SUMMARY

HERI ISPRIYAHADI. External Debt Management Strategy and Indonesia’s Economic Growth. Supervised by NUNUNG NURYARTONO, ADLER H. MANURUNG and DEDI BUDIMAN HAKIM

As undertaken by other developing countries, Indonesia still relies on external debt as a source in financing economic development. It has occurred due to the limited domestic financial resources. The external debt has been part of the history of Indonesia as the Old Order, the New Order and the recent Reform Order. During its path, the external debt was originally intended as a complementary resource in financing, but in its development, the external debt instead has become the main resource in offsetting the fiscal deficit and financing development.

Managing the external debt should be carried out in prudent ways. The external debt in a fair amount and its utilization in the productive sectors will drive the economic growth. And in contrast, the external debt in an excessive amount that is not optimal in utilization will be hampered in the process of economic development. It has been evidenced by the experience of crises that occurred in a number of countries, namely, Argentine, Russia, South Korea and Brazil for the adverse management of external debt. Indonesia has also undergone the economic crisis in 1997/1998 that one of the major fountainheads was managing the government and private external debt sector in imprudent ways (prudential borrowing). During the crisis, the Rupiah dropping sharply from IDR2.500 in 1997 to IDR16.000 in 1998 caused the manifold increase in the number of external debt. As a result, many companies were not able to repay their external debt. With respect to the matter, the Government had to undertake rescue measures to address difficulties in external debt repayment.

Currently, both government and private sector’s external debts constantly show uptrend. In fact, its number has passed Indonesia’s external debt during the crisis in 1997/1998. Accordingly, this is necessary to conduct a research on the impact of the external debt on the economic growth. This is to obtain empirical results whether Indonesia’s current external debt has either positive or negative impact on the economic growth. The research should separate the external debt into the government’s external debt and the private sector’s one, and subsequently, examined to test their impacts on the economic growth. By recognizing that investment in human capital is a significant modality in driving economic growth, this study will examine the impact of the public’s external debt and the fulfillment of basic needs on the economic growth. The fulfillment of basic needs is an indispensable factor in order to increase productivity, in turn, the favorable outcome of promoting the growth. The basic needs referred to the research of Wheeler (1980) are, namely, education, health and nutrition.

By employing the 3SLS (Three Stages Least Square) estimation method, it is obtained results that the government’s external debt has a negative impact on the economic growth. Meanwhile, the fulfillment of basic needs, except education variable, has significantly positive impact on the economic growth. The results showed that the improvement of human capital quality has an importance in promoting economic growth.
The people who have met the basic needs will increase productivity so as to contribute positively to promote economic growth. In contrast, when the economy grows highly, there is no assurance that the fulfillment of basic needs will increase. The underlying reason is that if the economic growth is only enjoyed by a limited circle, it means that economic development is not realized then the high economic growth will not push the fulfillment of basic needs.

Testing the model of the government’s external debt yields the coefficient of government’s external debt of -0.285 with p-value of 0.001 (significant level of 1%). This indicates that the current government’s external debt has passed the tipping point on the pattern of the debt Lafter curve. Increase in the private sector’s external debt of 1% may reduce the economic growth of 0.285%. With respect to the impact, the Government needs to be aware of this matter and, in turn, improving the quality of its external debt management.

The regression results by employing OLS (Ordinary Least Square) to examine the impact of the private external debt on the economic growth yield the coefficient of private sector’s external debt of -0.089 with p-values of 0.0017 (significant level of 1%). This results suggest that the private external debt is currently indicated having already passed the tipping point on the pattern of the debt Lafter curve. Increase in the private sector’s external debt of 1% may reduce the economic growth of 0.089%. It needs to watch out since the private sector’s external debt has increased significantly for the last five years. Favorable macroeconomic conditions, political stability and the predicate “investment grade” given by sovereign rating institutions have become the pull factors of foreign creditors and investors lending to companies operating in Indonesia.

By running the Analytical Network Process (ANP) in order to examine the strategy of the government’s external debt management, the result is that the strategy of switching the external debt into the domestic one is a strategy that gets top priority. Research carried out by in-depth interviews with 17 (seventeen) experts in external debt topics such as from Ministry of Finance, Bank Indonesia, Bappenas and economic analyst. To conduct interviews, they were guided by paired-wise comparisons questionnaire that had been prepared. After considering the Benefit, Opportunity, Cost and Risk (BOCR), it obtained the result that the overall outcome of the strategy of switching the external debt into the domestic one amounted to 0.076, much higher than the optimum currency strategy and the composition of the government’s external debt stood at 0.005. The results showed that the cost factor was a top priority as a benchmark in selecting the strategy of the government’s external debt. The next are risk, terms and conditions and politic. Switching external debt into domestic one is expecting to encourage the development of domestic market and diminish exchange rate risks.

Keywords: government’s external debt, private’s external debt, basic needs, 3SLS (Three Stages Least Squares), Analytical Network Process.