

# GENERAL AGREEMENT ON TARIFFS AND TRADE

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

### I N D O N E S I A

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 made was 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 general economic and balance-of-payments positions appeared to be improving. In the precious two years there had been balance-of-payments surpluses and the exchange reserves thus accumulated had permitted an easing in the import restrictions. Government revenue was increasing and the budget deficit was decreasing. 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 the balance of payments in particular. First, two major political problems arose which had diverted financial and physical resources from more productive uses and secondly world commodity prices had declined.

5. The political problems had been solved in the second half of 1962 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 objective 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 reasonable price levels for food and clothing, and (2) the rehabilitation of existing productive capacity to ensure its fullest use. The achievement of these two immediate objectives would be facilitated 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. 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, a factor obviously 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 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 hoard stocks, including export items. 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. As a result of new measures adopted, exporters receive a special incentive of rupiahs 270 per United States dollar in addition to the official rate of rupiahs 45 per United States dollar. Moreover, exporters were permitted to retain part of their export earnings for their own use and were given automatic allocations for imports. (Further details of the export incentive scheme are contained in paragraph 18 below.) It was not expected that Indonesia would diversify her exports in the near future since the immediate 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 imports of increased food production within Indonesia. The Government was encouraging rice production by raising producer prices. The multi-purpose project at Djatiluhur would permit three rice harvests per year instead of the present two on an area of about 217,000 hectares. Food production would also be enhanced by the completion of the Palembang fertilizer project. Increases in rice output 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 the normal course of events, would amount to more than \$200 million in 1963 was an extremely heavy burden in 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 the inflow of foreign private capital since, he observed, the policy of the Indonesian Government had in the past not perhaps been such as to encourage private foreign investment. He cited the "production sharing scheme" which, he considered, would not greatly attract 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 channel private investment for development purposes. 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 re-schedule repayments of foreign debts and was able to obtain the \$300 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.

14. 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 by taxing a population which at present had 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.

15. The representative of Indonesia stated that, with the introduction of the May 1963 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 rupiahs to the dollar.

System and methods of restrictions

16. The Committee noted that the information contained in the "basic document" (BOP/26/Rev.1) had been superceded by new measures introduced at the end of May 1963. The representative of Indonesia stated that, because the new measures had been introduced so recently, he was not himself familiar with all the details. 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.

17. In reply to questions, the representative of Indonesia explained that imports were divided into three categories. The effective cost to importers for these three categories were as follows:

Category I: (essential items i.e. rice, raw materials for the textile industry, pharmaceuticals, fertilizers, newsprint and books) 315 rupiahs per dollar (made up of 45 rupiahs basic exchange rate, plus 270 rupiahs "hasil perdagangan negara")

Category II: (those items not listed in categories I or III) 810 rupiahs per dollar (made up of 45 rupiahs basic exchange rate plus 495 rupiahs "h.p.n." plus 50 per cent duty)

Category III: (specified luxury items) 1,620 rupiahs per dollar (made up of 45 rupiahs basic exchange rate plus 765 h.p.n. plus 100 per cent duty).

The representative of Indonesia explained that "hasil perdagangan negara" could be translated as "state revenue from trade". A member of the Committee stated that he understood that items bound under the GATT would not be subject to the above new import duties as such but would be liable to a tax which would be the equivalent of the difference between the bound rates and the new import duties. He asked what action Indonesia was contemplating in relation to its GATT obligation if in fact this was the case. The representative of Indonesia replied that he was not in a position to give details of the new duties but he was sure that his Government would have taken account of the tariff bindings under GATT and, should there be any infringement of the bindings, would of course not fail to take the necessary steps in accordance with GATT procedures.

18. The representative of Indonesia explained the new export incentive facilities open to exporters. Exporters could retain 5 per cent of foreign exchange receipts and these could be used either to accumulate balances abroad or to import goods falling in any of the three categories of imports listed above. In addition, exporters were entitled to receive automatic allocation equivalent to 10 per cent or 15 per cent of their export proceeds (the 15 per cent applying to producers exporting direct) which could only be used to import items falling within categories I and II. Expenditure on imports from automatic allocations could be made without the prior obtaining of a permit as control, in this connexion, was vested in the custom authorities.

19. The representative of Indonesia confirmed that his Government was retaining the import licensing system which could be regarded as an additional means of controlling imports. There remained, moreover, a list of prohibited items which could not be imported into Indonesia even with retained exports proceeds, because local production was sufficient to supply the needs of the domestic market. However, exemption could be obtained from the Ministry of Trade.

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 registration of importers, must be regarded as exceedingly complex. They hoped that further simplification would be possible, looking forward to the eventual adoption of a realistic unitary exchange rate. The representative of Indonesia pointed out that the new measures adopted in May had simplified procedures in that there were now only three import exchange rates instead of a previous nine and one export exchange rate instead of two. Moreover, the Indonesian Government had abolished the "price component levy" or "siva retribution".

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 bases. 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 trade. 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 developments 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 considered that control of domestic inflation was fundamental to a solution of the difficulties which the Indonesian Government was facing in its efforts to restore internal and external equilibria and promote the development of the economy. They welcomed the recent simplification of the exchange and import control system and urged further efforts to simplify the still complex system. They expressed the hope that the Indonesian Government 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.