

## INDONESIA ON THE REBOUND

***RECENT CONSULTING WORK IN INDONESIA LEADS US TO BELIEVE THAT THE COUNTRY IS ON THE REBOUND AND THAT EARLY MOVER ADVANTAGES COULD EXIST FOR THOSE CONSIDERING INVESTING IN THE COUNTRY NOW.***

NOT THAT MANY COUNTRIES HAVE TAKEN HITS AS HARD AS INDONESIA HAS IN RECENT YEARS. THE ASIAN FINANCIAL CRISIS OF THE LATE 1990'S CAUSED SEVERE ECONOMIC AND SOCIAL DISLOCATION. AND THEN, AS INDONESIA WAS BEGINNING TO RECOVER, THE TSUNAMI OF DECEMBER 2004 STRUCK, KILLING OVER 200,000 INDONESIANS.

BUT THERE ARE SEVERAL SIGNS THAT INDONESIA, THE WORLD'S

FOURTH MOST POPULOUS NATION, IS ON THE REBOUND AND HAS THE POTENTIAL FOR SUSTAINED, ABOVE-AVERAGE GROWTH. THE BUSINESS AND GOVERNMENT SECTORS HAVE BEEN UNDERGOING LARGE-SCALE REFORMATIONS, AND THESE EFFORTS ARE BEGINNING TO BEAR FRUIT: THERE IS INCREASING MACROECONOMIC STABILITY, AND THE INTERNATIONAL FINANCIAL COMMUNITY HAS BEGUN TAKING NOTE OF THIS.

### OVERCOMING PROBLEMS OF THE PAST

THE ASIAN FINANCIAL CRISIS AND THE RESULTING SCRUTINY BY INTERNATIONAL FUNDING ORGANIZATIONS FORCED INDONESIA TO CONFRONT CORRUPTION, MISMANAGEMENT, CRONY CAPITALISM, AND WEAK FINANCIAL SYSTEMS. INDONESIA HAD BEEN AFFLICTED BY TOO-COZY RELATIONS BETWEEN BANKS AND CORPORATE BORROWERS AND IT LACKED FINANCIAL TRANSPARENCY IN ITS CORPORATE, BANKING, AND GOVERNMENT SECTORS. ALL

THAT HAS BEGUN TO CHANGE.

UNTIL 1998, INDONESIA HAD BEEN UNDER THE 30-YEAR, AUTHORITARIAN RULE OF PRESIDENT SUHARTO, WITH THE BACKING OF INDONESIA'S MILITARY, WHICH HISTORICALLY HAS INTERVENED AGGRESSIVELY IN INDONESIAN POLITICS. PRESIDENTIAL ELECTIONS FORMERLY WERE DECIDED BY THE PEOPLE'S CONSULTATIVE ASSEMBLY, WHICH HAD BECOME A RUBBER STAMP FOR SUHARTO'S AUTHORITARIAN RULE. THE MILITARY HAD 39 SEATS IN THAT ASSEMBLY.

## RECENT CHANGES

SINCE THEN, THERE HAVE BEEN DEMOCRATIC ELECTIONS, AND NOW THE PRESIDENT, VICE-PRESIDENT, AND ALL MEMBERS OF THE LEGISLATURE ARE DIRECTLY ELECTED BY THE PEOPLE. THE MILITARY'S ROLE IN CIVILIAN POLITICS HAS BEEN SUBSTANTIALLY CURTAILED.

WITH THE ELECTION OF PRESIDENT SUSILO BAMBANG

YUDHOYONO IN 2004, THE TRANSITION TO DEMOCRACY GOT ANOTHER STRONG LIFT. PRESIDENT YUDHOYONO HAS ATTACKED CORRUPTION, ASSERTED CIVILIAN CONTROL OVER INDONESIA'S MILITARY, AND SOUGHT TO IMPROVE THE CLIMATE FOR FOREIGN DIRECT INVESTMENT.

## GREATER MACROECONOMIC STABILITY

THE ECONOMIC AND POLITICAL REFORMS ARE BRINGING RESULTS. THERE WAS ABOVE-AVERAGE GDP GROWTH IN 2005 OF APPROXIMATELY 5%, DRIVEN BY CONSUMER CONSUMPTION, GROWTH IN FINANCIAL SERVICES, AND OIL AND GAS AS WELL AS OTHER COMMODITY EXPORTS. THERE IS A HIGH PROBABILITY THAT A SIMILAR GROWTH RATE CAN BE ACHIEVED IN 2006.

AS IT CONTINUES TO PROGRESS, INDONESIA IS HELPED BY THE FACT THAT ITS ECONOMY HAS A BEDROCK, WHICH IS THE NATION'S WEALTH OF NATURAL RESOURCES. INDONESIA IS THE ONLY SOUTHEAST ASIAN MEMBER OF THE ORGANIZATION OF PETROLEUM EXPORTING COUNTRIES (OPEC), AND IT IS A LARGE EXPORTER OF LIQUEFIED NATURAL GAS (LNG) AND OF THE HIGHEST GRADE PETROLEUM.

WITH RECENT ADVANCEMENTS IN ITS ECONOMY, INDONESIA'S MACROECONOMIC STABILITY HAS IMPROVED, THE FEDERAL BUDGET HAS BEEN BALANCED, AND INTEREST AND INFLATION RATES HAVE BEEN TRENDING DOWNWARD. IN TERMS OF THE PERFORMANCE AND TRANSPARENCY OF INDONESIA'S FINANCIAL SECTOR, THERE HAS BEEN A TREMENDOUS IMPROVEMENT IN BANKING, PARTICULARLY IN TERMS OF CAPITAL ADEQUACY, NON-PERFORMING LOAN, AND RETURN ON ASSET RATIOS.

THE INTERNATIONAL FINANCIAL COMMUNITY HAS BEGUN TAKING NOTE OF THESE ADVANCEMENTS. FOREIGN DIRECT INVESTMENT (FDI), MEASURED ON AN "APPROVED" BASIS BY INDONESIA'S INVESTMENT BOARD, NEARLY DOUBLED IN 2005, TO \$8.9 BILLION, AN AMOUNT EXCEEDING THE FDI OF MUCH LARGER INDIA, WHICH IS THE

STAR OF THE OUTSOURCING SCENE. IN ANOTHER MEASURE OF INDONESIA'S STRENGTHENING ECONOMY, THE RUPIAH ROSE NEARLY 8% AGAINST THE DOLLAR IN THE

FIRST QUARTER OF THIS YEAR, AND MOODY'S AND STANDARD & POOR'S HAVE ISSUED POSITIVE OUTLOOKS FOR INDONESIA'S SOVEREIGN CREDIT RATINGS.

## A SHIFT IN PERSPECTIVE BY AMERICAN COMPANIES

THIS UPWARD SWING IN INDONESIA'S FORTUNES AND ITS MORE FAVORABLE BUSINESS CLIMATE HAS CAUGHT THE EYE OF U.S. MULTINATIONALS. THE PRESIDENT OF THE U.S.-ASEAN BUSINESS COUNCIL DELEGATION THAT VISITED INDONESIA EARLIER THIS YEAR SAID THAT, "THE GOVERNMENT HAS FOUND ITS DIRECTION AND IS BEGINNING TO TAKE IMPORTANT ACTIONS TO ENCOURAGE INVESTMENT HERE. IT IS THE RIGHT TIME TO LOOK AT INVESTMENT OPPORTUNITIES IN INDONESIA." ECHOING THIS PERSPECTIVE, A COCA-COLA EXECUTIVE WHO WAS A MEMBER OF THIS VISITING COUNCIL SAID, "WE HAVE BIG PLANS FOR INDONESIA. [WE PLAN TO INVEST] MILLIONS AND MILLIONS OF DOLLARS [OVER THE NEXT FIVE YEARS]." AFTER ACCOMPANYING A SIMILAR DELEGATION OF BUSINESS PEOPLE TO THE COUNTRY, THE CHAIRWOMAN OF THE AMERICAN CHAMBER OF COMMERCE IN SINGAPORE SAID, "INDONESIA IS A VERY IMPORTANT COUNTRY IN THE REGION, AND IT IS AN AREA WITH A LOT OF OPPORTUNITIES AND INTEREST FOR OUR

MEMBERS."

THE U.S. GOVERNMENT IS ALSO STEPPING UP ITS COURTSHIP OF INDONESIA, WHICH IT PERCEIVES AS AN IMPORTANT STRATEGIC PARTNER IN SOUTHEAST ASIA. DURING THE VISIT TO INDONESIA OF SECRETARY OF STATE CONDOLEEZA RICE IN MARCH OF 2006, MS. RICE AND THE INDONESIAN FOREIGN MINISTER, HASSAN WIRAJUDA, USED THE PHRASE "STRATEGIC PARTNERSHIP," WHICH FROM THE AMERICAN SIDE REFLECTS A DESIRE FOR INDONESIA GROW INTO A MAJOR ECONOMIC AND MILITARY POWER IN SOUTHEAST ASIA AND THEREBY ACT AS A COUNTERWEIGHT TO THE INFLUENCE OF CHINA IN THE REGION.

WARMING RELATIONS APPEAR TO BE HAVING AN EFFECT ON THE BROADER POPULATION. PARTLY AS A RESULT OF AMERICAN HELP AFTER THE TSUNAMI OF DECEMBER 2004, IN WHICH THE U.S. PROVIDED \$400 MILLION IN OFFICIAL AID, APPROVAL RATINGS FOR THE U.S. HAVE RISEN TO 50 PERCENT, ACCORDING TO SOME OPINION POLLS.

## THE MAGELLAN ALLIANCE

*WE BRING THE  
WORLD TO WORK  
FOR YOU*

---

CONTACT US:

MR. TULLY MOSS

PRESIDENT

203-261-7731

[tully@magellanalliance.com](mailto:tully@magellanalliance.com)

---

## PROGRESS AND POTENTIAL

THE IMPROVED RELATIONS ARE BEARING FRUIT FOR AMERICAN COMPANIES. PHILIP MORRIS RECENTLY ANNOUNCED ITS INTENTION TO ACQUIRE, FOR \$5.2 BILLION, THE INDONESIAN TOBACCO COMPANY HM SAMPOERNA. IN AN EVEN MORE SIGNIFICANT INDICATION OF THE REFORM-MINDED RESOLVE OF PRESIDENT YUDHOHONO, A MULTIYEAR DISPUTE BETWEEN EXXONMOBIL AND THE STATE-RUN OIL MONOPOLY, PERTAMINA, HAS BEEN RESOLVED. RESOLUTION OF THE DISPUTE CLEARS THE WAY FOR DEVELOPMENT OF INDONESIA'S LARGE CEPU OIL FIELD.

THE TREND LINES FOR BUSINESS IN INDONESIA ARE CLEARLY POSITIVE, BUT U.S. MULTINATIONALS ARE INDICATING THAT THERE ARE SEVERAL KEY ISSUES THAT REQUIRE ONGOING GOVERNMENT VIGILANCE, INCLUDING BUDGET DISCIPLINE, ANTI-CORRUPTION INITIATIVES, AN END TO THE REBELLION IN RESOURCE-RICH ACEH PROVINCE, AND THE CREATION OF LEGAL CERTAINTIES AND A RESPECT FOR THE SANCTITY OF CONTRACTS. THERE IS ALSO THE ONGOING NEED TO ENSURE THE SECURITY OF COMPANY FACILITIES AND PERSONNEL,

WHICH THE GOVERNMENT RECOGNIZES AND HAS BEEN ACTIVELY WORKING ON. A CASE IN POINT IS ITS SUPPORT OF FREEPORT-MCMORAN, WHICH RUNS THE WORLD'S LARGEST GOLD AND COPPER MINE IN WEST PAPUA, THE EASTERNMOST PROVINCE IN INDONESIA. THIS FACILITY HAS BEEN THE TARGET OF VIOLENT PROTESTS FROM THE LOCAL POPULATION. THE YUDHOYONO GOVERNMENT HAS SIGNALLED THAT IT WILL SUPPORT FREEPORT IN MAINTAINING THE SECURITY OF THE MINE.

ALTHOUGH INDONESIA IS NOT OUT OF THE WOODS YET, IT CLEARLY IS ON THE REBOUND. EARLY MOVERS AMONG MULTINATIONALS AND THE INTERNATIONAL FINANCIAL COMMUNITY HAVE TAKEN NOTE AND ARE SECURING WHAT COULD PROVE TO BE ADVANTAGEOUS POSITIONS. THOSE THAT HAVE A LONG-TERM VIEW AND ARE WILLING TO CONFRONT THE INEFFICIENCIES AND RISKS THAT STILL EXIST IN INDONESIA, THOSE SEEKING TO BE A PART OF AN EARLY-MOVER GROUP, WILL LOOK AT INDONESIA AS AN OPPORTUNITY TO CAPITALIZE ON THE COUNTRY'S UPSWING AS ITS ECONOMY REBOUNDS.

## ***ABOUT THE MAGELLAN ALLIANCE...***

*THE MAGELLAN ALLIANCE IS A CONSULTANCY THAT ASSISTS COMPANIES IN NAVIGATING INTERNATIONAL MARKETS. ASIA, EUROPE, AND NORTH AMERICA ARE THE PRIMARY GEOGRAPHIC SECTORS IN WHICH WE OPERATE. OUR PERSONAL EXPERIENCE HAS INVOLVED CONSULTING WORK IN APPROXIMATELY 30 DIFFERENT INDUSTRIES. RECENT ENGAGEMENTS HAVE BEEN IN THE INSURANCE, FINANCIAL SERVICES, AND HUMAN RESOURCES SERVICES SECTORS. FOR FURTHER INFORMATION ABOUT OUR FIRM, PLEASE VISIT OUR WEB SITE: [www.magellanalliance.com](http://www.magellanalliance.com).*