High inflation follows Indonesian president's fuel price hike

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18 November 2005

A surge in prices and interest rates has followed the Indonesian government's October 1 reduction in the fuel price subsidy. The sharp rise in the costs of essential goods and services constitutes a severe attack on the living standards of the archipelago's impoverished urban and rural poor.

Yet, big business and financial market commentators have applauded president Susilo Bambang Yudhoyono's subsidy cut. The move is the most significant along these lines since the International Monetary Fund (IMF)-inspired economic restructuring that led to mass protests and the toppling of the Suharto military-backed dictatorship in 1998.

During October, prices rose 8.7 percent. The cumulative rise in inflation for the first 10 months of 2005 was 15.65 percent. Jakarta's statistical office put the increase in transportation and communications costs for October at 29 percent. In response to the surge in inflation, and in the international context of rising US interest rates, the central Bank Indonesia lifted its key interest rate 1.25 percent to 12.25 percent on November 1. The increase was the fifth in nine weeks and has pushed interest rates to their highest level for three years.

The general rise in prices flowed directly from the government's capping of its oil price subsidy at $US8.65 billion for 2005. Jakarta was under enormous pressure to act on the fuel subsidies. High world oil prices threatened to blow the cost of the subsidy out to $US14 billion and consume as much as one-third of all government expenditure. Even with the increases, the domestic price is still 60 percent below international levels.

The government is attempting to play down the effects of the price and interest rate rises. The chief of the Yudhoyono cabinet's economic team, Coordinating Economics Minister Aburizal Bakrie, repeated the official line that the price surge was a one-off occurrence and that its inflation forecast of 7 to 8 percent for 2006 was still valid. PT Bank International Indonesia chief economist Ferry Latuhihin was quoted on the *Bloomberg* web site as saying inflation in 2006 may be 8.5 percent.

There is no relief in sight for the Indonesian masses. The regulatory changes have led to petrol prices increasing by 87.5 percent and diesel fuel by 104 percent, while kerosene, the main cooking fuel of Indonesian's tens of millions of poor, has soared by 186 percent.

Furthermore, the compensation package for the poor is utterly inadequate. The payment of 100,000 rupiah per month ($US10) only applies to families earning less than 175,000 rupiah a month ($US17.50), which means that millions of families living on less than $US20 a month receive nothing to offset the dramatic rise in the cost-of-living. At least 17 percent of the country's 220 million people are unemployed or underemployed and 40 million live on $US2 a day or less.

The Indonesian ruling elite is haunted by the prospect of the type of mass revolt over fuel prices that played a large part in bringing down the Suharto regime.

Thus far, the government has not been confronted with large protests. Some media commentators, by way of an explanation, somewhat disingenuously point to the popularity supposedly enjoyed by Yudhoyono, a Suharto-era general who is commonly referred to as the country's "first directly elected president". Yudhoyono received 60.9 percent of the vote in the 2004 election, defeating Megawati Sukarnoputri.

Yudhoyono's administration has been given a breathing space not by the election result of 2004, however, but by the betrayals of the so-called "reformers". Megawati of the Indonesian Democratic Party-Struggle (PDI-P) and Abdurrahman Wahid of the National Awakening Party were among those who posed in 1998 as opponents of the corrupt ruling elite and Suharto. When they came to power in the aftermath of Suharto's fall, they dashed the hopes of the working class and poor for improvements in living standards and democratic rights.

As president, Wahid ensured that no significant Suharto-era figure was called to account for the crimes of the dictatorship. From 2000 on, Megawati and the PDI-P and other so-called reformers collaborated with Suharto's

Golkar Party to remove Wahid and create a new administration even more committed to protecting the interests of the Indonesian ruling elite.

Megawati's cabinet presided over brutal crackdowns against separatist rebels in Aceh and West Papua and made the first attempt to impose fuel subsidy reductions in 2002, but had to retreat due to mass protests.

Disillusionment with the "reformers" and the political alienation among large sections of the population provided the ruling elite with the opening to bring Yudhoyono into the presidency in the 2004 election. Yudhoyono conducted a populist campaign, labeling himself an "independent" and making vague promises of improved living standards. Since assuming office, however, he has worked to implement the demands of the IMF for further economic restructuring and sought to strengthen Indonesia's military and political relations with the Bush administration and the Howard government in Australia.

As the full effects of government policy begin to bite, however, there are signs that the political backlash feared in ruling circles is developing. A survey conducted by Lingkaran Survey Indonesia following the fuel price rises showed that the approval rating for Yudhoyono and his vice president, Golkar chairman Yusuf Kalla, fell to 52.4 percent from its high point of 79.7 percent in November last year.

The developing popular discontent is being reflected in the political establishment. Annis Matta, secretary-general of the Prosperous Justice Party (PKS), a partner in government with Yudhoyono, told the *Jakarta Post* on November 8 that the party was under pressure to withdraw from the coalition. Matta said these demands were coming from PKS regional chapters and supporters because of the fuel price rises.

There have been calls for Yudhoyono to sack his economic ministers. Ikrar Nusa Bhakti of the Indonesian Institute of Sciences told the *Jakarta Post* on November 7 that Coordinating Minister for the Economy Aburizal Bakrie, Finance Minister Yusuf Anwar and Trade Minister Mari Pangestu should be replaced because they were seen as responsible for peoples' hardships. He warned that "a majority of the people affected by the fuel price hike won't wait much longer".

At the same time, however, the government is under pressure from business circles to ignore any discontent and push forward with more restructuring in order to attract foreign investment and shore up corporate profitability.

The higher lending rates that will follow the central bank's interest rate rise are likely to cut consumer purchasing power. Domestic consumer demand was one of the main factors behind the 5.8 percent growth in the $US258 billion economy this year. High interest rates will also have an adverse effect on the state budget because of the government's large domestic debt, with each rise adding to the interest bill.

The higher interest rates will also make stabilising the exchange rate more difficult. On August 31, the Indonesian rupiah fell sharply to 11,800 to one US dollar, before recovering to around 10,000. An unstable rupiah undermines efforts to attract more foreign investment, which declined in 2003-2004 to the lowest levels since the 1970s.

In order to attract investment, the government has reduced charges for handling containers. Big business is calling for more changes, including cuts to tariffs, customs regulations, transportation taxes and charges, and massive infrastructure improvements.

An editorial in the *Jakarta Post* on October 18 entitled "Strong political mandate, weak economic performance" summed up the failures of Yudhoyono's first year in office. It described his cabinet as an "uncomfortable mix of technocrats and politically-connected businessmen".

The cabinet, it noted, had failed to meet Yudhoyono's promise to resolve a high profile legal dispute with the Mexican Cemex company over its attempt to buy a large stake in an Indonesian cement company. There are also ongoing disputes with the American companies, Karaha Bodas, Exxon Mobil and Newmont.

The newspaper, which speaks for powerful sections of Indonesia's economic elite, opined that the government's inaction was "further validating the notion that Indonesia is an unpredictable place to do business". It pointed out that only five of the 90 infrastructure projects the government had identified as urgent at a summit in January had been taken up by private investors.

The editorial concluded by noting the "low trust" the market has in Yudhoyono's economic team and its "perceived conflicts of interest". IT also called for a cabinet reshuffle.

All indications point to the relative political stability of Yudhoyono's first year in office evaporating over the coming months. A clash with the country's poor is looming as the government comes under pressure to meet more of the demands of big business and transnational capital.