

BUFF/04/85

April 30, 2004

**Statement by the Staff Representative on Indonesia
Executive Board Meeting 04/43
May 3, 2004**

1. **This statement provides a factual update of economic and policy developments since the issuance of the staff report (EBS/04/54).** The staff appraisal remains valid.
2. **The April 5 parliamentary elections proceeded smoothly and peacefully.** Pending the completion of vote-counting, indications are that Golkar (ex-President Suharto's party) has won around 21 percent of the vote, with President Megawati's PDI-P party coming second with 19½ percent, and a couple of smaller parties doing better than expected. The focus is now shifting to the presidential election scheduled for July 5. The main candidates are: President Megawati (PDI-P); head of the People's Assembly (MPR), Amien Rais (PAN party); former Coordinating Minister for Security Affairs, Susilo Bambang Yudhoyono (Democrat party); and ex-general Wiranto (Golkar).
3. **Financial markets have reacted positively to the peaceful election outcome.** The stock market rallied to new highs in the weeks following the election, before falling back somewhat in recent days, in line with regional developments. The rupiah has remained broadly stable in recent weeks, at around Rp 8,600 – 8,700 per dollar. Yields on long-term government bonds have continued to decline. At the most recent auction on April 27, Rp 3 trillion in 7½ year bonds were placed at a yield of 10.7 percent, down from 11.6 percent in the previous auction in March.
4. **In mid-April, Bank Indonesia revoked the licenses of two small banks which were in violation of prudential requirements.** The closure of the banks was implemented smoothly, with coordination among the relevant agencies. Market sentiment was not adversely affected.
5. **A recent questionable bankruptcy ruling has again underscored the need to accelerate legal reforms to improve the investment climate.** On April 23, Prudential Life Assurance, the Indonesian subsidiary of a major United Kingdom-based insurance company, was declared bankrupt by the Central Jakarta Commercial Court, in response to a petition from a former consultant whose contract had been terminated. The ruling is widely considered as not supported by law, and echoes a similar finding of bankruptcy against the subsidiary of a Canadian insurance firm in 2002 (later overturned by Indonesia's Supreme Court). Prudential is appealing the decision, and senior officials have expressed serious concern over the ruling and their hope that it will be overturned eventually. The episode highlights the need to improve governance and proceed with judicial sector reforms.