

REAPING THE BENEFITS OF REFORM

Business Advantage asked Miranda Goeltom, Senior Deputy Governor of Bank Indonesia—the country's central bank—for her perspectives on the banking sector and the outlook for economy.

The Indonesian Government has cut its subsidy of domestic fuel prices. Clearly, this will affect growth in the Indonesian economy. What are Bank Indonesia's predictions?

The economy will grow by 6.1% this year. It is lower than predicted earlier in the year, but it has grown by quite a remarkable amount since the 1997 crisis. Only last year we had 6.5%. It has gone down, but other countries in the region have had to revise down their GDP more harshly. We are struggling very hard to keep inflation to the lower teens.



BI'S MIRANDA GOELTOM

The central bank is required to retain price stability.

The Indonesian economy is still performing strongly?

On the exchange rate side, if we look at the balance of payments, we are still posting a surplus. Our liquid reserves are still a handsome US\$558.7 billion. The central bank is trying to recycle some of the foreign exchange receipts from oil back to the market to reduce the pressure, and yet our exchange rate on average is still appreciating. This situation—soaring food prices and commodity prices in the world, plus a decline of the subsidy from the Government—means inflationary pressures are mounting. The central bank will have to respond to give a signal that we are concerned, and that we want to reduce inflationary expectations.

Oil and commodities get the headlines, but how are other areas of the Indonesian economy performing?

Q1 growth this year was 6.3%, due not only to mining but transportation, telecommunications, agriculture, manufacturing and trade. It remains to be seen whether the secondary wave of inflation and increasing fuel prices will temporarily halt the speed of growth. I don't see a decline, however.

The world economy has also been affected by the US subprime mortgage crisis. How will this impact on Indonesia?

One very important thing to note is that our economy in general isn't affected so much by subprime issues, or rising commodity prices. Firstly, because we are the producers of some of the commodities benefiting from increased prices and, more importantly, because our banking system is very strong, very resilient. We have learned the lessons from the 1997 crisis. We have imposed a very prudent regulatory framework.

Given the increased supervision, are Indonesian banks lending?

Banks are lending—the credit growth was 28% until March 2008 on a year-on-year basis. A growth of 28% in the midst of this global meltdown is quite alarming, so we have already given a warning to banks that they will have to be careful with lending. Luckily, our bankers and the banking system are still way behind in product innovation compared to the banking system in the western world. Our products are very traditional and the risk is less. That is one of the reasons we are quite optimistic that we won't have too much of a problem. That doesn't mean that we won't be hit if the slowdown

in the world economy is prolonged and the oil price rise continues. But we have done a stress test on the banking system, a very severe stress test, and we haven't seen that the bank will be affected.

Reducing the number of banks is a stated goal in reforming Indonesia's banking sector. How is this progressing?

We have made quite a bit of progress in cutting the number of banks in half from 253 banks to 130, and now 118 banks. We want to reduce it as much as possible so that it is manageable for supervision and also because we think that competition is going to be fierce in the future. Banks are going to have to have a strong capital base, good quality in human resources and high IT infrastructure. Mergers have already started.

What opportunities are there to invest in the banking sector?

We are classed as one of the most liberalised countries as far as openness of the banking structure is concerned. We allow foreigners to own 99% of any Indonesian bank. We have seen some of our small banks bought by foreign banks. They are aiming to grab lucrative, solid and strong businesses. Their non-forming loans are very low—about 2%. We welcome owners of foreign banks because we hope they will bring money, networks, businesses and good people to work here.

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Finally, how do you see the prospects for the Indonesian economy in the medium term?

I am extremely positive about the Indonesian economy. We have seen growth of 5.5% over the last five years—not due to any authoritarian or dictatorial ruling but in the midst of democracy, with all its benefits and disadvantages. We could be running much faster.

Firstly, the Anti-Corruption Commission (KPK) is something that we have to welcome. Secondly, the Government has been very determined to improve infrastructure. In 2005 we had this infrastructure summit, but only a few projects have been implemented since. Will this be the case in five years? I don't think so. We'll see regions that have proper funding. They will recruit professionals and good bureaucrats to run the economy. Given their power, their money and authority, I think the regions will grow stronger than they are today.

Thirdly, we have ample, very diversified natural resources. I foresee there will be better regulations and these resources will better benefit the whole economy. Fourthly, but not least, democracy is going to be more mature and more balanced, in terms of understanding not only rights but also responsibilities.

Hence, I am looking forward to a world where most of the sectors in Indonesia are very much open to market price mechanics.

Although all these factors will only work if the last is there: political stability. And I think we now have that. ■