a period of relative stasis he is unlikely to change much. Washington will want to use the change of Presidency to bring Jakarta closer to the TPP, and Jokowi will have to make a big judgement in this respect. Mixed feelings about Wirjawan in Canberra, especially after his perceived willingness to tie Australian cattle exports to the heated dispute over allegations of Australian spying on Indonesian leaders, mean that Canberra is also likely to see a Jokowi Presidency as a chance for a serious reboot in relations. But in Jakarta's taste for a selective mix of openness and intervention we can be relatively sure that the hallmarks of Wirjawan's approach will outlast the man himself.

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