INDONESIA'S ECONOMY SINCE INDEPENDENCE

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In memory of my parents

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PREFACE

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2. 'The Impact of the Two Oil Booms of the 1970s and the Post-Oil Boom Shock of the Early 1980s on the Indonesian Economy', appeared in the *Proceedings of the Third AFC International Symposium 'Resources under Stress — Sustainability of the Local Community in Asia and Africa'*, published by the Afrasian Centre for Peace and Development Studies, Ryukoku University, Kyoto, 23–24 February 2008, pp. 239–51.

While the following two papers were unpublished papers:

1. 'Indonesia's Industrial Policies and Development Since Independence', which was originally presented at a Conference on Labour-intensive Industrialization in Southeast Asia, Kyoto, February 2008.

2. 'Indonesia's Auto Parts Industry', is an abbreviated and updated version of part 3 of the Final Report on *Indonesia's Industrial Competitiveness – A Study on the Garments, Auto Parts and Electronic Components Industries*, written by Haryo Aswicahyono, Raymond Atje and Thee Kian Wie for the Development Economics Research Group, The World Bank, March 2005.

Note: Some of these papers were published at different times in different books and journals, and for this reason may be repetitive. They were also written a few years ago, so some of the data may not be up-to-date.

INTRODUCTION

A short historical overview of Indonesia's economy since independence — Essays

This book contains a collection of papers on various aspects of Indonesia's economy and its industrial development since the early 1950s. This date is chosen because Indonesia only achieved effective sovereignty over the whole territory of the former Netherlands Indies, with the exception of Papua, after the official recognition of Indonesia's independence by the Netherlands government on 27 December 1949, even though on 17 August 1945 Sukarno and Hatta had officially proclaimed Indonesia's independence.

The Netherlands recognition of Indonesia's independence was only achieved after a bloody armed struggle by Indonesian freedom fighters against the returning Dutch army in late 1945. This armed struggle lasted until the delegations of the two contending parties (the Indonesian revolutionary government and the Netherlands government) under the auspices of the United Nations Commission on Indonesia (UNCI) at the Round Table Conference in The Hague in the autumn of 1949 agreed on the transfer of sovereignty from the Netherlands government to the government of the United States of Indonesia (*Republik Indonesia Serikat, RIS*) on 27 December 1949.

The Netherlands transfer of sovereignty to the federal Republic of the United States of Indonesia (RIS) was particularly galling to the revolutionary Republic of Indonesia based in Yogyakarta which had waged the armed struggle against the Dutch army. The reason was that it was forced to share power with 15 puppet states set up by the Dutch as a counterweight to the Republic. However, this federal structure proved to be fragile, as in the following months the puppet states one by one disbanded themselves to join the Republic.

At the celebration of independence day on 17 August 1950, President Sukarno was able to proclaim the restoration of the unitary state of the Republic of Indonesia (*Negara Kesatuan Republik Indonesia, NKRI*).

Outline of the book

This book does not provide a thematic account of Indonesia's modern economic history, as contained in Anne Booth's pioneering book *The Indonesian Economy in the Nineteenth and Twentieth Centuries: A History of Missed Opportunities* (1998) or the chronological account provided in the book *The Emergence of a National Economy: An Economic History of Indonesia, 1800–2000*, written by Howard Dick, Vincent Houben, J. Thomas Lindblad and Thee Kian Wie (2002).

Instead, this book discusses various aspects of Indonesia's post-independence history which have not yet been discussed in the above two books or are discussed in greater detail than has been the case with the above two books.

This book is divided into two main parts, namely Overall Developments and Industrial Development.

The part on **overall developments** is divided into three periods, namely the early independence period in the 1950s; the Soeharto era (often referred to as the New Order era, 1966–98); and the ensuing two economic crises, namely the impact of the Asian Financial Crisis of 1997/98 and the Global Financial Crisis of 2008.

In the section on the early independence period in the 1950s three papers are presented, including:

- Economic aspects of decolonization in the early 1950s, which discusses Indonesia's efforts at economic decolonization after political independence was achieved;
- The *Benteng* programme in the 1950s which was aimed at countering Dutch and Chinese economic dominance over the Indonesian economy;
- the debate on economic policy in newly-independent Indonesia between Sjafruddin Prawiranegara and Sumitro Djojohadikusumo, who were two of Indonesia's most prominent economic policymakers in the early 1950s.

The section on the Soeharto Era contains two papers, namely 'The Indonesian economy during the Soeharto Era — Achievements and Failings' which argues that during the first two decades the New Order state was a 'developmental

state', which during the third and last decade deteriorated into a 'predatory state' when economic policies were often designed to benefit President Soeharto's children and their cronies; and 'The Impact of the Two Oil Booms of the 1970s and the Post-Oil Boom Shock of the Early 1980s on the Indonesian Economy', which discusses the beneficial aspects of the two oil booms of 1973/74 and 1978/79 on the Indonesian economy, and the adjustment and deregulation (liberalization) measures which the Indonesian government had to take in early 1983 to restore macroeconomic stability and raise non-oil exports in response to the end of the oil boom era in 1982, when the price of crude oil in the international market steeply declined as a consequence of the economic recession in the major industrial countries.

The section on the Asian Financial Crisis of 1997/98, the Global Financial Crisis of 2008, and the prospects for rapid growth contains three papers, namely Indonesia's two deep economic crises, the mid-1960s and late 1990s' which compares the adverse impact of Asian Financial Crisis and the economic crisis of the mid-1960s on the Indonesian economy; the relatively mild impact of the Global Financial Crisis on the Indonesian economy; and a short discussion on the feasibility of Indonesia joining the BRIC (Brazil, Russia, India and China) group of rapidly-growing economies.

The second part on **Industrial Development** contains six papers, namely an overall discussion of Indonesia's industrial policies and industrial development since independence, a discussion on the Indonesian government's policies affecting Indonesia's industrial technology development; a discussion of the four major 'Channels of International Technology Transfer to Indonesia', specifically to its manufacturing sector; and three final papers on three of Indonesia's most important manufacturing industries, namely the labour-intensive garment industry'; 'the resource-intensive wood products industry'; and 'the medium-technology auto parts industry'.

PART I

THE EARLY INDEPENDENCE PERIOD IN THE 1950s

1

INDONESIANIZATION: ECONOMIC ASPECTS OF DECOLONIZATION IN THE 1950s[1]

The late Professor Harry Johnson at the University of Chicago defined economic nationalism as 'the national aspiration to having property owned by nationals and economic functions performed by nationals' (Johnson 1972:26). Following this definition, the force of economic nationalism in Indonesia, especially during the early independence period, can be easily understood. Economic nationalism was, and still is, reflected in the Indonesian government's economic policies. To a higher degree than in other Southeast Asian countries, economic nationalism in post-colonial Indonesia has been, and continues to be, an important factor affecting government policy. Whereas economic nationalism during the 1950s was primarily targeted at continuing economic dominance of the Dutch and ethnic Chinese business interests, in the years following the Asian economic crisis in the late 1990s economic nationalism came to be directed primarily at perceived interference by international organizations, in particular the International Monetary Fund (IMF), in the formulation of Indonesia's economic policies in order to handle the crisis.

Despite strong economic nationalism, pragmatic considerations have more often than not overruled popular pressures of economic nationalism, particularly after the advent of the New Order government in 1966. As a result, pragmatic economic policies have often been able to offset adverse economic and political effects of virulent nationalism, except during the final years of President Sukarno's rule.[2]

In the following pages the so-called 'Indonesianization' policies pursued during the 1950s, when economic nationalism was very strong, will be discussed. Using Johnson's definition, 'Indonesianization' (*indonesianisasi*) is

understood here as efforts by the Indonesian government to transfer property, or more correctly, productive assets owned by foreigners or foreign business, especially Dutch business, or residents viewed as foreigners, in particular Indonesians of Chinese descent, to indigenous Indonesians and to transfer economic functions performed by foreigners or residents viewed as foreigners to indigenous Indonesians. The drive towards 'Indonesianization' involved various measures taken by the Indonesian government in the 1950s aiming at an 'economic decolonization' considered all the more urgent since the Indonesian government already in early 1950 realized that political independence had not been accompanied by economic independence. 'Indonesianization' also formed an official response to the strong appeal by several nationalist leaders, such as Sujono Hadinoto of the Indonesian Nationalist Party (Partai Nasional Indonesia, PNI), who wished 'to convert the colonial economy into a national economy' (*merombak ekonomi kolonial menjadi ekonomi nasional*) (Hadinoto 1949:1).

THE POLITICAL AND ECONOMIC CONSEQUENCES OF THE ROUND TABLE CONFERENCE

With the transfer of sovereignty to Indonesia on 27 December 1949, a new phase began in the often tortuous relations between Indonesia and the Netherlands. Sovereign Indonesia could now deal with the Netherlands on an equal basis. However, during the 1950s, Indonesian-Dutch relations were marred by the lingering aftermath of the colonial relationship. While President Sukarno's efforts from the early 1950s onwards were aimed at 'completing the national revolution', specifically the 'liberation of West Irian' (West New Guinea), still under Dutch control, the Netherlands attempted strenuously to hold on to what little was still left of its formerly vast colonial possessions (Houben 1996:160).

The uncomfortable legacy of the colonial past was a direct consequence of agreements reached at the Round Table Conference (RTC) held in The Hague from late August until early November 1949 where the terms of Dutch acknowledgement of Indonesia's independence were formulated. The Indonesian delegation at the RTC agreed to a number of controversial conditions under pressure of wanting a quick agreement with the Dutch. The expectation of substantial financial assistance from the United States also induced Indonesian leaders to make economic concessions to the Netherlands. However, concessions greatly outweighed the relatively paltry economic assistance in the form of a loan of $100 million from the United States Exim-Bank that was at long last extended. Moreover, this loan, that had to be repaid

with interest, corresponded to only one–third of post-war credits by the same bank to the Netherlands. This was all Indonesia received after yielding to the insistence by Merle Cochran, the American observer at the RTC, that the United States government would shoulder the overseas debt bequeathed by the Netherlands Indies government to Indonesia (Kahin 1997:26).

Four provisions of the RTC agreement, two political and two economic, were particularly resented by the Indonesians (Dick et al. 2002:170). The first one was that the Netherlands would transfer sovereignty to the Republic of the United States of Indonesia (Republik Indonesia Serikat, RIS), a federation in which the Indonesian Republic (Republik Indonesia, RI), that had waged war with the Dutch, constituted only one state next to fifteen puppet states in various regions created by the Dutch in order to counterbalance the Republic. In addition, the Dutch insisted on the creation of a Netherlands-Indonesian Union along the lines of the British Commonwealth. However, within a few months after the transfer of sovereignty the fragile puppet states one by one dissolved themselves and joined the Republic. By 17 August 1950, five years after the proclamation of Indonesia's independence, RIS was dissolved and replaced by the present unitary Republic of Indonesia.

The second, far more contentious issue concerned the status of West New Guinea (named West Irian by the Indonesian nationalists, today's Papua). The Indonesian nationalists considered themselves the rightful inheritors of the Netherlands Indies. At the RTC the Dutch had refused to hand over West Irian to Indonesia, arguing that its Papuan population was racially, culturally and linguistically no part of the Indonesian nation. Since the Dutch adamantly refused to transfer sovereignty over West Irian, Dutch-Indonesia relations were doomed from the start and deteriorated until broken off altogether on 17 August 1960 (Houben 1996:173).

One economic matter that rankled Indonesian nationalists was the Dutch insistence that Indonesia would take over the foreign debt incurred by the Netherlands Indies government to the Netherlands to an amount of $1,130 million running with an interest rate of 3 per cent and due to be repaid in full no later than June 1964 (Kahin 1997:26; Sumitro Djojohadikusumo 2000:95). In addition, Indonesia was obliged to take over the rights and liabilities of the colonial government's external floating debt amounting to another $70 million (Kahin 1997:314). The total inherited debt obligation would have been even higher had Sumitro not at the RTC insisted that a large part of it consisted of military expenses by the Netherlands in its military campaigns to subdue the Republic (Kahin 1997:26; Sumitro 2000:95).

Despite resentment at the huge inherited debt, the Indonesian government faithfully fulfilled its international financial obligations. When the Burhanuddin

Harahap cabinet on 21 February 1955 abrogated the economic and financial agreement of the RTC as a result of the protracted West Irian dispute, only $171 million of the original $1,130 million remained to be repaid. No other former colony was obliged to take over such a large debt from its former colonial ruler as Indonesia (Kahin 1997:27).

The second, equally contentious economic issue was the guarantee that Dutch economic and business interests would be allowed to continue to operate in Indonesia without any hindrance, just like during colonial times. During the four-year armed struggle against the Dutch (1945–49), leading Dutch business firms had come to realize that trying to reoccupy Indonesia by military force was futile. Their top priority, therefore, was to rehabilitate and reconstruct their business establishments, estates, mines, and factories, which had been severely damaged during the Japanese occupation and the armed struggle against the Dutch (Lindblad 2002:141). Private Dutch business exerted heavy pressure on the Netherlands government to ensure that the RTC would yield an agreement safeguarding their extensive economic interests in independent Indonesia.

With these guidelines, the Dutch delegation at the RTC refused to make any concessions and insisted on obtaining necessary guarantees for unrestricted operations by Dutch business enterprises in independent Indonesia. Interestingly, on this issue the Indonesian and Dutch delegations quickly reached agreement formalized in the so-called Finec (Financieel-Economische Overeenkomst). This agreement secured the maximum possible economic and financial benefits for the Netherlands, in particular private Dutch business in Indonesia. Finec also included a clause to the effect that nationalization would only be permitted if it was in Indonesia's national interest and if both parties agreed. A judge would then decide on the amount of compensation to the owners on the basis of the real value of the nationalized enterprise (Meijer 1994:46-7).

Finec also contained provisions favouring Dutch economic interests, including a commitment by Indonesia that it would consult with the Netherlands whenever its fiscal and monetary policies would affect Dutch economic interests in Indonesia (Meijer 1994:46-7). No wonder that the late Professor Henri Baudet, a conservative Dutch economic historian, stated that the Finec contained the maximum attainable guarantees for the unhindered continuation of Dutch business (Baudet & Fennema 1983:213).

The achievement of political independence, yet without economic independence, posed a serious problem for the Indonesian government. Not being able to exert any control over important segments of the Indonesian economy clearly restricted the scope of action of Indonesia's economic

policymakers. For instance, pursuing an independent monetary policy would be difficult if the Java Bank, the bank of circulation which acted as the country's central bank, was still in the hands of the Dutch. It also gave rise to the widely held notion that the economic phase of decolonization had not even started. The late Sutan Sjahrir, Indonesian prime minister during the early years of the revolution and chairman of Indonesia's Socialist Party (Partai Sosialis Indonesia, PSI), expressed the widely felt dissatisfaction in 1951 stating that 'continuing Dutch economic domination in Indonesia, and not West Irian, was the real fundamental problem adversely affecting Netherlands-Indonesia relations' (Meijer 1994:349).

Dutch economic domination over the Indonesian economy is, amongst others, reflected by the fact that only 19 per cent of the capital not invested in agriculture was owned by indigenous Indonesians. Economic gains for the Netherlands from continued operations of Dutch business in Indonesia were substantial: out of total profits pocketed by foreign private business in Indonesia in 1953, no less than 70 per cent (Rp449 million) were transferred to the Netherlands. In addition, Rp464 million or 83 per cent of total overseas transfers for social purposes (pensions, personal savings and the like) also went to the Netherlands in that year (Meijer 1994:349).

Indonesia's economic dependence on the Netherlands was in particular visible in inter-island shipping, which was largely controlled, or virtually monopolized by the Dutch shipping concern KPM (Koninklijke Paketvaart Maatschappij, Royal Packet Company). Realizing that inter-island shipping constituted the vital artery of trade in the Indonesian archipelago, the Indonesian government understandably wished to terminate the domination by the KPM. However, these early plans could not be realized, because the Indonesian government lacked the financial means to take over KPM (Meijer 1994:350) at a price acceptable to KPM.

Continuing Dutch economic dominance in the Indonesian economy is evident from an estimate by the late Professor Benjamin Higgins, a United Nations consultant to the Indonesian government in the early 1950s. Higgins calculated that the Dutch-owned segment of the modern sectors in the Indonesian economy accounted for about 25 per cent of the nation's GDP and about 10 per cent of total employment (Higgins 1990:40). Many senior positions in the fledgling Indonesian public service were occupied by Dutch officials, whose loyalty to newly-independent Indonesia could not readily be taken for granted. According to one estimate, after the transfer of sovereignty about 17,000 Dutch public servants entered Indonesia's public service, although many of them were soon relegated to unimportant positions. Their incomes were eroded because of the monetary measures of the Indonesian

government to curb inflationary pressures (Houben 1996:171). Eurasians, that is persons of mixed Dutch and Indonesian descent, were also removed from the bureaucracy. They were distrusted by the Indonesians because they had sided with the Dutch during the revolution (Houben 1996:171).

The president and most directors of the Java Bank (which had functioned as the bank of circulation during the colonial period) were still Dutch (Higgins 1990:40). The head of the Foreign Exchange Control Board was also a Dutchman. The Board was an independent government body that in the colonial period had reported directly to the Governor-General. Sumitro observed that, when he became minister of finance in 1952, he entered a department full of Dutch officials who, as he caustically noted, had no clue about economics, but were very good at administrative procedures (Sumitro Djojohadikusumo 2003:59).

INDONESIANIZATION AND MEASURES TO REDUCE DUTCH ECONOMIC PREDOMINANCE

Despite unhappiness with the continuing Dutch predominance in the economy, the leading economic policymakers in the early 1950s, including vice president Mohammad Hatta, Sumitro Djojohadikusumo, Sjafruddin Prawiranegara and Djuanda, were pragmatic men who, while attracted to socialist ideals, did not adhere to any rigid ideological doctrine (Booth 1986:13). They did not constitute a cohesive group and adhered to views about several economic issues such as the role of foreign direct investment or the feasibility of crash industrialization. However, as pragmatic politicians they realized that top priority had to be given to economic stabilization and rehabilitation. Since a large part of the modern export sector, including large estates and several mines, were still owned and operated by Dutch private firms, these policymakers realized that they had to protect the legal rights of the Dutch enterprises, unpalatable though this was. The Dutch enterprises could therefore operate without any official restrictions, although this policy was often criticized by more radical nationalists. Yet, the pragmatic policymakers also realized that the Dutch export-oriented large estates and mines generated much-needed foreign exchange revenues to import food, raw materials and capital goods.

Despite constraints imposed by Finec, the pragmatic economic policymakers were determined to match Indonesia's hard-won political independence with meaningful economic sovereignty, even though they appreciated that it would take a long time and great effort. Since Finec provided the legal basis for nationalization under specified conditions, the Indonesian

government soon took steps to nationalize key economic institutions and enterprises of singular economic or strategic importance.

The first important economic institution to be nationalized was the Java Bank, the bank of circulation during the colonial period that had been chosen as the nation's central bank also after 1949. On 30 April 1951, Yusuf Wibisono, minister of finance, announced that the Indonesian government intended to nationalize the Java Bank as soon as possible. He explained to the press that the Masyumi party, of which he was a member, at its national conference in Yogyakarta in December 1949 had already urged for nationalization, and that he was proud to be able to implement that decision (Saubari 2003:71-2).

But Yusuf Wibisono had made his announcement in the press without consulting the Dutch (Sjafruddin 2003:81). Not surprisingly, the Dutch initially attempted to retain control over the Java Bank, but in the event the nationalization of the Java Bank proceeded relatively smoothly as the Dutch accepted that control of money and credit was an essential ingredient of sovereignty (Anspach 1969:137).

On 3 July 1951, the Sukiman cabinet, dominated by Masyumi, installed a committee on the nationalization of the Java Bank authorized to take all necessary preparatory steps towards nationalization, including drafting the required legislation. Members of the committee were Sumitro, Moh. Sediono, Soetikno Slamet, T.R.B. Sabaruddin, A. Oudt and Khouw Bian Tie (Saubari 2003:72).

Upon advice of the committee, the government decided that nationalization would be implemented through the purchase of shares from both domestic and overseas shareholders. To speed up the purchase of shares, the government sent two officials to the Netherlands, Moh. Saubari, secretary-general at the department of finance, and Khouw Bian Tie, advisor of the Java Bank. Their talks with Piet Lieftinck, the Dutch minister of finance, and the Dutch association for trade in securities in Amsterdam went smoothly, resulting in a decision to suspend trading of Java Bank shares on the Amsterdam Stock Exchange. The announcement was signed by Moh. Saubari and published in Het Financieel Dagblad (Financial Daily) on 3 August 1951 (Saubari 2003:72).

In Indonesia, Wibisono issued a statement on the same day about the government's offer to purchase privately held shares at 120 per cent of the nominal value when expressed in Dutch guilders or 360 per cent when expressed in Indonesian rupiah. The purchase of the shares proceeded well and within a couple of months 97 per cent of all shares had already been acquired by the government. On 6 December 1951 the law on the nationalization of the Java Bank was enacted (Saubari 2003:72-3).

A. Houwink, the last Dutch president of the Java Bank, had resigned and been succeeded by Sjafruddin Prawiranegara already before the nationalization took place. Sjafruddin, former minister of finance in the cabinets headed by Moh. Hatta and Moh. Natsir, was at first reluctant to take up the position at the Java Bank as he wanted to retire from public life. Sjafruddin wanted to earn enough money for the education of his children but was only in a position to do so in a private capacity as he, possibly as a result of his Dutch-styled education, did not want to abuse his power as a public servant to make money (Sjafruddin 2003:80). Sjafruddin therefore put forward as a condition that his salary, and that of all Indonesian staff, should not be changed to an Indonesian level and that privileges which the Dutch staff enjoyed should also be made available to the Indonesian staff. The government agreed and Sjafruddin became the first Indonesian president of the Java Bank. His candidacy was also supported by the staff at the Java Bank, including his predecessor Houwink (Sjafruddin 2003:80). In 1953, the Java Bank was transformed into Bank Indonesia with Sjafruddin Prawiranegara as its first governor.

Nationalization also affected other Dutch-owned enterprises occupying a key position in the Indonesian economy, for instance the railways in Java and public utilities such as electricity and gas companies (Burger 1975:170). Domestic air transport was transferred from the Koninklijke Nederlandsch-Indische Luchtvaart-Maatschappij (KNILM, Royal Netherlands Indies Airlines) to Garuda Indonesian Airways, Indonesia's national carrier. This airline was initially established as a joint venture between the Royal Dutch Airlines KLM and the Indonesian government. However, in 1954 Garuda was transformed into a fully state-owned airline with the role of KLM limited to providing technical assistance and advice (Burger 1975:170).

However, efforts to nationalize the Dutch-controlled KPM, which in 1956 still dominated inter-island shipping, did not succeed. However, the newly established Indonesian shipping company PELNI (Pelayaran Nasional Indonesia), the state-owned, inter-island shipping company which received financial assistance from the Indonesian government was able to make steady inroads into the market dominated by KPM. For instance, while in 1956 PELNI carried 25 per cent of the cargo, in 1957 it was able to increase its share to 29 per cent. Although in the passenger trade, the KPM was better able to keep its dominance with 94 per cent of the traffic, the introduction in 1956 of six new passenger ships enabled PELNI in 1957 to double the number of passengers carried (Dick, 1987: 18).

The nationalization of the Java Bank and other enterprises deemed to be of crucial importance to the Indonesian economy proceeded relatively

smoothly. Both the Dutch government and the owners of the enterprises in question realized that no sovereign government could leave its central bank, public utilities and vital modes of transport in the hands of foreigners.

Other efforts to counter Dutch economic control included vice president Hatta's instruction to the executive board of Central Trading Company (CTC), Indonesia's first government-owned, trading company established in Bukittinggi in 1947, to challenge the monopoly of the 'Big Five', the five leading Dutch trading companies (Daud 2003:256). The establishment of the CTC had been urged by Hatta who did not approve of the involvement by Indonesian revolutionary army units in smuggling agricultural commodities to Singapore and British Malaya in order to acquire military equipment and arms for the struggle against the Dutch. Therefore, Hatta wished to legalize these trading by separating smuggling from military operations through the establishment of a formal trading house, CTC (Daud 2003:255).

Heeding Hatta's instruction to challenge Dutch control over Indonesia's export and import trade, yet lacking any business experience themselves, the two directors of the CTC, Teuku Moh. Daud and Teuku Abdul Hamid Azwar, realized they had to look for people possessing the required experience and skills, especially with regard to international business. At the time, the only people who had such business experience and skills were Indonesians of Chinese descent. They therefore approached some Sino-Indonesian managers employed in the few large companies owned by Sino-Indonesians such as the Liem Goan Seng and Kian Gwan firms (Daud 2003:257).

At first, Daud and Azwar experienced some difficulty persuading CTC's board of trustees to recruit mainly Sino-Indonesian managers. They eventually succeeded because it was obvious that Daud and Azwar were not playing politics, and were only concerned with making CTC an efficient and viable corporation. This would be imperative to achieve the first task of CTC of reducing the domination of the Dutch companies over the Indonesian economy (Daud 2003:257).

Daud and Azwar were successful in recruiting a senior manager from the Liem Goan Seng company, Koo Liong Bing, who was willing to join CTC. Through Koo, CTC was able to recruit several other Sino-Indonesian managers, mainly from the Kian Gwan company. Later Koo himself became one of the directors of CTC (Daud 2003:257).

Another measure to try to counter the 'Big Five' was the so-called *Benteng* (fortress) programme launched in 1950 (Sumitro 2003:59). This programme was also the first major official strategy to further the development of a strong indigenous Indonesian business class. The *Benteng* programme focused on securing national control over the import trade by reserving import licenses

in certain restricted categories of easy-to-sell goods exclusively for indigenous Indonesian importers. The provisions of the programme, however, did not specifically exclude ethnic Chinese businessmen who possessed Indonesian citizenship (Mackie 1971:47-8). In fact, however, the *Benteng* programme was primarily aimed at countering both Dutch and Chinese economic domination.

To promote the development of an indigenous Indonesian business class, the government established new financial institutions providing credit to eligible businessmen. Such institutions included the Bank Industri Negara (State Industrial Bank, BIN), extending credits to large-scale agricultural enterprises and manufacturing and mining enterprises, the Bank Negara Indonesia (Indonesian State Bank, BNI), that gave loans to exporters and importers, and also the Yayasan Kredit (Credit Foundation) which provided guarantees for loans for which the customary business collateral was not available (Burger 1975:171).

Another important measure to 'indonesianize' the Dutch companies was a 'gentlemen's agreement' between the Indonesian government and the Dutch firms that 70 per cent of the companies' personnel had to be (indigenous) Indonesians. However, this 'indonesianization' (*indonesianisasi*) programme turned out to be limited to the lower functions in the companies. In fact, the Dutch companies in general were little motivated to train their Indonesian personnel in order to enable them to occupy higher functions and include the most competent among them in the companies' board of directors, as stipulated in provision 12 of Finec. At the estates the top function occupied by Indonesian personnel was usually that of *mandor* (supervisor) (Meijer 1994:352).

Very much aware of the fact that the Dutch companies were reluctant to promote their Indonesian staff to higher and managerial positions, the Wilopo cabinet (April 1952 – June 1953) resorted to reducing drastically the work permits for Dutch citizens in Indonesia. While in 1950 Dutch citizens could still freely enter Indonesia, after 1951 strict entry quotas were introduced, which gradually reduced the number of Dutch citizens given work permits and in 1953 only 1000 work permits were issued (Meijer 1994:353).

The Dutch companies soon experienced great difficulties because of the tiny visa quotas. Despite offering higher salaries and other favourable incentives, the firms were unable to slow down, let alone stop the steady outflow of Dutch employees. While remaining Dutch staff was initially able to take over the tasks of those who had repatriated, over time this was no longer possible as more and more Dutch employees were leaving (Meijer 1994:352-3).

The outflow of Dutch employees seriously threatened continuity in the operations of Dutch business in Indonesia. The companies therefore reluctantly started to train Indonesian staff in greater numbers to occupy the higher functions left vacant by departing Dutch employees. To this end, Dutch import and export companies established a trade school for their Indonesian staff. In general, however, numbers of participants in the training programmes remained limited as the directors of most Dutch companies were concerned that to elevate their Indonesian staff to senior managerial positions or to allow participation of Indonesian capital would pave the way to nationalization of their enterprises (Meijer 1994:353).

THE CURTAIN FALLS: NATIONALIZATION OF ALL DUTCH ENTERPRISES

Relations between Indonesia and the Netherlands deteriorated rapidly from the mid-1950s because of the Dutch government's adamant refusal to discuss the status of West Irian (Papua). When the Indonesian government in November 1957 failed to persuade the United Nations General Assembly to adopt a resolution calling on the Netherlands to negotiate a settlement with Indonesia on the West Irian issue, anti-Dutch demonstrations broke out in Jakarta. On 3 December 1957 workers of militant labour unions affiliated with the Indonesian Nationalist Party (PNI) started taking over Dutch enterprises and business offices (Meier, 1994: 584).

The head office of the Dutch interisland shipping company KPM in Jakarta, a prime symbol of Dutch economic dominance, was the first to be taken over by the workers. Another symbol of Anglo-Dutch economic power, Royal Dutch Shell, was not taken over as it was partly British-owned.

On 5 December 1957 the Department of Foreign Affairs called the Dutch *charge d'affaires* and presented him with a note that all Dutch citizens had to leave the country within the shortest possible time. The subsequent Dutch exodus proceeded relatively smoothly, and by March 1959 30,000 of the last remaining Dutch had repatriated, leaving only about 6,000 Dutch citizens behind. These people had stayed on because they were either working under contract with non-Dutch foreign enterprises (about 3,500), or were serving as missionaries (about 1,600) (Meier, 1994: 585, 592).

During the following two weeks this action was followed by similar takeovers of other Dutch enterprises all over the country. Although the Indonesian government had not initiated the takeovers, it did not attempt to resist the actions (Glassburner 1971:92). Some senior government officials, notably Sjafruddin Prawiranegara, governor of Bank Indonesia, openly spoke

out against the takeovers (Sjafruddin 2003:81). Sjafruddin felt that Indonesians through education and training first had to acquire the required skills to manage and run the modern Dutch enterprises.

Concerned about the economic and political chaos caused by unauthorized takeovers, General Nasution, the army chief of staff, took control of events on 13 December 1957 by issuing an instruction to the army to manage the seized enterprises. The PKI and SOBSI, anxious to avoid an open confrontation with the army, promised to support the military forces by keeping the seized enterprises operating (Ricklefs 1994:261).

In December 1958 the legal foundation was laid down for the nationalization of seized Dutch enterprises and this was effectuated for various categories of enterprises during the first half of 1959. All nationalized companies became state property (Dick et al. 2002:184). With one drastic action, the powerful Dutch business firms that had operated in Indonesia since the second half of the nineteenth century, were eliminated. Unlike the nationalization of the Java Bank and the public utilities at an earlier stage in the 1950s, which had been achieved by mutual consent, the nationalization of Dutch enterprises in 1959 was a unilateral measure taken by the Indonesian authorities in response to the collapse of Dutch-Indonesian relations because of the acrimonious dispute about West Irian.

DEALING WITH THE 'CHINESE PROBLEM'

The nationalization of Dutch enterprises went a long way towards satisfying the national aspiration 'to convert the colonial economy into a national economy' in Hadinoto's formulation. The nation's important productive assets, formerly owned by the Dutch, were now Indonesian-owned and important economic functions, formerly performed by the Dutch, were now filled by Indonesian nationals. But this conversion was still not felt to be complete as the large indigenous Indonesian population was still facing the economic dominance of ethnic Chinese businessmen, including both Indonesian as well Chinese nationals, who since colonial times had played a major role in the economy, particularly intermediate trade, rice milling, and money lending. Their economic dominance, and the perceived usurious activities of Chinese moneylenders (*Cina mindering*) caused much resentment, if not outright hatred, among indigenous Indonesians. For this reason the late Professor Everett Hawkins, an American economist who had worked in Indonesia in the 1950s and early 1960s, once referred to the 'double colonialism' that had prevailed in Indonesia.[3]

Next to efforts to limit Dutch economic dominance, the Indonesian government therefore in the early 1950s also took steps to reduce the

economic role of ethnic Chinese. However, taking measures to limit Chinese economic activities proved to be more difficult than eliminating Dutch economic interests. For one thing, the number of ethnic Chinese was much larger than the Dutch. Through intermediate trade and money lending, their economic activities in the rural areas were also far more intertwined with the economic activities of the indigenous population than the Dutch activities had ever been.

Moreover, the large ethnic Chinese group included Indonesian citizens as well as citizens of the People's Republic of China and a small group of pro-Taiwan 'stateless' citizens. It was therefore difficult for the Indonesian government to take measures directed at all ethnic Chinese, as this category included a relatively large group of Indonesian citizens. Having fought against Dutch colonialism and its implied racism, many Indonesian leaders found that overly discriminatory policies against its citizens of Chinese descent did not accord well with the ideals of the Indonesian revolution. Nevertheless, given strong political pressure, the Indonesian government did initiate measures in the early 1950s to reduce the economic role of the ethnic Chinese and promote the development of indigenous Indonesian (*Indonesia asli*) entrepreneurs. Such measures are discussed in detail in the following.

THE *BENTENG* (FORTRESS) PROGRAMME

Pressure to promote the development of indigenous Indonesian business grew stronger but, by and large, economic activities of indigenous Indonesians were confined to small-scale agriculture, small retail stores, and small-scale industries, such as batik, handicrafts, and clove cigarettes. To promote the development of indigenous entrepreneurs, Djuanda, minister of welfare, in April 1950 issued a regulation which gave priority to indigenous businessmen to import goods from abroad. To facilitate their import trade, indigenous businessmen were given priority access to cheap credit (Siahaan 1996:168). As noted above, the *Benteng* programme was primarily aimed at countering the dominance of the 'Big Five' Dutch trading companies in import and export trade.

Protection to the indigenous importers was provided by reserving the imports of specified categories of goods, referred to as *Benteng* goods, solely for indigenous importers, and by channeling credits to these importers through the state-owned BNI Bank Negara Indonesia (BNI) (Sutter 1959:1017-8). The required qualifications for receiving preferential treatment through the *Benteng* programme were, at least on paper, quite stringent.

Choosing import trading as the first major economic activity to promote indigenous entrepreneurship was understandable, as at the time almost all

export and import trade was handled by Dutch and ethnic Chinese firms (Suhadi 1967:218). Focusing on the import trade to secure indigenous Indonesian dominance appeared to be the most feasible option since this line of business was considered the most responsive to state direction through controls over the allocation of import licenses (Robison 1986:44). The import trade was also the most accessible to indigenous businessmen. They could easily set up business with a minimum of overhead investment and concentrate on products sufficiently standardized to require a minimum of business experience, and also specialize in goods that were protected by import restrictions (Anspach 1969:168).

The *Benteng* programme attracted a great deal of interest. While in 1951 some 250 businessmen had registered with this programme, in 1952 the numbers had increased to 741, and to 1,500 in 1953 and to 2,211 in 1954 (Siahaan 1996:68). As a result, the percentage of total government foreign exchange credit allocated to the *Benteng* importers increased from 37 per cent in 1952/3 to 76 per cent in late 1954 (Robison 1986:45). By the early 1950s around 70 per cent of the import trade was reportedly done by indigenous Indonesian businessmen (Burger 1975:171).

Many of the new indigenous Indonesian importers receiving preferential treatment under the *Benteng* programme, lacking capital and/or business experience, engaged in business practices which, although not in violation of the letter of the law, did offend ethical standards. There were of course several other new, capable indigenous importers whose companies grew into viable companies. However, there were many more cases which could hardly be named 'bonafide' enterprises, but rather 'Ali-Baba' enterprises involving indigenous importers and ethnic Chinese businessmen (whether Indonesian citizen or foreign national). Such enterprises in fact proliferated under various forms, such as fronts and strawmen and the selling of import licenses to genuine, mostly ethnic Chinese, importers (Sutter 1959:1027).

The *Benteng* programme failed to foster a strong, self-reliant indigenous merchant class, but rather furthered a group of licensed brokers and political fixers, in short what we now call unproductive 'rent-seekers' or 'rent-harvesters'. These importers were often referred to as 'brief case importers' (*importir aktentas*), whose sole qualification as an importer was that they carried a briefcase (Siahaan 1998:168).

As the *Benteng* programme progressed, it became increasingly apparent that this programme was not effective in nurturing a viable group of indigenous entrepreneurs. To eliminate abuses, Roosseno, the minister of economic affairs from November 1954, introduced a foreign exchange auction system in the textile sector. He also banned discrimination on ethnic grounds, and thus