

Regulatory Reform in Indonesia (1983-2000)

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Indonesian economy has changed radically since last two decades. In 1960's and 1970' Indonesia was categorized as very poor country, and then significantly moved toward semi-industrialised country in 1980's and 1990's. There were many difficulties in reforming the society and the economy. It was working within two decades and now Indonesia has been challenged with economic and financial crisis since 1997.

This paper describes at least five issues, *i.e.* economic reform from inward looking to outward looking, reform on investment system, trade reform, competition law, and prohibition of monopoly practices by KPPU. These five issues are important in the economic system as the main policies since 1983 that makes Indonesian economy growing.

1. REFORM FROM INWARD TO OUTWARD LOOKING

Indonesia has changed its economic policy and strategy from inward looking to outward looking since two decades ago. Before 1983, the industry was developed merely for domestic need in line with development strategy at that time. Fertilizer, iron, shipping industries and others were constructed based on government initiatives without considering their competitiveness (government driven). The need to develop industry was judged only by opinion of the minister, president, and other policy makers. There was no consideration from aspect of the market.

The government took dominant roles for developing industry using windfall profits from oil. It was made possible because of oil, the largest income in the national budget in those decades. The centralistic system was also supportive in deciding such inward looking policy. Central government had significant roles in many sectors of the economy.

Therefore, those industries had to be protected with certain level of tariff for their survival. The output of this strategy was inefficient industries which were dependent on the government protection. They could not compete with other similar industries in the international market. Therefore, this strategy was fail and not sustained because more burden and more subsidies in the national budget.

In the beginning of 1980's, the oil price was very unstable and tended to decrease continuously. This made the government income decreased fast. Therefore, it was not possible for the government to depend only on oil export and easily develop inefficient industry which could not compete in the international market. Other potential industries must be developed, but not possible to be supported by inward looking strategy.

In 1983 the government has started to transform its strategy toward export oriented by reforming step by step almost regulatory system in relation at least in many economic areas, *i.e.* trade and industry, investment, financial and fiscal system.

2. REFORM ON INVESTMENT

In 1985, the government has launched an economic policy package to simplify the application and procedure for foreign direct investment. Bureaucracy in Indonesia was very complicated and became significant barrier for business, investors, and companies. It was therefore difficult to compete in the international market with the existing bureaucracy which created a very high transaction cost. Reform for promoting investment was started by reforming bureaucracy and its regulatory system.

Complicated procedure was demolished and replaced by the simple one. The objective of this reform was to support more inflow of investment and more foreign investors coming to Indonesia. Other objective was to make Indonesia more attractive for both domestic and foreign investors.

This policy was then recognized to have successful impact to limit the document involved in the process. Another positive impact was an increasing investment application to Indonesia from abroad. The procedure was then more and more simple and more conducive for investment climate.

To support this strategy, the government has expanded the reform to improve the export credit scheme for local exporters as well as joint venture companies in Indonesia. Reform had an impact in increasing export activities and more business involve in exporting their product in international market. They needed support from banking sector. Then, the government took initiative to facilitate them with export credit from State Owned Banks.

The government opened again more areas in investment activities. The foreign investors were invited to invest in retail and distribution system in Indonesia. This area of investment was opened in 1985. The impact could be identified in increasing activities of foreign investor in national trading system. This was launched because of higher level of confidence toward Indonesian economy in the middle of 1980's.

The regulatory reform was continued by simplifying system of custom procedure. The government decided to free an entrance visa for 29 countries which were recognized had an intensive economic relation with Indonesia. In this year tax for capital good imported from other countries was removed for the purpose of more export orientation activities among the business actors.

In 1986, the government has devaluated Rupiah for about 30%. Rupiah was considered over valued, which made Indonesian products could not compete with other products from many countries. This policy was decided to further support export orientation strategy and to get more comparative advantage for Indonesian products.

Further deregulation was continued by opening stock market for foreign investor. Capital inflow in the middle of 1980's increased significantly in Indonesia as Indonesian economy was opened to the world market. Therefore, it was the time to open the modern stock market system in Jakarta to attract more foreign investor indirectly. The results, in the end of 1980's competition in many areas increased significantly.

In 1988, the shipping industry was further deregulated by inviting foreign investors to involve in this industry. Before 1988, this industry was closed to only state owned companies. Shipping industry was closed for only domestic investors or government.

More deregulation was implemented in which joint venture company was also allowed to distribute the product in local market. Distribution system was opened to foreign investor, especially to distribute their products. The implication of this deregulation significantly increased competition in domestic market. In 1989, the government still continued to improve the investment climate. More negative investment lists were reduced to allow more investors come to Indonesia. Certain sectors or sub-sectors were not exclusively given to certain persons, less discrimination and more areas were opened to investors.

Furthermore, the government started to reform state owned enterprises. More state owned companies were listed in stock market which meant more control from the public and more transparent. Opening the economy continued (1989) in which the government allowed maximum 49% of non-banking companies in stock market.

State owned companies was further included in the reform in 1989 to increase their efficiency level, especially 75 SOE's. This policy did not significantly change the SOE's but slightly increase productivity and selling in those companies.

In 1990, more investments areas were opened to the domestic and foreign investors. About 75 negative lists of investments were reduced to only 60 lists. Licence for land use was also allowed to foreign investors so that there was no barrier to implementation of direct investments (Presidential Decree 32/1992). This policy means opening more investment opportunities in Indonesia in line with the objective of economic reform in 1980' and 1990's.

One year later, about 10 areas of negative lists were removed from the government regulation, such as palm oil industry, block board, rattan industry, motor vehicle, cigarettes, gas lighter, medicine formula). More public sector were further opened by the government to foreign investors, such as harbour, telecommunication, water, mass media, etc (Government Regulation 20/1994).

3. TRADE REFORM

In period of 1970-80, economic policy could be categorized as inward looking strategy. The government utilized almost windfall profits from oil for development as well as to develop industries (government driven). The government income mostly depended on oil and gas export. Meanwhile, income from non-oil and gas product was not significant.

In the end of 1970's or the beginning of 1980's, that policy was recognized not to have significant improvement on industries and not sustained because more subsidy was expended from the government budget. The competitiveness of industry was also stagnating which means difficult to compete in the international markets. Furthermore, oil price in the international market was fluctuating which made more uncertain for the government income and budget.

Based on this reason, the government considered to strengthen the national economy by changing the strategies and policies. The inward looking strategy was left and the outward looking strategy was chosen. The economy was opened to the market system to make industries more efficient and to compete in the international market. Protection was lowered to make the market working and more competition in the business.

Trade deregulation was started in the beginning 1980's. It was done by removing entry barrier from bureaucracy. Export orientation policy needs more effective support from bureaucracy, especially custom. The policy makers had serious difficulties in such bureaucracy which became critical barrier in the economic activities. Custom had a negative performance which influenced business negatively.

Therefore, in 1985 government decided to privatize custom services by replacing custom office with SGS (Switzerland). It was a radical decision done by the government for the shake of economic reform. This had an increase in confidence which further indicated that the government was very serious in deregulating economic system as a whole. Indonesia became more attractive for domestic and foreign investors.

In 1985, the government also improved system procedure in shipment and also simplified handling system in harbour. This policy was able to reduce inefficiency in export and import activities. The government further improved the system in custom office because trade reform had an indication to increase non oil export activities. Reform had a good response from business and investors with more orientation toward international market.

Tariff system was slowly harmonized too and reduced significantly to make more competition. This was implemented by the government as core policy. Protection was not able to increase competitiveness in industry. It was continuously done to get more positive effect of the market and more competition.

In 1987, import licence was also improved by reducing bureaucratic procedure. The process was made simple to create more significant improvement of import activities, specifically for import in raw material and capital goods. These two products were important for industries and exports.

Import quota was reduced significantly to get more participants and more competition in this business. Monopoly in import of steel and iron as well as plastics was also demolished. Many import licences had been given to monopolists, then deregulated by opening that activities for any investors which were interested to involve.

Trade reform was further implemented to the medical industry and animal husbandry. Tariff and non-tariff barriers were removed in those industries to increase competition, to improve investment climate, and to increase government credibility

In 1990, the government continuously decreased and harmonised tariff system. Tariff of many products were reduced significantly which made Indonesia as an opened economy. Non-tariff barriers were also reduced to make more competition among the industries.

In 1999, Indonesia has started to implement new law, called competition law. The commission was able to demolish cartel system in air transport. At present, airline is in full competition which makes ticket price decrease radically to almost 35% level. Number of Passenger increases significantly more than twice within two years. Domestic market is now being more intensive, dynamic and supportive because of air ticket price much cheaper.

4. REFORM IN COMPETITION LAW

Fairness in business activities was in big question before implementation of the Competition Law. Business opportunity was not distributed equally among all level of business actors. The government of Indonesia under the past regime created unfair business and developed crony capitalism in almost sectors of business. Further, economic growth was followed by raising market distortion. The government policies just give the opportunity only to a small group of business actors.

The business actors who had been closed to the ruling elite acquired excessive facilities that created an opportunity gap in business. This condition improved the growing of conglomerates and caused the economy to be very fragile and unable to compete. There were many corners of privileges in the business which then indicated the need of fairness and regulatory reform in the system.

The House of Representative of the Republic of Indonesia has taken the initiative to draft the Competition Law. This was the first law that was initiated by the House of Representative after more than 30 years it has never initiated a law). As the result, in March 5, 1999 the Government of Indonesia has enacted Law No. 5 of 1999 concerning Prohibition of Monopolistic Practice and Unfair Business Competition and it took into effect on September 5, 2000.

The main objective of the Indonesian Law No.5 of 1999 is to increase the national economy efficiency as one of the efforts to increase the people's welfare and to establish a conducive business climate through the arrangement of fair business competition, thus guaranteeing the certainty of equal business opportunities for large, middle, and small business actors in Indonesia. Furthermore, the other objective is to prevent monopolistic practices and unfair business competition caused by business actors, as well as to create effectiveness and efficiency in business activities.

To supervise the law, an independent body was established, called KPPU (The Commission for Business Competition). The KPPU is responsible for supervising the execution of the Law. The independency means free from the influence of the government and other parties. The commission is responsible to the President of the Republic of Indonesia and the people of Indonesia through the Parliament (DPR "House of Representative).

First main duty of the Commission is conducting evaluation of agreements, business activities or actions of business actors, and whether there is not any abuse of dominant position that could result in the occurrence of monopolistic practices and/or unfair business competition. The second is providing policy suggestions and consideration on government policies regarding monopolistic practices and/or unfair business competition.

Since 2000, the commission has received hundred reports from the public and/or business actors concerning presumption of the occurrence of monopolistic practices and/or unfair business competition. The commission has also started to role its function by conducting research on presumption of any business activities and/or actions of business actors that cold cause monopolistic practices and/or unfair business competition. Investigations have been conducted on presumed cases of monopolistic practices and/or unfair business competition reported by the public or by business actors or discovered by the Commission as result of its investigation. And sanctions have been imposed in the form of administrative sanctions to the business actor who is violating provisions in this Law.

5. MONOPOLY PRACTICES: CASES IN KPPU

Since 1999, the Commission has handled some cases, as follows:

- 1) The Decision of Commission No. 01/KPPU-L/2000 on tender casing and tubing of PT Caltex Pasific Indonesia. This was a case of unfair bidding. The commission then nullify the bidding and order re-bidding.
- 2) The Decision of Commission No. 03/KPPU-L-I/2000 on retail business activity of PT Indomarco Pristama. Competition in retail business is very intensive which influences the traditional market. Modern retail businesses enter many corners of the cities in Indonesia then create complaint from traditional traders. The commission decided to protect traditional market and gave policy advice to the mayors and governors to improve city plan and protection for traditional market as a part of the system.
- 3) The decision of Commission No. 07/KPPU-L-I/2001 on tender procuring of importing cow in East Java. The bidding was decided to be unfair and the project leader (bidder) in bureaucracy must be replaced by others.
- 4) The Decision of commission No. 03/KPPU-I/2002 on tender offering for PT Indomobil Sukses International. The bidding was nullified, but the court allowed the winner to get it.
- 5) The decision of commission No. 09/KPPU-L/2002 on tender in PT (Persero) Telekomunikasi Indonesia
- 6) The decision of Commission No. 08/KPPU-L/2001 on tender procuring barite and bentonite in YPF Maxus Southeast Sumatra B.V. Company.
- 7) The decision of Commission No.10/KPPU-L/2001 on Insurance company in PT Bank Negara Indonesia (Persero) Tbk. PT BNI was ordered to open its market for insurance companies.
- 8) The Decision of Commission No. 02/KPPU-I/2002 Cartel of Day Old Chick Company.
- 9) The decision of Commission No. 01/KPPU-I/2002 on work sharing PT siemles Pipeline and PT Citra Tubindo. The bidding system was recognized unfair and the commission ordered to improve it.