REVIEW OF ECONOMIC DEVELOPMENTS

Opportunities and Challenges at the Beginning of the Political Year

AUDREY SOEDJITO AND DANDY RAFITRANDI

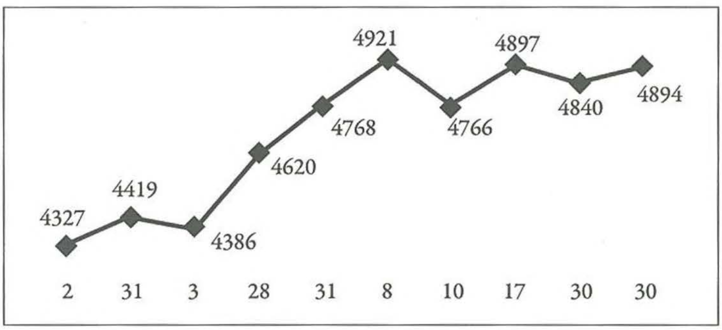
THE FIRST QUARTER OF 2014 witnessed the beginning of the election year, with the legislative election taking place in April. Possibilities of political instability after the parliamentary election, and towards the presidential election, will have consequences on the economy. The first quarter of 2014 also witnessed the issuance of the new trade law and industry law, which add to a long list of trade protection measures deployed by the Indonesian government. Meanwhile, the Central Bank of Indonesia (BI) also continues its tight monetary policy, keeping the interest rate at 7.5%.

Nonetheless, there are signs of recovery of Indonesia's economy, which is first reflected by the movement of the Jakarta Composite Index (JCI) during this quarter. After a steady decline of the index beginning of May 2013, the index has been moving in a positive direction since January 2014. The JCI closed higher at 4418.76 by the end of January 2014, in

***Audrey Soedjito** and **Dandy Rafitrandi** are research staff at the Department of Economics, Centre for Strategic and International Studies*

comparison to the end of December 2013 (4274.18), and January 2013 (4346.48). By the end of February, JCI reached a higher level at 4620.22 as improving trade deficit, appreciation of Rupiah and moderate inflation rate returns investors' confidence in Indonesia's economy. The positive growth of JCI continued until the legislative election in April. Although the JCI recorded a significant downturn to 4766 on the 10th of April 2014 (a day after the election), it bounced back straight away the day after (Figure 1) and thus the effect of legislative election on JCI seems to be temporary and insignificant.

Figure 1. Jakarta Composite Index 2014



Source: Indonesia Investment (JCI), available at http://www.indonesia-investments.com/finance/stocks-bonds/jakarta-composite-index-ihsg/item887

In contrast to 2013, the first quarter of 2014 witnessed the strengthening of Rupiah from February to March, an improvement in the current account deficit, as well as maintained inflation within targeted range. Healthy recovery of the current account in the first quarter is evident from the decrease of the current account deficit to 4.2 billion US Dollar (USD) this quarter, from a deficit of 4.3 billion USD last quarter (Table 1), which was attributed to the decrease in services and income deficits, as well as to a contraction of overall imports. However, the improvement of current account deficit is not due to the improvement of exports performance, as both exports and imports are decreasing. Meanwhile, the increase in surplus of direct investment account is attributed to substantial decrease in the investment outflows, rather than substantial growth of Foreign Direct Investment (FDI). Improvements in Indonesia's economic fundamentals have led to robust portfolio inflows in stocks and bond market reflected in the large surplus of portfolio investment account. Nevertheless, the slowdown in FDI is reflected in the smaller surplus in financial account. Overall, Indonesia's balance of payment (BOP) account recorded a 2.1 billion USD surplus during the first quarter of 2014, which is a 50% decrease in surplus from the last quarter of 2013. Although the BOP surplus this quarter was much lower than the surplus of 4.4 billion USD in the previous quarter, this prolonged trend of BOP surplus is to be viewed positively, especially after continuous deficits of BOP during the first three quarters of 2013. In addition, foreign reserves have started to catch up to the previous high level on January 2013 due to among many other factors the issuance of global bond of USD 4 billion in January 2014.

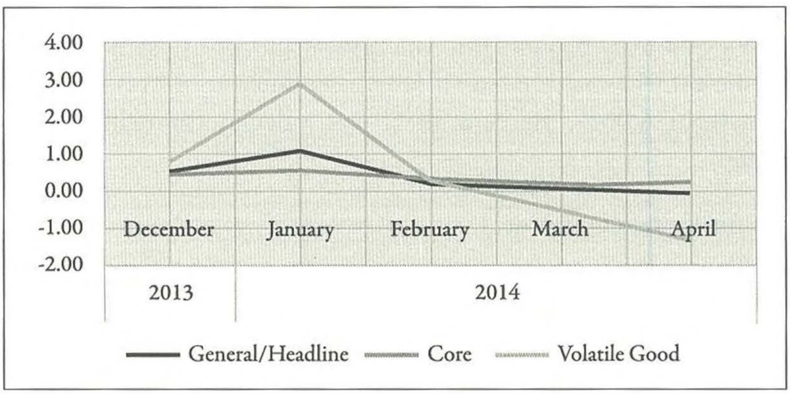
Table 1. Indonesia's Balance of Payment (in billion USD)

	Mar-13	*Jun-13*	*Sep-13*	*Dec-13*	*Mar-14*
CURRENT ACCOUNT	**-6.0**	**-10.1**	**-8.6**	**-4.3**	**-4.2**
Exports	45.2	45.6	44.1	48.4	44.4
Non-oil & gas	36.8	37.6	35.6	39.7	36.7
Oil & gas	8.5	7.9	8.5	8.7	7.7
Oil	4.3	4.2	4.8	4.5	3.6
Gas	4.2	3.7	3.7	4.1	4.1
Imports	43.6	46.1	44.0	43.7	40.9
Non-oil & gas	32.3	36.1	32.8	32.9	30.5
Oil & gas	11.3	10.0	11.2	10.8	10.4
Oil	10.7	9.3	10.5	9.9	9.6
Gas	0.7	0.7	0.7	0.9	0.8
Merchandise Trade Balance	1.6	-0.5	0.1	4.8	3.5
Non-oil & gas	4.5	1.6	2.8	6.9	6.2
Oil & gas	-2.9	-2.1	-2.6	-2.1	-2.6
Services	-2.6	-3.5	-2.8	-3.1	-2.2
Income	-6.1	-7.1	-6.8	-7.0	-6.5
Current Transfers	1.1	1.0	0.9	1.0	1.0
CAPITAL AND FINANCIAL ACCOUNT	**-0.5**	**8.6**	**5.5**	**8.8**	**7.8**
Capital Account	0.0	0.0	0.0	0.0	0.0
Financial Account	-0.5	8.6	5.5	8.8	7.8
Direct Investment	3.6	3.7	5.8	0.5	3.0
Portfolio Investment	2.8	3.4	1.9	1.8	9.0
Other Investment	-6.9	1.6	-2.3	6.5	-4.1
Net Errors and Omissions	**-0.1**	**-1.0**	**0.5**	**-0.1**	**-1.6**
Overall Balance (Change in Reserves)	**-6.6**	**-2.5**	**-2.6**	**4.4**	**2.1**
Foreign Reserves	**104.8**	**98.1**	**95.7**	**99.4**	**102.6**

Source: Bank Indonesia

Meanwhile, BI has maintained 7.5% interest rate for seven consecutive months up to the end of the first quarter of 2014. This tight monetary policy is aimed at maintaining financial stability after high inflation during 2013, which was attributed to the fuel price hike and the quantitative easing by the Fed in the United States in 2013. Throughout the first quarter, inflation was maintained within the range of 3.5-5.5% targeted by BI. In January 2014, Indonesia's headline inflation rate spiked up to 1.07% (Figure 2), which is the highest since 2009 due to two factors. First, severe flooding in Indonesia -notably in Manado and Jakarta- at the peak of this year's rainy season disrupted distribution of goods, which leads to an increase in food prices. Second, further depreciation of Rupiah leads to increased price of commodities as imports became more expensive.[1]

Figure 2. Inflation (January-April 2014, 2012=100 and December 2013, 2007=100)



Source: Badan Pusat Statistik

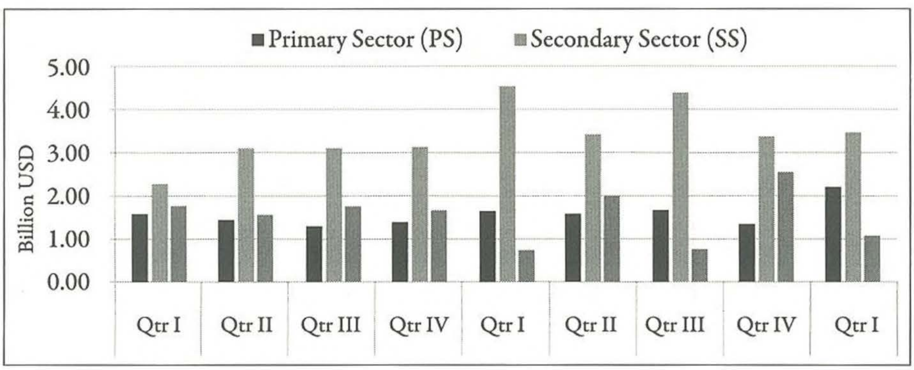
Figure 2 shows that the rise of core inflation is far lesser than the rise in headline inflation, which suggests that seasonal factors such as floods and bad weather contributes most to the overall inflation on January 2014. In February 2014, Indonesia recorded lower inflation rates, 0.26% headline inflation and 0.37% core inflation. In contrast to February 2014, clothing and food commodities recorded the lowest inflation rates in March 2014 due to two reasons. First, Rupiah exchange rate continued its appreciation, which consequently reduced the price of imports and thus prevented the

1 The depreciation of Rupiah at the beginning of 2014 was the continued effect of the end of quantitative easing (QE) in the United States that had been contemplated since late May 2013. The immediate effect of QE tapering is seen in 2013 as the rupiah lost more than 21 percent of its value against the US Dollar as capital flows out of the region.

rise in domestic commodities prices. Second, March is the start of the harvest season, which led to decline in prices of the main food products. In April 2014, Indonesia recorded 0.02% headline deflation. In addition to increased consumption during this year's Eid festivities and the upcoming presidential election, the current level of foreign reserve is still less than the level achieved during the first quarter last year, and thus provides an incentive to maintain the rate. Despite an increasing trend in foreign reserves, the level of foreign reserves at 102.6 billion USD has not reached the level of foreign reserves in the first quarter of 2013 (104.8 billion USD).

Aside from the aforementioned improvements in economic fundamentals, the first quarter of 2014 also witnessed some worrying trend. First, there was a slowdown in Gross Domestic Product (GDP). Despite a quarterly growth of 0.95%, Indonesia's economy slowed down. The 0.95% quarterly growth rate is significantly lower compared to the previous year's quarterly growth rate of 1.44% during the same period. In addition, the GDP growth (year-to-year) was down to 5.21% after the previous growth of 6.03%. Second, there was a decline of realized FDI into Indonesia.

Figure 3. FDI Realization by Sector



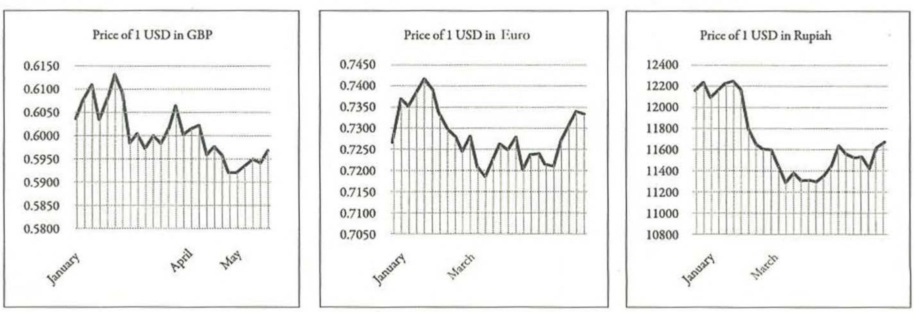
Source: CEIC database

Based on data on investment realization from the Investment Coordinating Board (BKPM), there was 6.9 billion USD of realized FDI in this quarter compared to 7.4 billion USD of realised FDI in the previous quarter (see Figure 3). The realization of FDI this quarter is also less than the 7.04 billion USD from the same quarter last year. The largest decline in FDI is found in electricity, supply, and gas sector which was alarming due to the ongoing supply side problem of electricity and energy security in general. On May 2014, the new negative investment list was issued through a Government Regulation in lieu of law (PP) No. 39/2014. The newly issued regulation is a revision of negative investment list issued through PP No.36/2010 and lists significant restrictions of foreign ownership in horticulture, distribution and warehousing, as well as telecommunication. There is a maximum 30% of ownership in seeding, manufacturing, research, tourism, as well as services in horticulture. Meanwhile, foreign ownership in distribution is restricted to 33%, the same in cold storage (in Sumatra, Jawa and Bali) as well as warehousing. Foreign ownership in telecommunication network providers is restricted to 65% while foreign ownership in telecommunication services is restricted to 49%. Third, despite significant appreciation during the first quarter of 2014, Rupiah started to depreciate, starting from the end of the first quarter of 2014.

Depreciation of Rupiah

By 8 March 2014, the position of Rupiah is at 11,289 per USD in contrast to 12,160 per USD at the beginning of the year (Figure 4). The appreciation of rupiah was due to increasing inflow of money to Indonesia, following the high interest rate of 7.5%. High interest rate encourages more savings, and leads inflows of money coming to Indonesia. This is evident from the BOP data in Table 1, in which the incoming portfolio investment is increased from 1.8 billion USD in fourth quarter of 2013 to 9 billion USD. However, after 8 April 2014 Rupiah started to depreciate against the USD despite the high interest rate. The trend of depreciation has continued well into the second quarter of 2014.

Figure 4. Price of 1 USD in Great Britain Pound, Euro and Rupiah

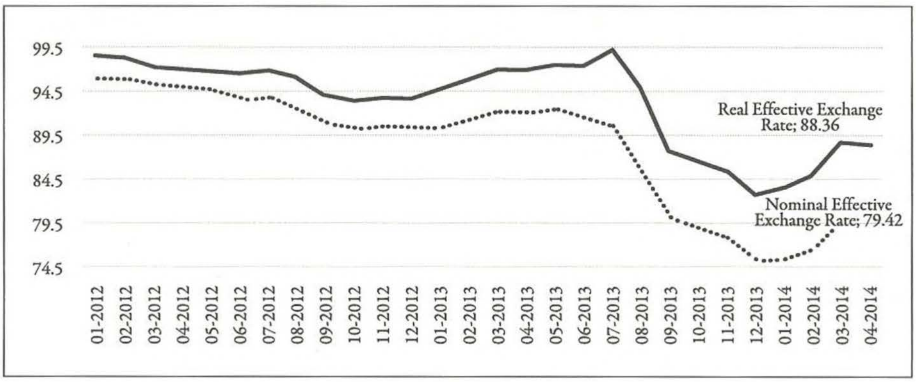


Source: Bloomberg

External factors such as the strengthening of USD in global market as the result of improvement of economy across US that leads to growth in employment contributed to the strengthening the USD that leads to depreciating trend of Rupiah. Evidently, Pound Sterling and Euro exhibit similar trend with Rupiah (Figure 4). Meanwhile, the increase in domestic demand of USD might be one of the factors that contributed to depreciation of Rupiah. In reality, large private external debt would add pressure on Rupiah in the long run.

Figure 5 shows that the gap between Real Effective Exchange Rate Index and Nominal Effective Exchange Rate Index has widen since the decrease of both indexes nearing the end of 2013. This indicates that the domestic price increases faster than overseas price. If this continues, it will impede Indonesia's competitiveness.

Figure 5. Real Effective Exchange Rate Index (2010=100)



Source: Bank for International Settlement

Depreciation of Rupiah is likely to continue as the U.S. economy continues to improve. This will have positive impacts on exports and tourism. However, since Indonesia relies heavily on imports for inputs of production, the depreciation of Rupiah will be detrimental as it raises cost of production. Nevertheless, depreciation of Rupiah will benefit specific sectors such as tourism and export of Indonesia's mainstay export commodities. In addition, fulfilment of domestic consumption that relies on imports will drive inflation.

GDP Slowdown

The overall slowdown in this quarter could be attributed to temporary contraction of exports due to mineral export ban and appreciation of Rupiah, the decline of imports of capital goods amidst slowdown of economy, in addition to slowdown in GFCF.

Table 2. GDP Growth (% year-to-year)

	Mar-13	*Jun-13*	*Sep-13*	*Dec-13*	*Mar-14*
GDP	**6.03**	**5.76**	**5.63**	**5.72**	**5.21**
Excluding Petroleum and Gas	6.67	6.31	6.07	5.98	5.56
Petroleum and gas	-4.93	-4.07	-2.53	0.69	-1.64
By Expenditure					
Private Consumption	5.24	5.15	5.48	5.25	5.61
Government Consumption	0.44	2.17	8.91	6.45	3.58
Gross Fixed Capital Formation (GFCF)	5.54	4.47	4.54	4.37	5.13
Construction	6.78	6.61	6.23	6.68	6.54
Machinery and Equipment					
Domestic	0.17	3.98	9.77	4.97	4.89
Foreign	0.91	-1.40	-0.45	-0.45	5.11
Transportation					
Domestic	21.34	9.45	8.04	13.65	8.73
Foreign	-3.13	-10.18	-7.50	-18.65	-15.76
Other Domestic	19.43	23.01	7.72	14.94	6.30
Other Foreign	1.14	0.45	9.05	9.00	2.46
Exports of Goods and Services	3.58	4.82	5.25	7.40	-0.78
Imports of Goods and Services	-0.03	0.69	5.09	-0.60	-0.66
By Sector					
Tradable Items					
Agriculture, Livestock, Forestry	3.73	3.33	3.33	3.83	3.30
and Fisheries (ALFF)	0.10	-0.60	1.99	3.91	-0.38
Mining and Quarrying					
Manufacturing					
Petroleum and Gas	-4.68	-2.78	-2.50	2.97	-0.65
Excluding Petroleum and Gas	6.86	6.62	5.55	5.44	5.56
Non-tradable Items					
Electricity, Gas and Water Supply	7.91	4.04	3.83	6.62	6.52
Trade, Hotel & Restaurant	6.50	6.37	6.14	4.78	4.59
Transport	5.96	7.66	6.73	7.84	8.24
Communication	11.69	12.84	11.82	11.75	11.34
Financial, Ownership and Business	8.18	7.75	7.56	6.79	6.16
Other Services	6.49	4.49	5.62	5.27	5.81

Source: CEIC Database

Table 2 shows that export was contracted by 0.78% this quarter, while it was expanding at 3.58% rate on first quarter 2013. In addition, there is a prolonged slowdown in imports since the previous quarter. The growth of Gross Fixed Capital Formation (GFCF) this quarter is 5.13%, lower than 5.5% recorded during the first quarter in 2013. The largest slowdown is found in mining and quarrying, as well as manufacturing. Meanwhile, the growth in private consumption was driven by the legislative election. This quarter's government consumption accelerated to 3.58% from 0.44% in first quarter 2013, which was due to the initiation of various infrastructure projects, such as roads and bridges, as well as higher distribution of subsidized rice for the poor.

The contraction of exports during the first quarter of 2014 is also evident from the BOP data in Table 1. Indonesia recorded a decrease of 4 billion USD from last quarter, reaching 44.4 billion USD of export during the first quarter of 2014. In addition, this quarter's exports was down by 0.8 billion USD in comparison to the first quarter of 2013. This suggests that the contraction of exports is not seasonal in nature.

There are several reasons for the contraction of exports. Due to the shrinkage of US and European market, competition between suppliers has become more intense. Naturally, competition in the Southeast Asian region (also known as the ASEAN region, with reference to the Association of Southeast Asian Nations) becomes more intense as the result; on the other hand, Indonesia still has to improve its competitiveness in ASEAN. Furthermore, mineral export ban for raw material that was implemented on January 2014 further contribute to contraction of exports from mining sector. And lastly, high interest rate increases the cost of production, which further impedes Indonesia's competitiveness. Slowdown of China's manufacturing sector also has some effect on the contraction of Indonesia's exports, especially for mineral products.[2]

Meanwhile, decrease in FDI contributes to the contraction of GFCF, as evident from BKPM data. FDI realization in this quarter is amounted to 6.9 billion USD, which is lower compared to 7.4 billion USD of realised FDI in the previous quarter. The realization of FDI this quarter is also less than the 7.04 billion USD from the same quarter last year. The slowdown of FDI could be attributed to the "wait and see" attitude of foreign investors due to political uncertainty, as well as the expectation of a slowdown in economy as the result of tight money policy.

2 By authors' own calculation, mineral products have the largest percentage in China's import basket from Indonesia. Between 2006-2012, mineral products constitute around 46% of China's import from Indonesia.

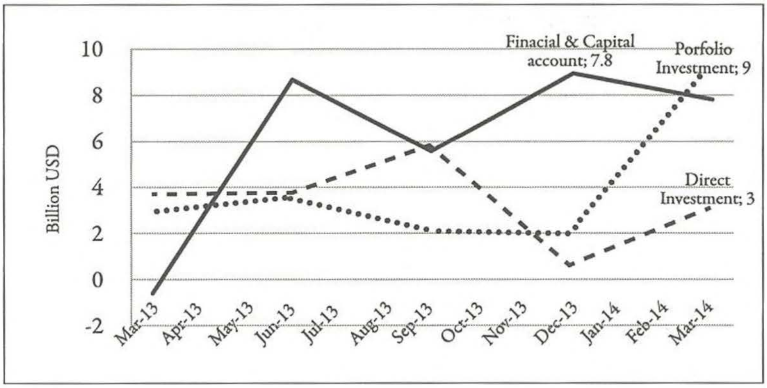
Prospect of Balance of Payment

The deterioration of BOP this quarter was due to a decrease of surplus in capital and financial account. Even though capital and financial account has recorded surplus since the second quarter of 2013, it has decreased to 7.8 billion USD in this quarter from the previous 8.8 billion USD in the 4th quarter of 2013.

Despite of this, current account deficit has lessened to 4.2 billion USD. While the 4.2 billion USD deficit could be financed by the 7.8 billion USD of investment, it is important to note that, in this quarter alone, the 9 billion USD surplus from portfolio investment account is enough to finance the deficit in current account. Meanwhile, surplus in direct investment account amounted to 3 billion USD in this quarter. Since last quarter, the surplus in portfolio investment account is larger than that of direct investment account.

Table 1 shows that the increase in surplus of direct investment account is slightly larger than the increase of surplus in portfolio investment account this quarter. Nevertheless, this has not always been the case. Looking at Figure 6, before the fourth quarter of 2013, direct investment account has always recorded larger surplus than portfolio investment account. Nevertheless, surplus in direct investment account has sharply declined starting from the end of the third quarter of 2014. This shows that the increase in investment portfolio inflows is attributed to high interest rate that is maintained by BI. Decline in FDI is especially high by the end of the first quarter of 2014. The current progress of event shows that new investments that are coming into Indonesia is not long-term in nature, but rather short-term as investor is taking advantage of high interest rate in Indonesia. In terms of capital and financial account, there should be little change until the presidential election on July 2014, as investors are waiting for the direction of Indonesia economic policy after the presidential election on July 2014.

Figure 6. Capital and Financial Account



Source: Balance of Payment, Bank of Indonesia

Meanwhile, the improvement in current account deficit was due to improvement in service trade, as well as contraction of imports. Merchandise trade is not showing significant improvement, as there is contraction in both exports and imports. The contraction of exports was due to increased competition due to the shrinkage of US and European market. In addition, slowdown in China's manufacturing sector, as well as the newly implemented mineral export ban, might have some effect on the contraction of mineral exports. Moreover, high interest rate increases cost of production, which further reduces Indonesia's competitiveness. If there is no significant changes in global market, or domestic regulation, current account deficit is not likely to change significantly.

Current Issues in Indonesian Economy

Protectionism on the Rise: New Trade Law and the New Industry Law

After the mineral export ban, trend of protectionism continued well to this quarter with the issuance of both the new law for Industry, Law No. 3/2014 on January 2014, and the new trade law, Law No. 7/2014 on February 2014, which is Indonesia's new trade law since 30 years. Deputy Trade Minister Bayu Krisnamurthi stated that the new trade law further solidifies Indonesia's stance in international trade scheme, in which it adopts a managed trade, rather than free trade, and that the new trade law will provide clear direction for investors, creating conducive investment climate, as well as protecting Small and Medium Enterprises (SME). The obvious intention to save domestic industry, especially SMEs through the new industry law is found in article 117.2 in which the new law extend the scope of industrial obligation to include export oriented and green businesses, as well as businesses that use products or parts made by small- and medium-sized enterprises (Article 117.3). In essence, both laws were aimed at saving domestic industry through a series of protectionist measures, or increasing nationalist sentiments in the election year.

Protectionist measures are well-defined in the new industry law. Article 32 gives full authorization to the government to restrict exports of minerals and commodities as an effort to prioritize the provision of natural resources for domestic needs, while Article 86 dictates prioritization of domestic products in the procurement of goods and services by government agencies or projects financed by state budget. In addition, the law enables the government to fully control strategic industries, including setting price for the local market (Article 84.3) on the grounds of national interest and objectives. The new industrial law will also provide more fiscal and non-fiscal incentives companies (Article 100 and 111). In addition, Articles 25, 27.2 and 28 set some regulations, or restrictions as some may say, towards foreign workers. This includes regulation on working time, knowledge and skill requirements in accordance to the national standards of work competency.

Meanwhile, the new trade law addresses several areas that could affect Indonesian companies, namely international and domestic trade, trade in services, standardization of trade goods, e-commerce, product labelling (Article 6), international trade security for exports and imports, export business facilities, warehouse registration, and the regulations that dictate competency requirement for technical personnel that should be fulfilled by business service providers. In addition, Article 85 enables lawmaker to have full authorization in approving international trade pacts and reviewing current trade pacts.

There are ambiguities of statements inside the new trade law, in addition to unfair and one-sided policy, which all the more add to the unattractiveness of the new trade law.[3] Moreover the trade law legalizes protectionist acts by the government in Articles 32 and 51, which could further add to the existing harsh criticism on Indonesia's recent protectionist trade measure

3 The word "national competitiveness" in Article 49.4 could be used as a justification for the implementation of protectionist regulations. In addition, many of the articles grant freedom to break contract to the government, on example being Article 84.1.

in general.[4] Similarly, some of the clauses in the new industry law are ambiguous. Both laws seem to have one common problem: the statements are general in nature and refer to later implementation regulations.

Nevertheless, the important question is whether these new laws would truly be an efficient solution to its stated goal to protect local SMEs and to gear up domestic production. In reality, the more pressing issue is to increase Indonesia's competitiveness in order to welcome the coming ASEAN Economic Community (AEC). Indonesia needs to strengthen its industrial base for downstream and component industry in order to compete with the other ASEAN countries. In addition, Indonesia's economic problems do not ease the problem in infrastructure, education and human capital among other things. All of these issues contribute to the high cost of production that is faced by Indonesian industry. Meanwhile, the government has not yet issued implementing regulations and rules (government and ministerial) in relation to both the new trade and industry laws. The longer the government delays the issuance of implementing regulations on the laws in regards to these issues, the more difficult it is for Indonesia to catch up with the other ASEAN countries, and the economic impact of this will be long term, and negative at least.

Development in Electricity Sector

According to the estimates from the State Electricity Company (PLN), the national electricity demand will reach 386.6 terawatt hour (TWh) in 2022 and will grow by an average of 8.3% per year (see Table 3). Increasing population, along with rapid economic growth during the last decade, and especially the rising number of the middle class has led to high consumption of electricity. The Ministry of National Development Planning (Bappenas) estimated 28.13% increase in Indonesian population from 238.5 million people in 2010 to 305.6 million people in 2035. In addition, Indonesia needs to increase competitiveness of national industry that will become the catalyst for Indonesia's economic growth in the long run. To increase industry growth, the Indonesian government has done industrial acceleration since 2012, which continued on to 2014.[5] Additional capacity of about 6,000 MW of electricity per year is required to sustain economic growth of around 6% per year, demographic increase of 1.7%

4 Article 32 stipulates that the government has the authority to limit import/export of goods in case of "national security or public interests", while Article 51 implies the possibility to restrict imports of specific goods if this has become a threat for the local industry.

5 "Menperin: Indonesia Percepat Pertumbuhan Industri," *Berita Sore*, 25 April 2014, http://beritasore.com/2014/04/25/menperin-indonesia-percepat-pertumbuhan-industri/

per year, electricity industry growth between 7.5-8.5% per year.[6] With this agenda, energy security has become an important issue.

Nevertheless, meeting the demand of electricity has been an ongoing problem in Indonesia. The General Plan of Electricity Supply 2013-2022 (RUPTL 2013-2022) compiled by the PLN mentioned a number of urgent problems faced by PLN such as meeting the shortage of electricity supply in areas that experienced shortage of supply of electricity, providing short-term and long-term supply of electricity to outskirt and remote areas,[7] as well as replacing oil-fired electric power plants with non-oil-fired electric power plants (see Table 3).

Table 3. Projection of Economic Growth, Demand for Electricity and Peak Load 2013-2022

Year	Economic Growth (%)	Sales *TWh*	Peak Load (non-coincidence) MW
2013	5,6	189,0	31.892
2014	6,0	207,8	34.987
2015	6,9	226,8	38.128
2016	6,9	246,5	41.303
2017	6,9	266,0	44.526
2018	6,9	286,4	47.85
2019	6,9	308,0	51.337
2020	6,9	331,6	55.226
2021	6,9	357,7	59.518
2022	6,9	386,6	64.299

Source: The General Plan of Electricity Supply 2013-2022 (RUPTL 2013-2022)

In June 2014, the House of Representatives approved the increase of electricity tariff to be implemented on 1 July 2014. The electricity tariff hike could help finance infrastructure building in electricity sector. However, FDI in electricity sector is also required in order to fulfil the growing demand of electricity, as well as to accelerate the development of electricity generation, transmission and distribution processes. Nevertheless, FDI in electricity, gas

6 "Pemerintah Terbitkan Peraturan baru untuk Tambah Kapasitas Listrik," Ministry for Energy and Natural Resources, http://www.djlpe.esdm.go.id/modules.php?_act=detail&sub=news_media&news_id=3732

7 Data from Indonesia's Consumers Association (YLKI) shows that around 20% or about 40 million people in Indonesia do not have access to electricity.

Concluding Notes

During the first quarter of 2014, Indonesia's economy has shown recoveries in most aspects. Albeit the slowdown in GDP growth, current account deficit has lessened and foreign reserves has started to catch up to the previous high level on January 2013. In addition, the appreciation of Rupiah occurred from February to March. Depreciation of Rupiah at the end of the first quarter in 2014 was most likely due to external factors such as the appreciation of USD rather than internal domestic factor. Finally, the Jakarta Composite Index showed increasing trend during the first quarter.

The high interest rate policy applied by the central bank of Indonesia seems to be an effectual treatment. Nevertheless, it remains to be seen whether the Indonesian government will maintain high interest rate throughout 2014. High interest rate attracts money inflows to Indonesia, but nevertheless will increase the cost of operation which leads to decrease in competitiveness in ASEAN. Long-term investment instead of short-term investment is needed for industrial growth in the long run. The main concerns should be on how to attract the right FDI to bolster industrial growth.

Indonesian government's attempt to save domestic industries through a series of protectionist laws has yet to be effectual. The effect of the new trade and industry laws are yet to be seen as the implementation regulations have not yet been issued, while the new investment regulation is expected to reap positive response from investors and private sectors. The mineral export ban was implemented on January 2014, but government's monitoring of the completion of plants and smelters is needed in order to ensure investors' adherence to the regulation.

Meanwhile, Indonesia is facing infrastructural problems in many sectors, which have posed as obstacles for further FDI and industry growth. Electricity sector, for example, has long faced the problem of matching the demand of electricity. Synchronization of laws and efficient bureaucracy are necessary in order to push for reform, and to attract investors to Indonesia.

At the end of the day, Indonesia has to be able to compete with other ASEAN countries in order to tap the shrinking American and European markets. Taking advantage over Thailand's domestic situation in 2014, tourism has to be promoted intensively, and take-over of investment and trade portion that are previously directed to Thailand is necessary to gain momentum in this year. Nevertheless, domestic problems posed as impediments and remain to be leftover homework for the next government. Given that external factors and internal factors stay unchanged, the current state of economy will persist, and the direction of Indonesian economy remains to be seen until after the result of presidential election on 9 July.

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email: Indonesian.quarterly@csis.or.id

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“ As Indonesia is busy in the midst of domestic grand developments in relation to the 2014 election, the environment surrounding Indonesia is also witnessing some significant developments in some crucial issues. In finance, today's emerging Asia registers excess savings. The implication of surging inflows and excess savings is an ample liquidity with lower cost of borrowing, both of which spurred credit and growth in Asia.

Meanwhile, the major power rivalry in East Asia has continued to make interesting twists and turns, as the ascendancy of China threatens the major role of the United States in the region. The U.S. has responded by engaging deeper with countries in the region of Asia-Pacific, strategically and economically. The Trans-Pacific Partnership is a part of the U.S. economic engagement in the region.

As the region grows to be even more dynamic, it would be very interesting to witness how the new leader of Indonesia would respond. Relations with major powers would be even more crucial, and the resolution of ongoing disputes will impact greatly on Indonesia's foreign policy and regional cooperation. ”

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