



REFORM AT THE MINISTRY OF FINANCE OF THE REPUBLIC OF INDONESIA

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OUTLINE

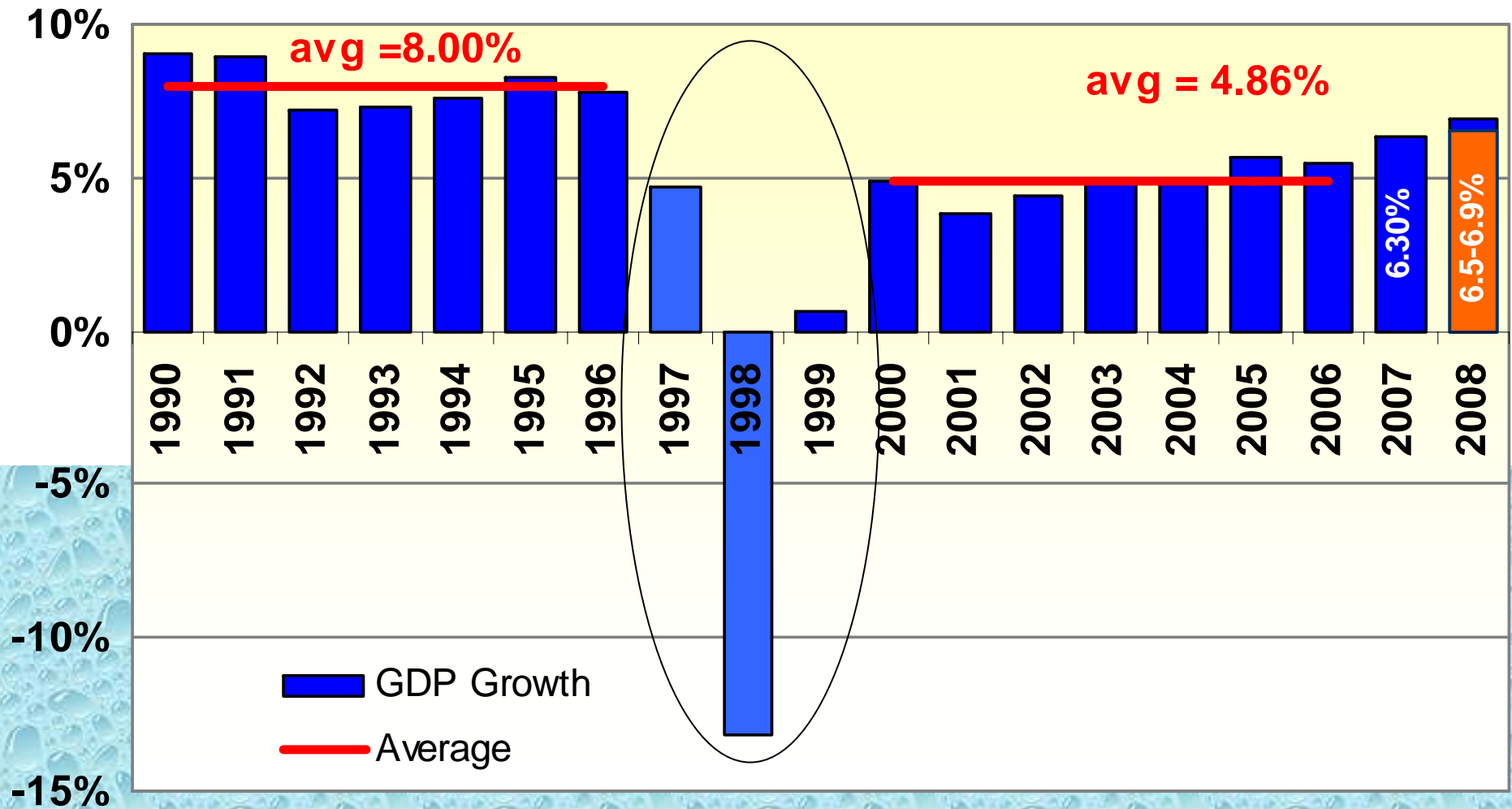
- 1. Pre - and Post Crisis**
- 2. External Challenges**
- 3. Post-Crisis Reform**
- 4. Reform at Indonesia MOF**



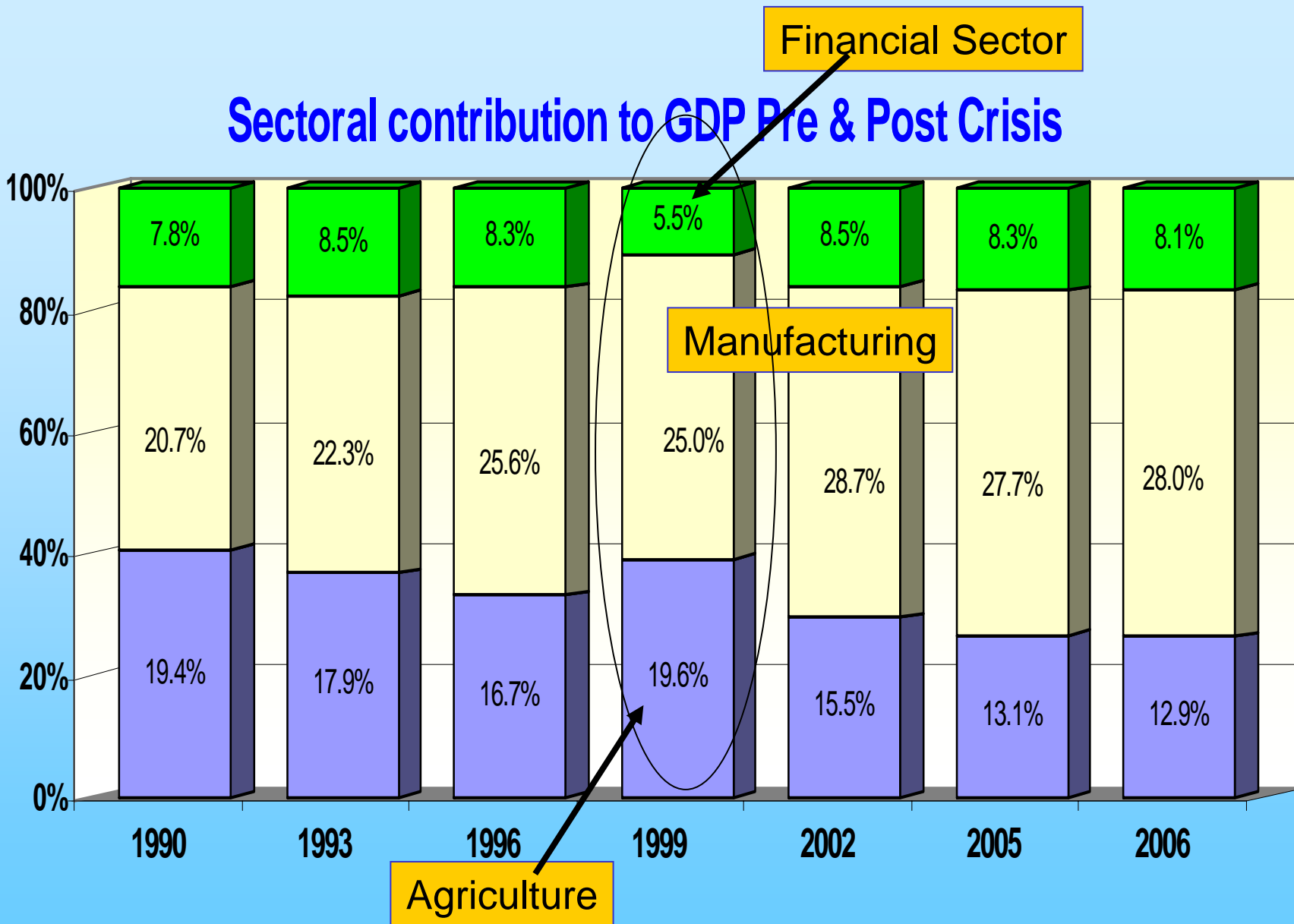
Pre - and Post Crisis

The pre-crisis Growth ave 8%, post Crisis ave 4.8%

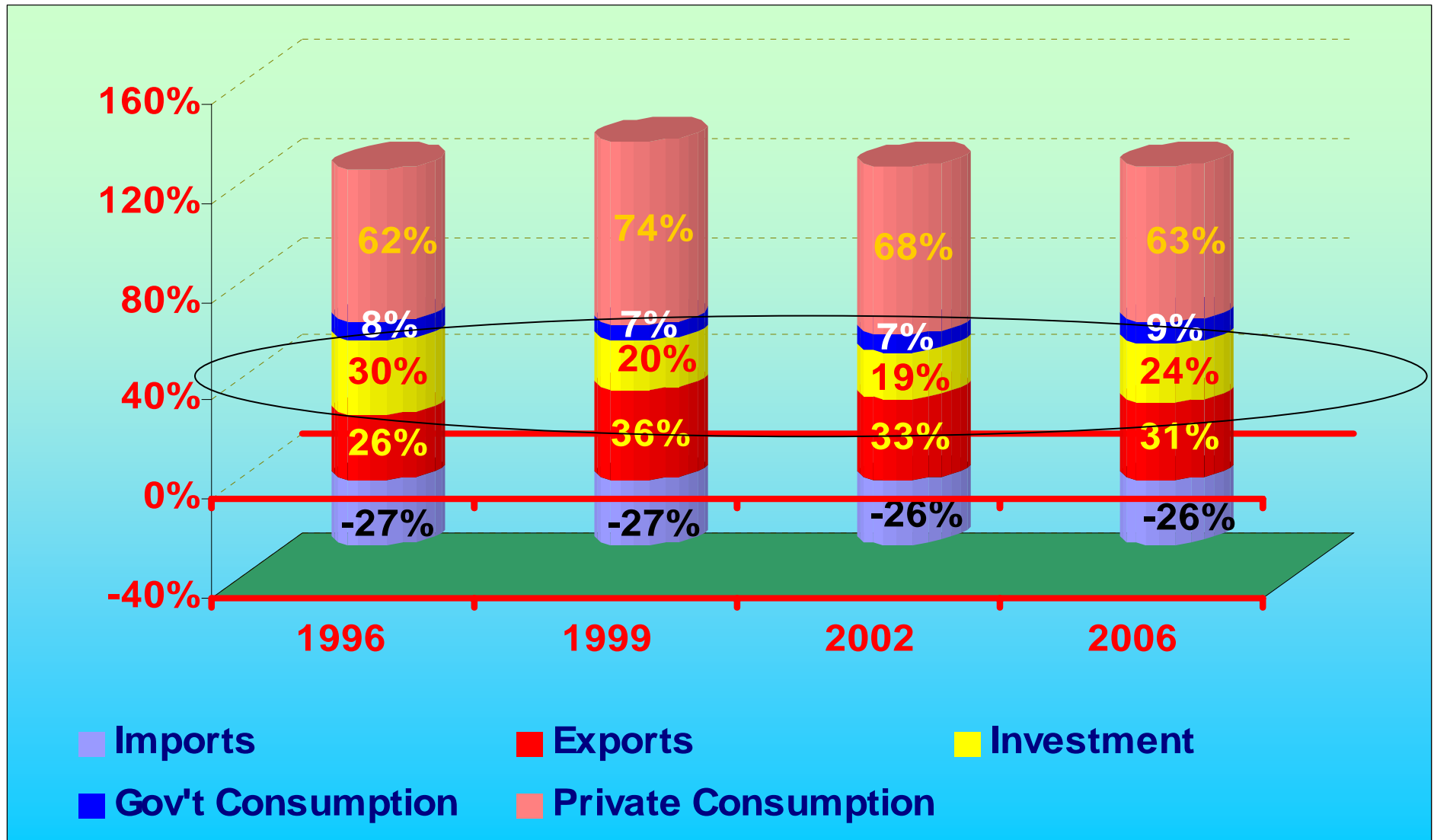
GDP Growth Pre & Post Crisis'97



Financial Sector hardest hit by the crisis, follows by manufacturing sector. Agriculture sector remain strong.



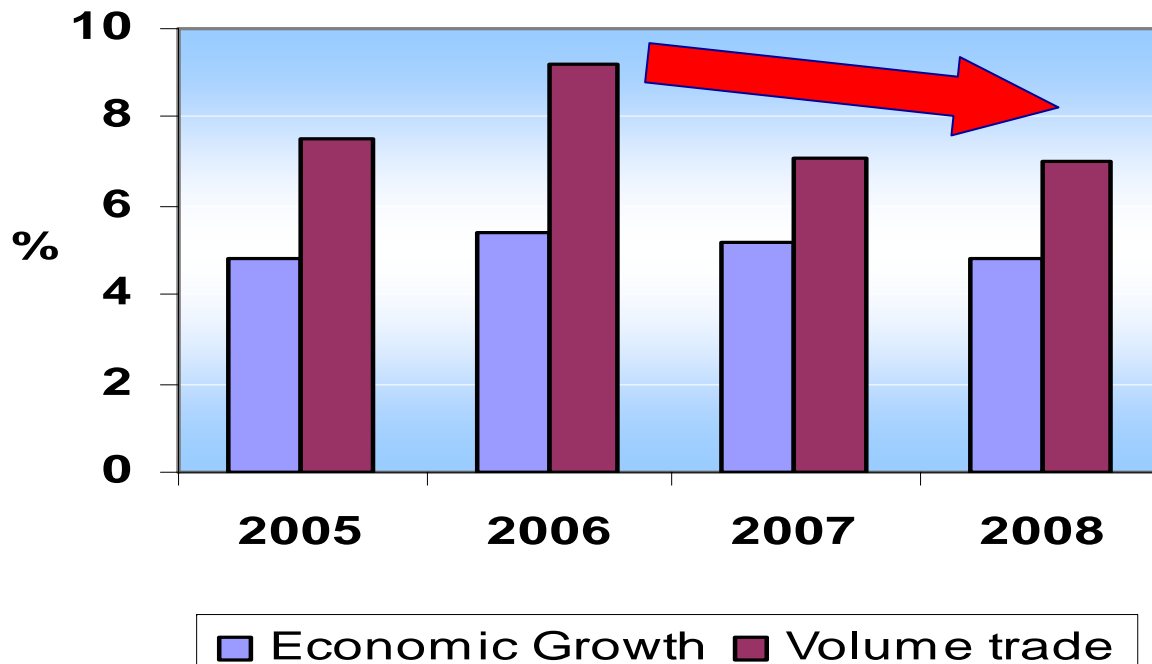
Before crisis investment was 30% of GDP, current level 24% of GDP





Current External Challenges

GLOBAL SLOWDOWN

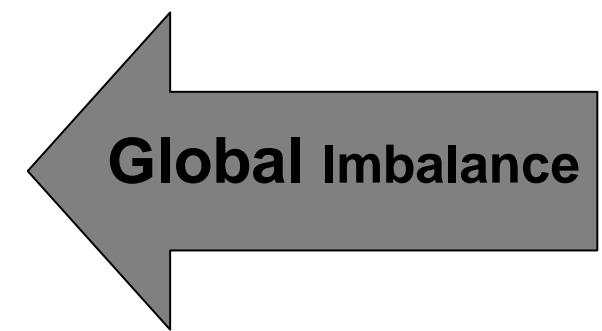
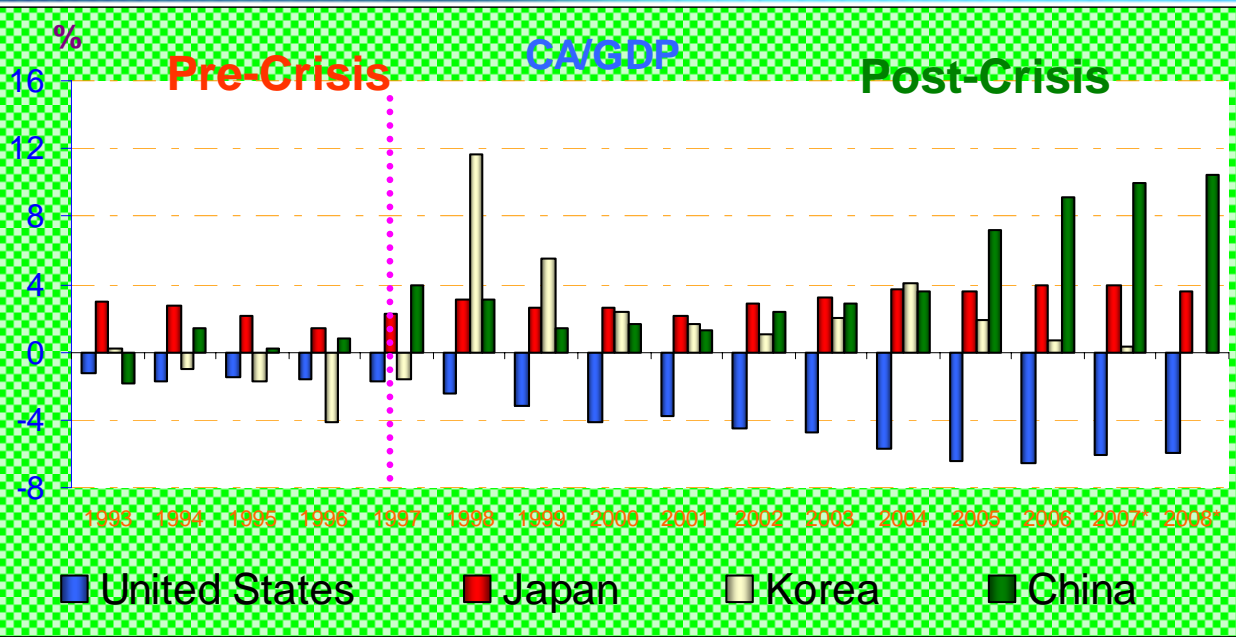


- Global and Trade Slowdown
- US Recession: unemployment and reduce consumption demand
- Subprime Impact
- High Oil Price and inflation pressures
- Further Fed Funds rate cut and stimulus needed
- China and India factor

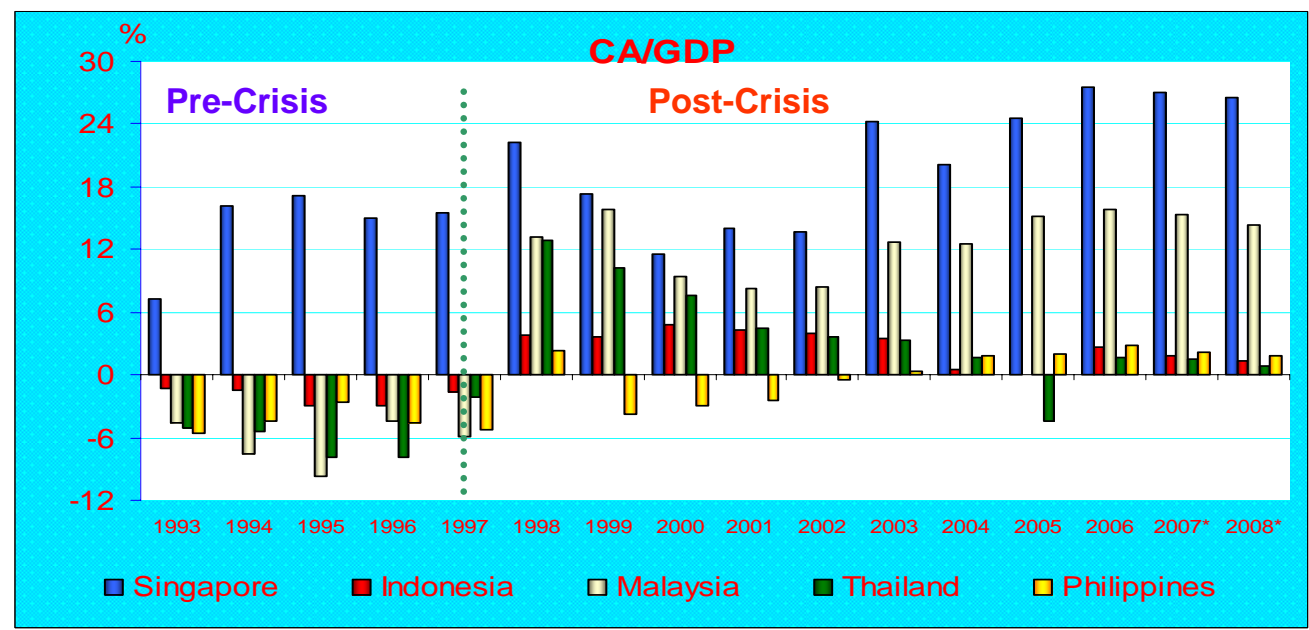
	2005	2006	2007	2008
Economic Growth	4.8	5.4	5.2	4.8
Industrial Countries	2.5	2.9	2.5	2.2
Developing Countries	7.5	8.1	8.1	7.4
Growth Trade Volumes	7.5	9.2	7.1	7.0
Inflation (CPI)				
Industrial Countries	2.3	2.3	1.8	2.1
Developing Countries	5.2	5.1	5.4	5.9
Price of Non-Oil Commodities	10.3	28.4	12.2	2.1

Sumber: WEO, Oktober 2007

Global Imbalance Wider and Capital Flows



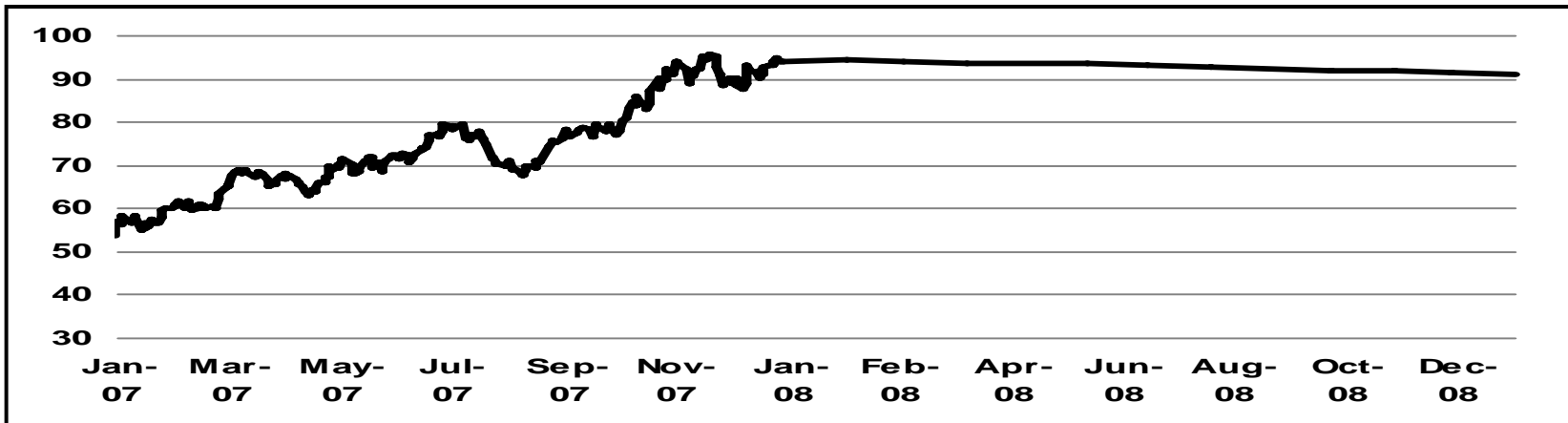
US VS East Asia?



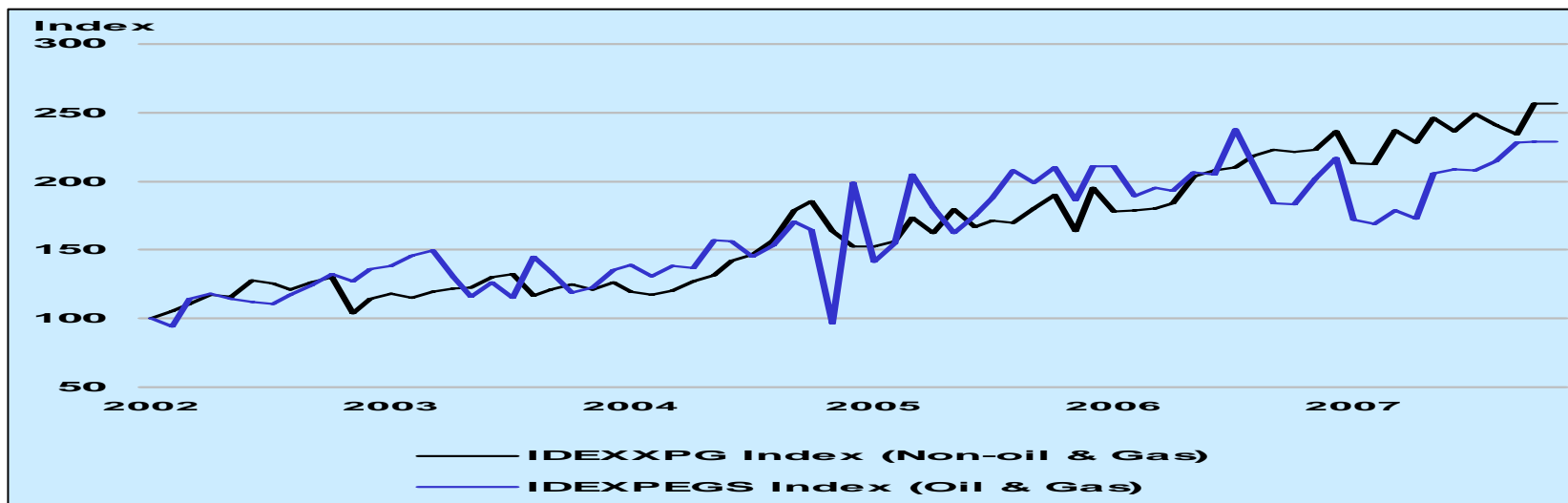
Source: IMF

Higher Oil Prices and Primary Commodities remain Uncertain

Historical and Projected Crude Oil Prices



Historical Prices of Major International Commodities

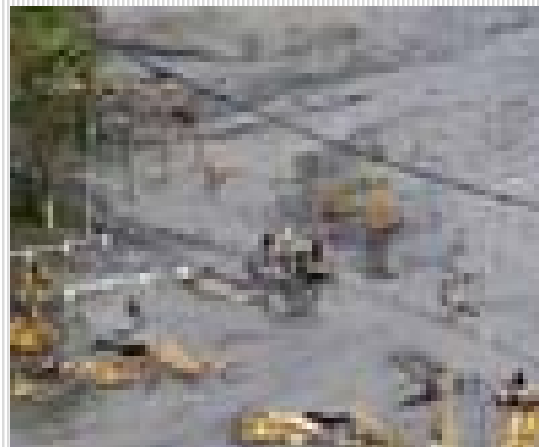


Series of Natural Disasters.....

Tsunami and Earthquake



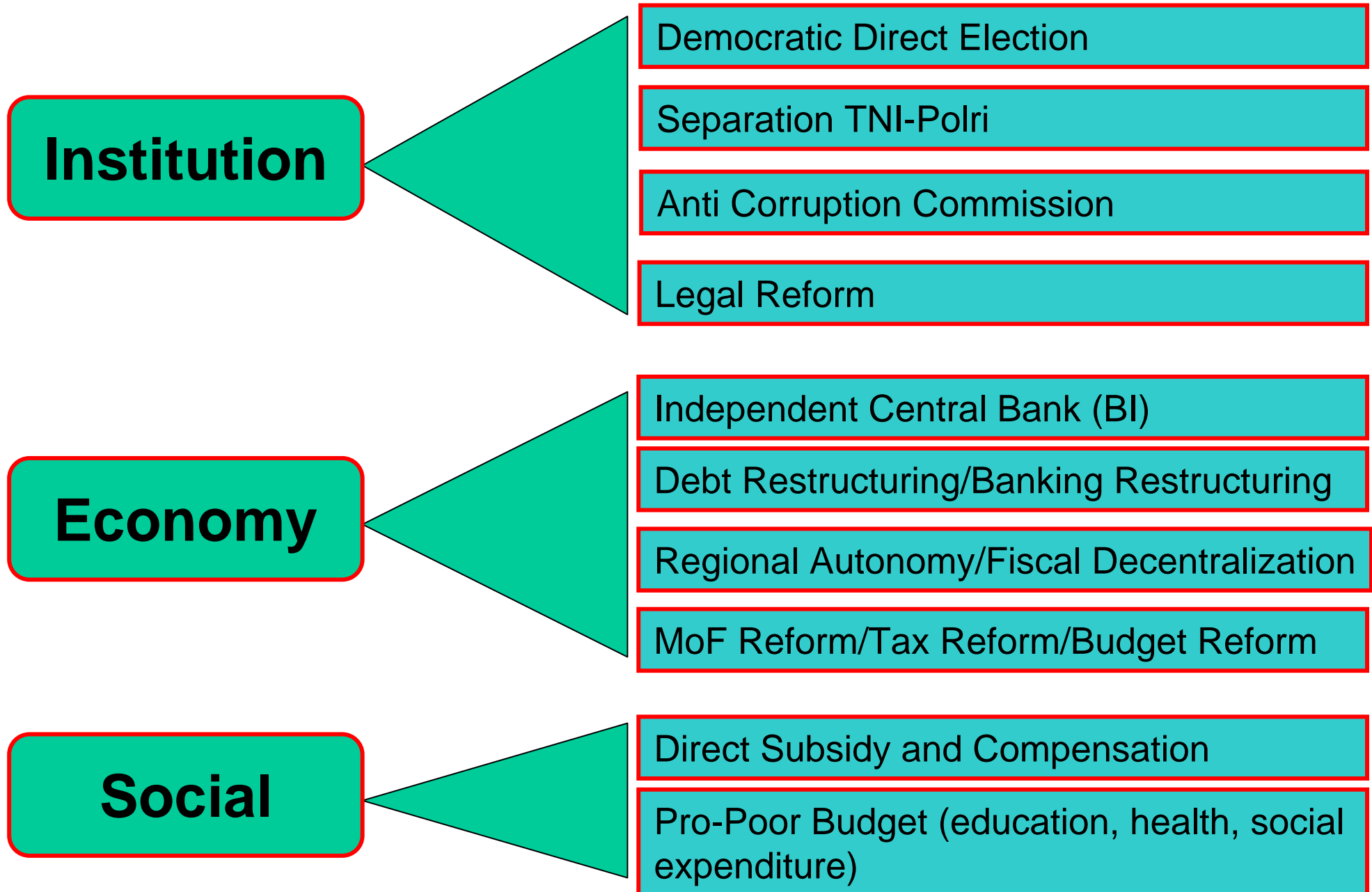
Mud, Hurricane and Floods





Post-Crisis Reform

POST-CRISIS STRUCTURAL REFORM

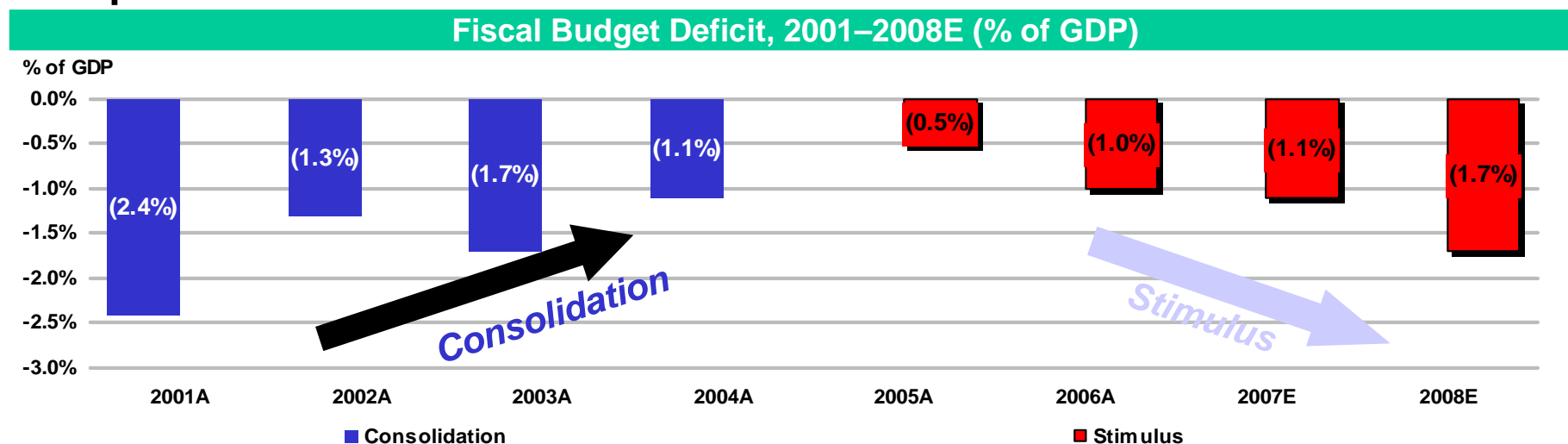


Institutional Reform on Economic and Fiscal Matters post Crisis

- Central Bank Independent
- State Finance, Treasury and State Audit Law
- Planning Function: 'Bappenas' function
- Managing SOE, Privatization and Public Service Obligation (PSO)
- Fiscal Decentralization
- Customs and Excise Operation
- Investment Law: equal treatment of foreign and domestic investors, investment incentives
- Government Bond Securities Post Recap Bonds
- Administration Tax Law (KUP)—to follow Income Tax and VAT

Fiscal Policy Post Crisis: 2000–2007

To stimulate growth, Indonesia has adopted a shift in policy from consolidation to expansion



Key Policy Highlights

Efficient & Effective Expenditure

- Infrastructure development
- Social expenditure through education and health
- Subsidies

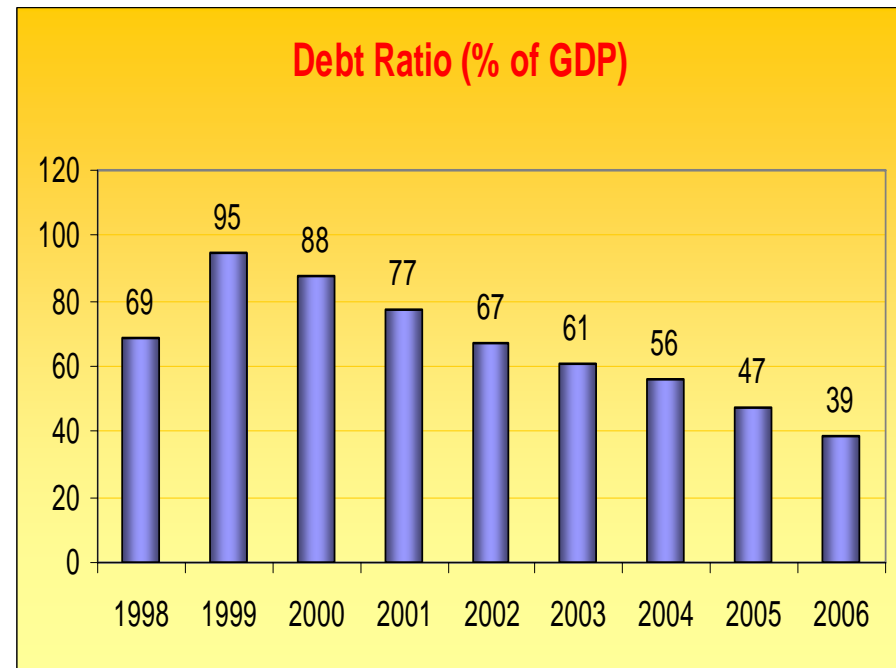
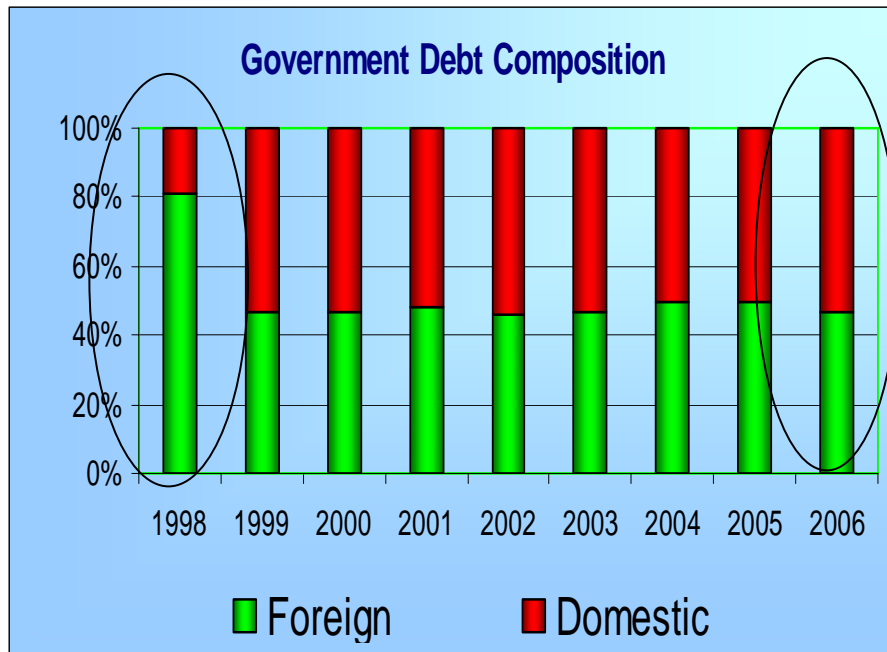
Medium-term Budget & Treasury Reforms

- Performance and multi-year budget
- Treasury single account, accrual basis

Consolidation of Fiscal Decentralization

- Transition towards non hold-harmless
- Regional borrowing and municipal bond issues subject to MOF approval
- Regional financial information systems to support decentralization based on transparency and accountability

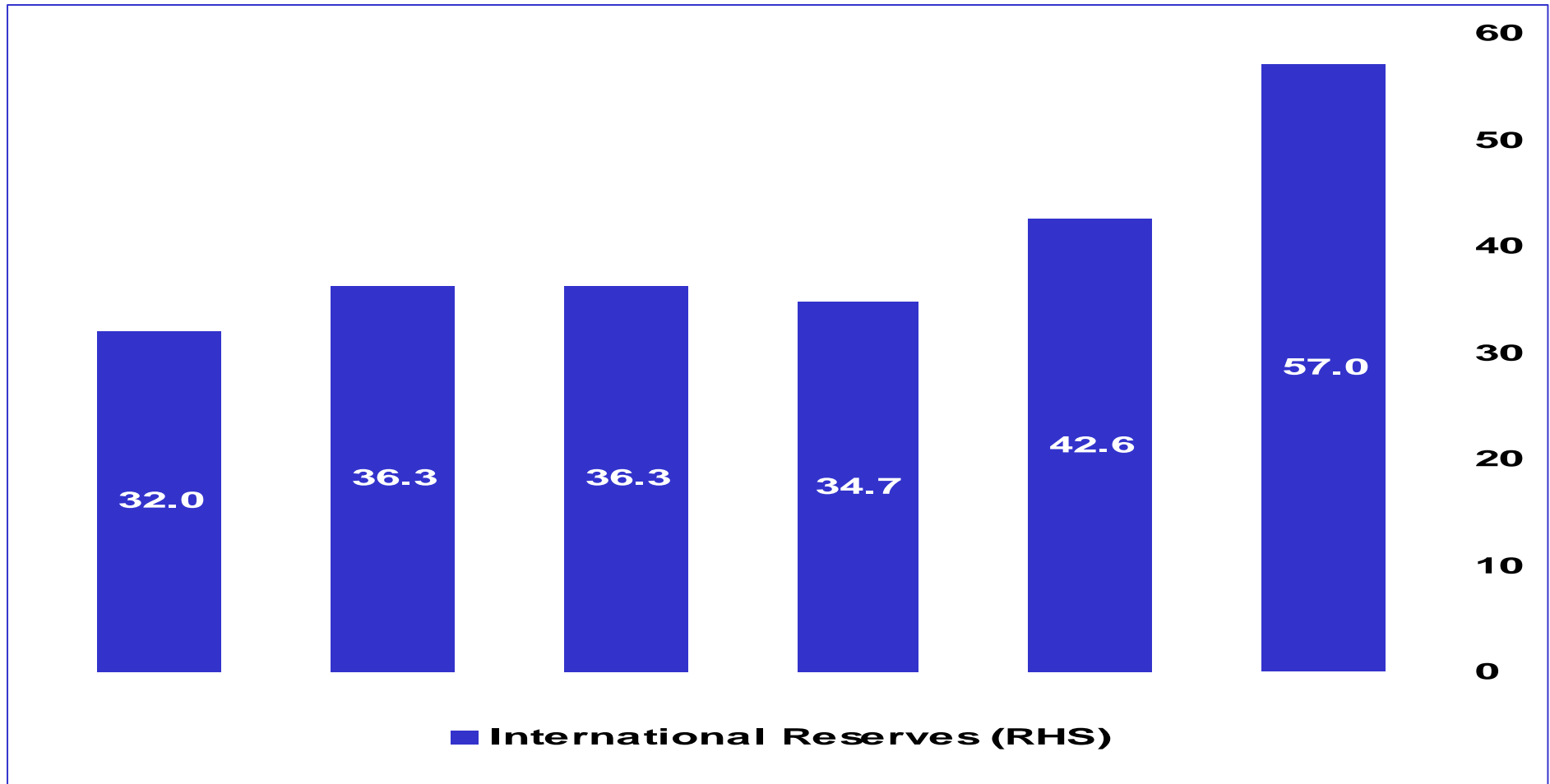
Improving domestic strength in facing external risks (1): Declining Debt Ratio



- The Government debt to GDP ratio improved from 95% in 1999 to 37 in 2007.
- Indonesia moving from external loan to government debt securities to finance budget deficit

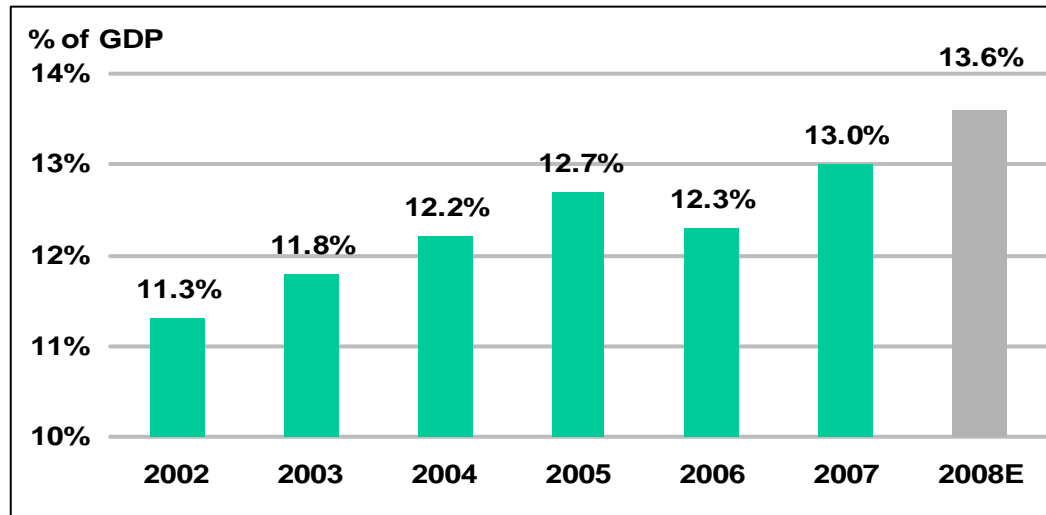
Improving domestic strength in facing external risks (2): Accumulative Reserves

Internal Foreign Reserve (bio US\$)



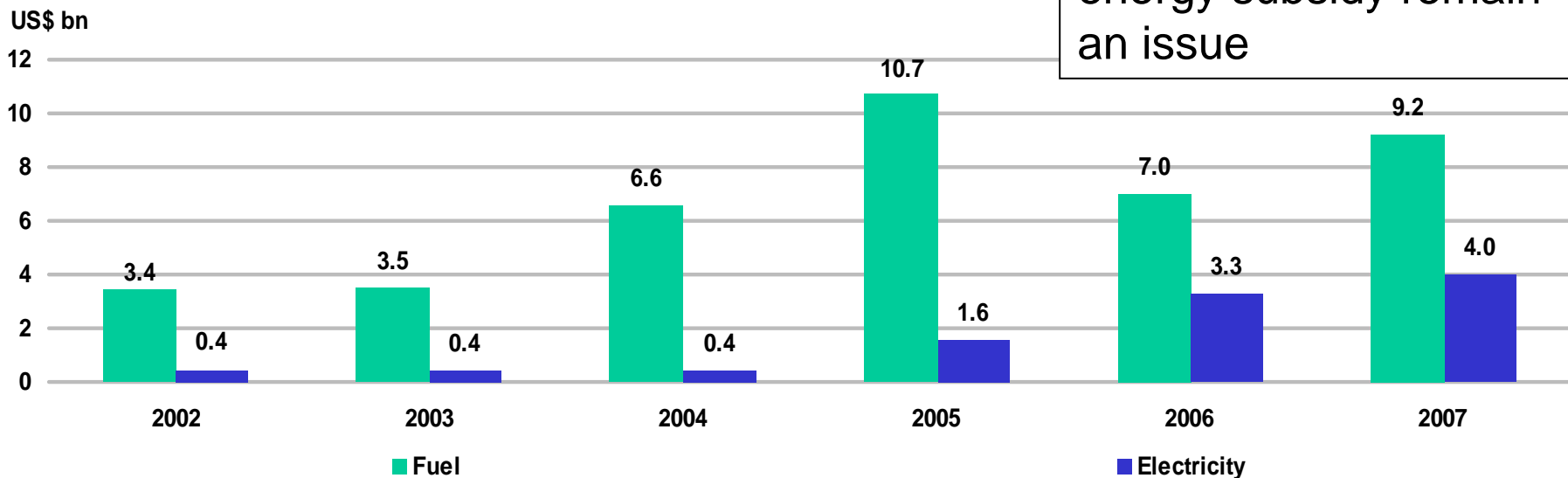
- Foreign reserves increased to US\$57 billion in 2007 even after prepayment of US\$7.8 billion to the IMF in 2006.

Issues to be Resolved: Intensify Gov. Revenue and Government Fuel Subsidies



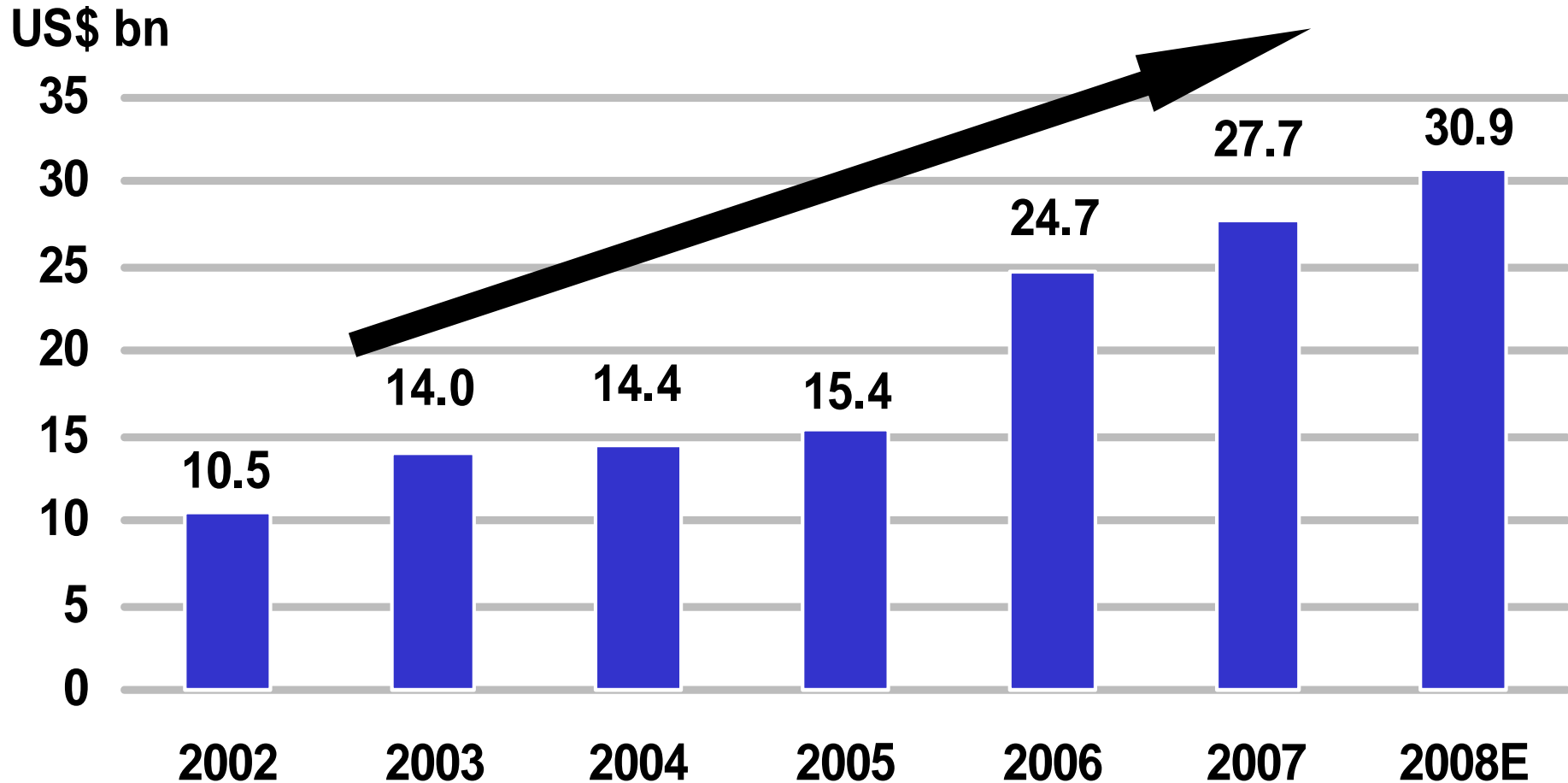
Tax to GDP ratio steadily Increase but lower than regional level, 15-18%

Electricity and Fuel Subsidies



Huge amount of Un-targetted energy subsidy remain an issue

Fiscal Decentralization: Increase Transfer To Region

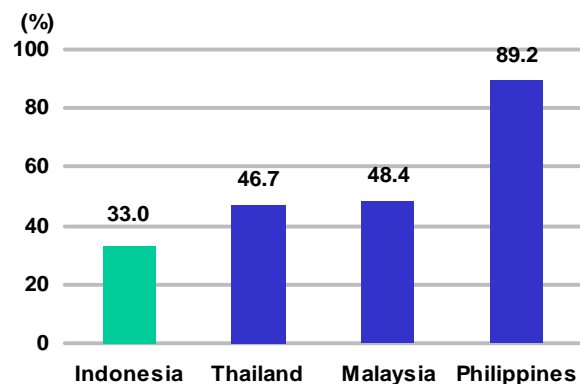


Significant Increase on transfer to region to support Fiscal Decentralization since 2002 need improvement in regional development process

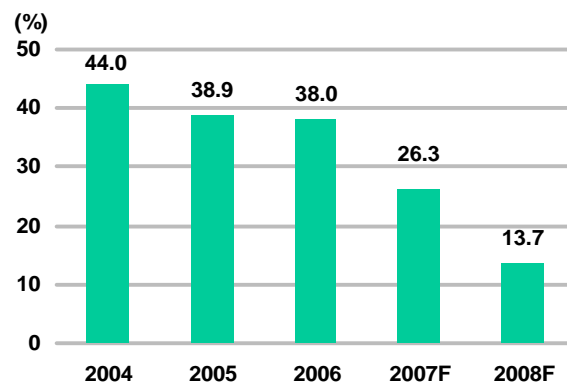
Healthy Macro and Micro Financial Conditions

Strong performance amongst ASEAN peers

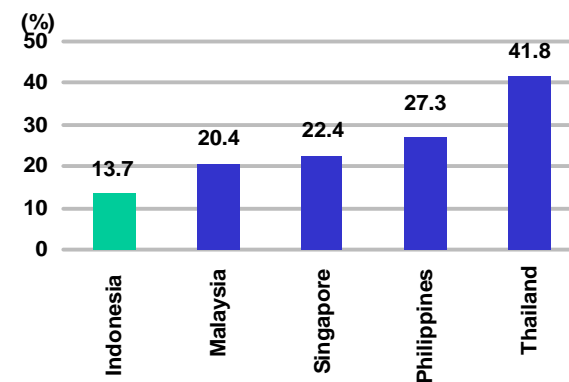
Public Sector Debt to GDP, 2008



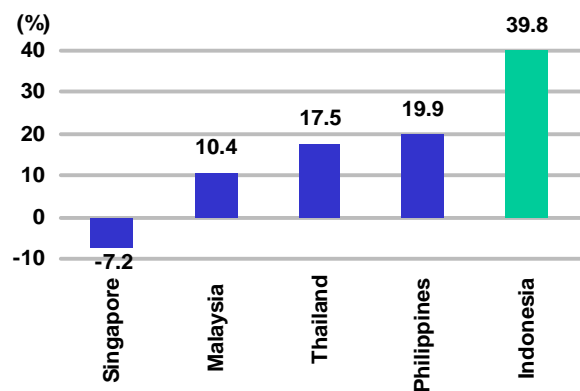
Indonesia Corporate Net Debt / Equity Ratio



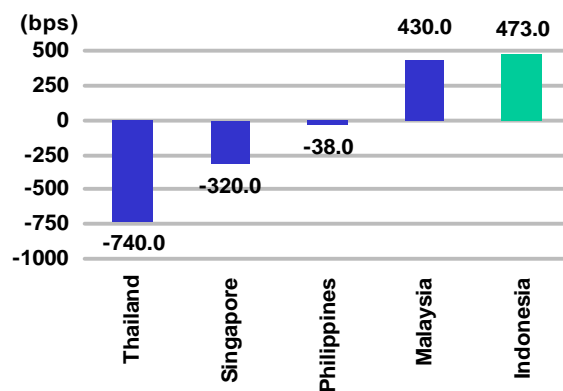
ASEAN Net Gearing, 2008



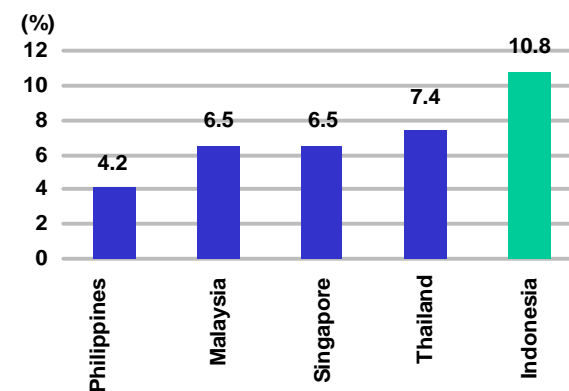
Average Operating Cashflows Growth 2007–2008



Change in ROE 2005–2007

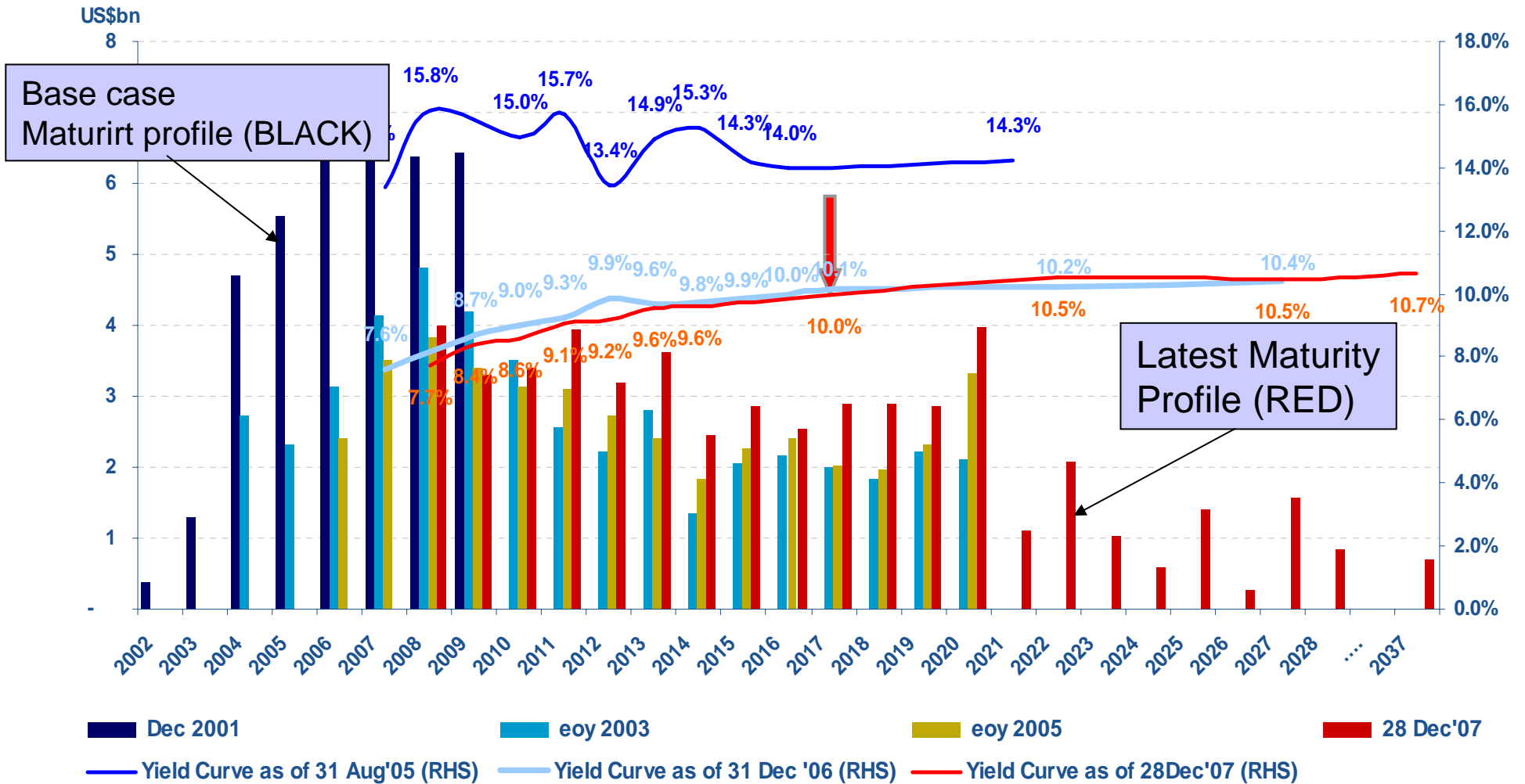


Interest Coverage 2007



Improving Maturity Profile of Debt Securities

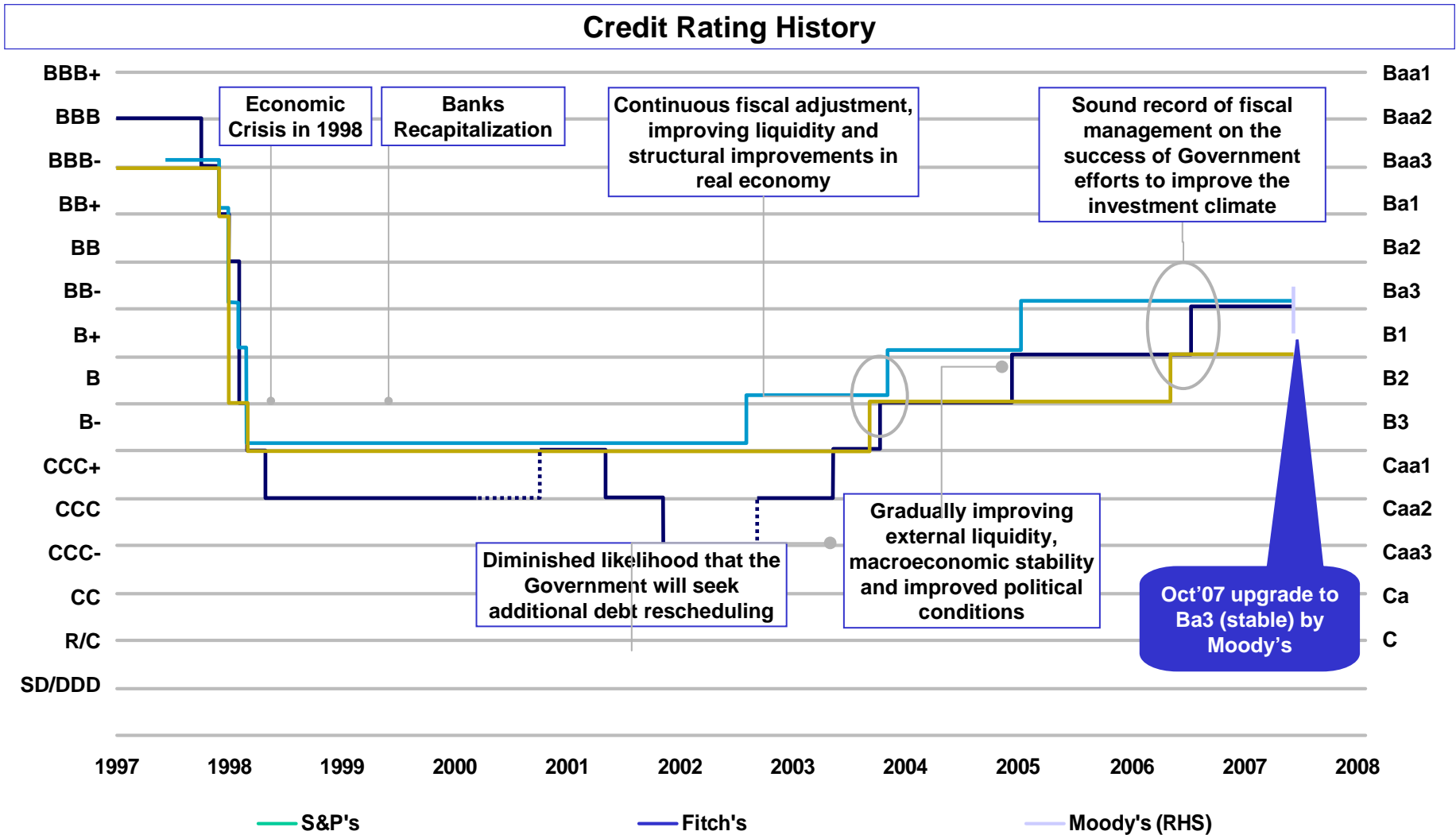
Significant reduction of debt refinancing risk and enhanced government bond market liquidity



Source: Ministry of Finance

Improving Indonesia's Credit Rating History

Prudent government debt securities management helped the improvement of Indonesia's sovereign credit rating





Institutional Reform in the Ministry of Finance

Background

- ❑ The Indonesia fiscal policy and budget system was based on the colonial law dated back in 18 century;
- ❑ Closed, authoritarian and centralized political system with virtually more checks and balances;
- ❑ The system was not transparent, lack of accountability, even no accounting standard and non functioning audits;
 - Bureaucracy was designed to absorb employment;
 - Reward/incentive and penalty system not functioning;
 - No performance measurement;
 - Uniform policy across ministries with different role and responsibilities;
 - Tainted with bad image—corrupt; abuse of power; low public respect and public distrust.

REFORM

- ❑ The change in laws governing fiscal policy and budget system
 - The State Finance Law;
 - The State Treasury Law;
 - The Accountability Reporting Law;
 - The State Audit Law.

- ❑ MOF as CFO;

- ❑ Checks and balances (shared responsibilities and budget right with parliament);

- ❑ Independent and effective State Audit Body;

- ❑ Rigorous reports and accountability standard and system;

- ❑ Establish procurement system—open, competitive and transparent.

BUDGET PRINCIPLES

- ❑ Unified budget– to avoid overlapping; to establish transparent and consistent budget;
- ❑ Medium Term Expenditure Framework (MTEF)– allow to have consistent medium planning, budgeting and executing;
- ❑ Performance Based Budgeting (PBB)— allocation of resource/budget based on performance/output/outcome.

BUDGET MECHANISM

- ❑ Government propose/submit medium term national plan (5 years) and annual working plan;
- ❑ Government propose budget—submit to the parliament;
- ❑ Parliamentary discussion and approval:
 - Underlying assumption, budget envelope, size of deficit/surplus; (law forbid Indonesia to have more than 3% of GDP deficit)
 - Budget allocation for each ministry;
 - Transfer/allocation to regions.

- ❑ Budget approval, implementation, execution;
- ❑ Budget accountability reports (3 months after December);
- ❑ Independent and external audit (finish 6 months after December);
- ❑ Accountability report and audit results → with Parliament (DPR).

IMPLEMENTATION OF BUREAUCRATIC REFORM

❑ To implement new sets of rules and governance needs:
effective—clean—efficient bureaucracy;

❑ Context:

62,000 staff/employees under MOF;

- 30,000 under DG Tax;

- 11,000 under DG Custom;

- 12,000 under DG Treasury;

- 5,000 under DG Asset Management;

- 4,000 HQ Office : DG Budget

DG Fiscal Balance

DG Debt Management

Fiscal Policy Office

Secretariate General

Inspectorate General

Stock Exchange Regulator and NFI

Training and Education Agency.

How we conduct the reform

- ❑ Establish a dedicated team—non structural team;
- ❑ Mandatory weekly meeting;
Brainstorming, teamwork, institutional mechanism
(less personalized)
- ❑ Develop a road map:
 - Mandate given by the law;
 - Public expectation and view;
 - Parliament pressure;
 - Create a “normal and logical” structure of incentive and reward.

STEPS

- Reorganize, restructure → strong checks and balances, division based on focused responsibilities;
- Define Jobs—describe responsibility and output;
- Establish Standard Operating Procedure (SOP);
- Establish rank based on risk, responsibility;
- Design rational remuneration system;
- Define performance and measurement;
- Enforce discipline.

CHALLENGES AND OPPORTUNITIES

- ❑ Legacy of past policies/structure—amount, competency;
- ❑ Huge scepticism—deep rooted problem, huge in magnitude and scale; risk and loof; no idea where and how to start; failures in the past.
- ❑ Strong political support:
 - President,
 - Political parties (majority),
 - Media and public;
 - KPK and Ministry of state apparatus;
- ❑ Gather the support through:
 - Public
 - Honest/frank about weaknesses;
 - Appoint a high/reputable echelon I
 - Prepare to sacrifice—budget.

Thank for your attention

The background is a solid blue color with a fine grid pattern. A faint, light blue world map is visible in the background. In the bottom left corner, there is a 3D-rendered globe of the Earth, showing continents and oceans, with a blue glow around it.