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# Petroleum and the Politics of Decolonization in Indonesia: A Study of Economic Development and Nationalism

Jan P. Wenger

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A Thesis submitted to the Global Studies Department, Colby College, Waterville, in partial fulfillment of the requirements for the degree of Bachelor of Arts (BA).

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Dr. Arnout van der Meer, History

Dr. Patrice Franko, Economics

**Abstract**

This study examines Indonesia's reliance and independence on foreign direct investment (FDI) and multinational corporations (MNCs) in the oil and gas sector. Analyzing historical, economic, and political primary and secondary sources and conducting qualitative interviews, the research explores the friction between economic development aspirations and nationalist sentiments. The study reveals that the current ambiguity surrounding FDI and MNC policies in Indonesia's oil and gas sector can be traced back to the country's economic decolonization and demonstrates that Indonesia's economic policies towards these factors shifted in the aftermath of political change. Since gaining independence, Indonesia has strived to balance the pursuit of economic sovereignty and the potential benefits of FDI and MNCs in driving growth and social welfare. This investigation pays particular attention to the interplay between the socialist Indonesian Constitution, specifically Article 33, and the more liberal regulations governing investments that led to the establishment of production-sharing regimes for resource extraction. The experiences of the oil and gas industry serve as a case study for broader discussions on natural resources.

***Keywords:*** *Foreign Investment, Economic Decolonization, Article 33, PERTAMINA, Resource Nationalism*

## Acknowledgements

Research in Jakarta. Tennis. A school shooting. Interviewing. Visa issues. Upcoming Graduation. Racing to finish my thesis this spring, I was often overwhelmed by the past, present, and future. The writing was hard, and the subject matter is complex. Yet, at the same time, I felt that Colby, especially the Global Studies major, gave me the opportunity of a lifetime. Arriving at the end of this seemingly interminable project, I feel grateful. I just spent an entire year thinking about and working on a project I care about. Moreover, as an undergraduate, I just spent three weeks in Indonesia interviewing experienced professionals. How many people are lucky enough to do that? And how many can count on the support and guidance of an incredible team?

As I complete this thesis, I cannot help but feel a sense of gratitude for the many people who have played a significant role in helping me reach this point. During the pandemic, I was lucky to fall under Dr. Patrice Franko's wings. One of the first decisions she encouraged me to make was where to study abroad. I had been discouraged by the language requirements in China and many closing programs across East Asia due to the Covid-19 pandemic. I pragmatically considered applying to programs in London or Amsterdam. During one of my first calls with Patrice, discussing study abroad opportunities, she said: What are you interested in? I said: "Asia" to which she responded: "Why then would you want to study abroad in your backyard? Long story short. We found a program at Yonsei University that supported entry-level Korean and was open during the pandemic. Despite all the uncertainty and bad omens, the experience at Yonsei was incredibly unique.

At a similar time, Colby paused its Hill to Hill program, and I was curious about career paths in Washington, DC. Again, it was Patrice who introduced me to Colby Alumni Ambassador Robert S. Gelbard (stationed in Indonesia from 1999 - 2001) and encouraged me to step out of my comfort zone and expose me and my thoughts to one of the most senior persons I have met in my short academic career. Every single contact and discussion with Ambassador Gelbard was a source of insight and encouragement. Everything started with brainstorming internship opportunities and the Ambassador offering me access to a network of supporting professionals in DC. During a 3AM phone call from Seoul, I was able to secure the opportunity for an internship position at the US-ASEAN Business Council, which redefined my focus on Southeast Asia and introduced me to the relevance of American Fortune 500 companies operating in the region. Thank you, Patrice, for providing me with the courage and the opportunities to follow my passion and get my project started. Thank you, Ambassador Gelbard, for being such a kind and guiding academic and professional mentor.

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I am thrilled to share that my project has soared to new heights through the fieldwork conducted in Jakarta this past January. I am immensely grateful for being awarded a scholarship from the David Hunt Fund and Davis Connects. Your support allowed me to embark on an unforgettable journey and connect with remarkable individuals in the industry.

Jennifer Yoder and Patrice, thank you for creating a sense of community in the Global Studies major by flexibly arranging workshops, providing feedback, and organizing sparring sessions. My parents, Felix and Danielle, watched more of this process unfurl than any of us expected. I could not have done without them and their unwavering encouragement.

To my roommates, the tennis team, and friends: We are all sad that something great is ending, but we share the excitement of what is coming. The hundreds of discussions and the thousands of minutes spent together will provide bonds that connect us for a long time to come - Thank you!

I started this project with so many questions. I end it with even more. One-hundred and twenty-three pages and 297 footnotes later, I don't think I'll ever look at the word foreign direct investment the same again. But I wouldn't have it any other way. To everyone who has played a role in helping me complete this thesis, thank you from the bottom of my heart. Your support, guidance, and encouragement have been invaluable, and I am grateful for the many opportunities you have provided me with.

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## List of Abbreviations

| | |
|---|---|
| ASA | Association of Southeast Asia |
| ASEAN | Association of Southeast Asian Nations |
| BKMP | Investment Coordinating Board |
| EU | European Union |
| FDI | Foreign Direct Investment |
| FLNG | Floating Liquified Natural Gas |
| G.A.M. | Gerakan Aceh Merdeka |
| GDP | Gross Domestic Product |
| IBRA | Indonesian Bank Restructuring Agency |
| ILRF | International Labor Rights Fund |
| IMF | International Monetary Fund |
| IOC | International Oil Corporation |
| ISI | Import-Substitution Industrialization |
| ILRF | International Labor Rights Fund |
| KADIN | Indonesian Chamber of Commerce and Industry |
| KNIP | Central Indonesian National Working Committee |
| MNC | Multinational Corporations |
| NIC | Newly Industrializing Countries |
| NAM | Non-Aligned Movement |
| NASAKOM | Nationalism, Religion, Communism |
| PKI | *Partai Komunis Indonesia* (Communist Party) |
| PNI | *Partai Nasional Indonesia* (National Party) |
| PSC | Production Sharing Contract |
| SBY | Susilo Bambang Yudhoyono |
| SEATO | South Asia Treaty Organization |
| SOE | State-Owned Enterprise |
| TNI | *Tentara Nasional Indonesia* (Indonesian National Armed Forces) |
| UN | United Nations |
| USAID | United States Agency for International Development |
| USINDO | United States-Indonesia Society |
| WTO | World Trade Organization |
| 1945 UUD | The 1945 State Constitution of the Republic of Indonesia |

# Chapter One:

## Introduction: Indonesia's Oil Production Paradox

The decline in Indonesia's oil production has been a persistent trend over the past two decades. According to data from Trading Economics (see Figure 1), there has been a marked reduction in the country's crude oil production, decreasing from a peak of 1'720 thousand barrels per day in December 1977 to 604 thousand barrels per day in October 2022. This decline made Indonesia a net oil importer since 2003.[1] The production of gas in Indonesia has exhibited a stable trend over the last two decades, attributed primarily to the reduced risk and cost associated with exploration. Data from Statista indicate that natural gas production has fluctuated between 60 to 70 billion cubic meters annually.[2] However, the Ministry of Energy and Mineral Resources of Indonesia (*Kementerian Energi dan Sumber Daya Mineral Republik Indonesia*, or *Kementerian ESDM* for brevity) predicts that Indonesia may potentially transition to a net importer of natural gas by 2040.[3] Despite abundant natural resources, Indonesia's output is failing. Why? The oil and gas sector present important lessons in understanding the country's independence and reliance on foreign direct investment and multinational corporations.

Oil and gas are frequently studied in conjunction with one another. Regarding production output, gas exhibits greater potential than oil at present and has shown notable growth over the previous two decades. In relation to the discovery and exploration development in Indonesia, gas production is approximately 30 years behind oil. Nevertheless, oil and gas are both natural resources and are frequently extracted by the same corporations. Consequently, concerning the

[1] Rulandari et al., "Valuation of Production Sharing Contract Cost Recovery Vs Gross Split in Earth Oil and Gas Cooperation Contracts in Indonesia and The Aspect of Public Service."
[2] BP. "Natural gas production in Indonesia from 1998 to 2021 (in billion cubic meters)." Chart. June 28, 2022. Statista. Accessed May 05, 2023. https://www.statista.com/statistics/265340/natural-gas-production-in-indonesia/
[3] Wenger Interviews, Jakarta 2023

relationship between the Indonesian government and foreign investment, oil and gas confront similar challenges, which will be elaborated upon in subsequent discussions.

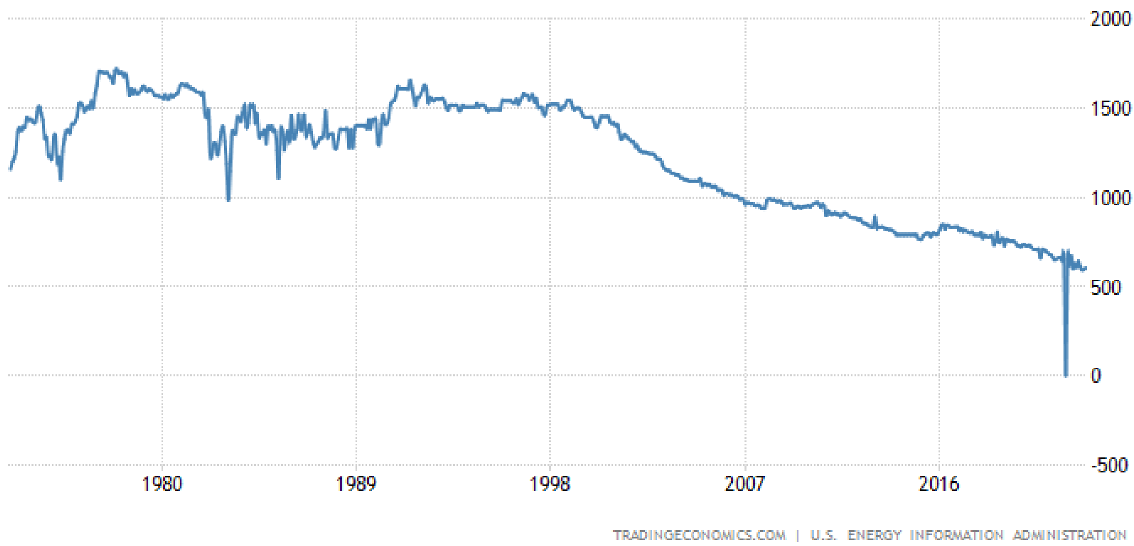


Figure 1: Indonesia Crude Oil Production: Data from Trading Economics, 1973 – 2022 Historical (in 1000 barrels per day)

The oil and gas sector can be segregated into three primary domains: upstream, midstream, and downstream. This study focuses on the upstream sector, which pertains to the exploration and production of oil and gas and encompasses the process of identifying and extracting resources in a safe and efficient manner. The midstream sector concerns the transportation and storage of oil and gas, while the downstream sector centers on refineries responsible for converting oil and gas into finished goods.

The Indonesian National Energy Council (*National Energi Council*) reported in 2022 that the maturity of oil-producing wells and new regulations primarily caused the decline in production. Although the number of newly established wells being brought into production is limited, sustaining the production output of older fields is increasingly challenging. The Ministry of Energy and Mineral Resources Regulation No. 42 of 2018 exacerbates this trend by requiring private

multinational corporations and state-owned enterprises to prioritize domestic energy requirements over favorable export market conditions, making exploration less appealing.[4] Consequently, aging fields and unfavorable market conditions constrain exploration efforts and contribute to diminishing production and Indonesia's net oil importer status.

Academic research highlights depleting oil deposits, reduced exploration efforts, and the deteriorating investment climate as the primary reasons for the production decline. Regarding the latter, research from Johns Hopkins University demonstrates that crude oil price volatility has generated uncertainty concerning the profitability of exploration for foreign investors and the Indonesian government. Further, as scholars from both Padjadjaran University in Bandung and Johns Hopkins University in Washington D.C indicated, the regulatory and legal uncertainty in Indonesia further deteriorated the fiscal terms for foreign investors. Lastly, Indonesia's inefficient bureaucracy can create a 'decision-making paralysis,' making the contract-based oil and gas operations time intensive and increasingly unattractive. [5]

Mirroring the diminishing oil production in Indonesia, several International Oil Companies (IOCs), such as the French Total, the American companies Chevron, ConocoPhillips, and Exxon Mobil, and the Anglo-Dutch Royal Dutch Shell, have suspended or paused development without renewing their government contracts.[6] The departure of these multinational corporations triggered a reduction in foreign direct investment in the oil and gas exploration sector.

Paradoxically, despite this withdrawal of IOCs, the Minister of Energy and Mineral Resources, Arifin Tasrif, publicly declared that Indonesia necessitates approximately 187 billion USD in upstream foreign investment in the upcoming decade.[7] According to an Indonesian

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[4] Wenger Interviews, Jakarta 2023
[5] Boyd et al., "A Note on Policies for the Oil and Gas Sector."; Rulandari et al., "Valuation of Production Sharing Contract Cost Recovery Vs Gross Split in Earth Oil and Gas Cooperation Contracts in Indonesia and The Aspect of Public Service."
[6] Mcbeth, "How Nationalism Destroyed Indonesia's Oil and Gas."
[7] "Indonesia Seeks $187bn in Upstream Oil and Gas Investment - News for the Energy Sector."

journalist, negotiations between the Italian multinational ENI and the government are currently underway.[8] However, IOCs and the Indonesian government have exhibited reluctance to enter into new contracts with each other. Instead, the state-owned company PERTAMINA acquired numerous contracts and operations previously possessed by IOCs.

PERTAMINA (*Pertambangan Minyak dan Gas Bumi Negara*)[9], the major state-owned oil and gas enterprise in Indonesia, faces challenges in maintaining production levels comparable to those of IOCs due to its limited technological resources and fiscal constraints. Despite significant technological advancements, PERTAMINA needs more technological capabilities and knowledge to extract oil and gas from large deep-sea reserves. In addition, since a Constitutional Ruling in 2012, PERTAMINA has been regulated by the Ministry of Energy and Mineral Resources and depends directly on the state budget. According to an oil and gas expert, even simple oil drilling necessitates capital expenditures, and if the government restricts PERTAMINA's fiscal capabilities, it becomes unfeasible for the state-owned enterprise to maintain the IOCs' production output.[10]

IOCs exacerbate the natural decline in oil production in Indonesia by withdrawing their operations from the country due to unfavorable investment climate and fiscal terms. Following the annulment of the 2001 Oil and Gas Law by the Constitutional Court, the Indonesian government regulates oil and gas through temporary regulations and the Special Task Forces for Upstream Oil and Gas Business Activities (*Satuan Kerja Khusus Pelaksana Kegiatan Usaha Hulu Minyak dan Gas Bumi*, or *SKK Migas* for brevity).[11] An international consultant observed that by failing to reform the legal and regulatory framework in the oil and gas sector to ensure political stability, the

[8] Wenger Interviews, Jakarta 2023
[9] PT Pertamina (Persero), founded in 1968, Revenue in 2021 USD 57 billion
[10] Wenger Interviews, Jakarta 2023
[11] Davidson, "The Demise of Indonesia's Upstream Oil and Gas Regulatory Agency."

government is knowingly sacrificing millions of USD in tax revenue from international oil and gas operations.[12]

*Problem Statement*

The ambiguity surrounding foreign direct investment and multinational corporations in Indonesia's extractive industries is a complex issue rooted in the country's political and economic decolonization. Despite declining natural reserves and increasing exploration challenges, the association between declining oil production and the exit of foreign capital and corporations from the oil fields reveals the presence of conflicting interests. This study examines the historical context of Indonesia's political and economic decolonization, exploring how the country navigated its independence and reliance on foreign direct investment and multinational corporations in the oil and gas sector. I aim to shed light on the current uncertainties surrounding foreign investment in natural resources and contribute to a more nuanced understanding of the challenges developing countries face in reconciling their own political and economic identities with the potential need for foreign investment.

Indonesia, a nation abundant in natural resources, has a long history of resource dependency spanning both the colonial and independent periods. According to Hal Hill and Donny Pasaribu, economists at the Australian National University, Indonesia experienced two resource booms after gaining independence. The first boom was driven by oil and gas in the 1970s, followed by a second boom fueled by coal, palm oil, and gas between 2005 and 2011.[13]

[12] Wenger Interviews, Jakarta 2023
[13] Hill and Pasaribu, "Some Reflections on Indonesia and the Resource Curse."

Indonesia's historical dependence on its natural resources, specifically in the upstream sector of oil and gas exploration and extraction, provides a significant case study for examining the country's broader relationship with and reliance on its natural resources. As highlighted by economist Peter Warr, oil constituted around 75 percent of the country's export earnings and over 60 percent of the government's revenues during the first boom, which peaked in the 1970s.[14] Moreover, American historian Theodore Friend observed that during this period, PERTAMINA's budget accounted for half of the entire national government's budget.[15] Given the focus on extraction and export, it is imperative to explore how the Indonesian government can optimize the use of its natural resources to serve the best interests of the Indonesian people. Can the fall in oil production output be traced to competing political objectives between economic development and economic decolonization and national control?

*Methodological Approaches*

Against this background, I conducted a series of interviews spanning a three-week period in January 2023. The interviewees comprised foreign counselors, independent consultants, active and retired oil and gas experts, and Jakarta-based journalists and think tanks. The interviews focused on exploring diverse political and economic perspectives, examining foreign direct investment and multinational corporations in the oil and gas specifically focusing on the upstream industry.

To gain a comprehensive understanding of Indonesia's evolving stance towards foreign direct investment and private multinational corporations, this study examines the interrelationship

[14] Warr, *Indonesia's Other Dutch Disease*, 1.
[15] Friend, *Indonesian Destinies*, 167.

between economic growth and natural resources in the context of colonialism, regional cooperation, and global integration. As a newly independent nation grappling with political and economic decolonization, Indonesia faced challenges in balancing the development of its distinctive political and economic identities. This study addresses the limitations of existing economic models and concepts that suggest insufficient progress by thoroughly analyzing historical and economic literature while incorporating primary sources to provide a more nuanced account of Indonesia's economic history.

Two fundamental questions shaped Indonesia's framework for foreign direct investment and multinational corporations: Firstly, should the country prioritize economic sovereignty and independence or integrate into the global economy, relinquishing some level of control? Secondly, if Indonesia engages with the global economy, what principles should be adopted to allow local stakeholders to participate in the benefits that arise – should capitalist or socialist principles be favored, or is there an intermediate way? Indonesian leaders have been faced with persistent challenges while navigating the intricate process of economic decolonization and developing an economic identity within the context of newly gained independence during World War II and the Cold War. The political discourse and legislation followed distinct patterns across the three discernible epochs since decolonization: the Sukarno Era (1945 – 1968), the Suharto Era (1969 – 1998), and the Modern Democracy (1998 – today). The project traces this historical pattern and evaluates its implications for the oil and gas industry.

## Literature Review

*Theories of Economic Development and Dependence*

The Indonesian experience balancing growth and independence has perplexed scholars. Economic scholars often viewed Indonesia's economy as underdeveloped from a neoliberal perspective. For example, Harvard economists Michael Porter and Christian Ketels highlighted Indonesia's wealth of resources, perceived underperformance in development, and instances of mismanagement in modern history, particularly in comparison with other Asian miracle economies such as China and India.[16] Even some economic historians, foremost Anne Booth, seem somewhat frustrated with Indonesia and often speak of "missed opportunities,"[17] referring to the fact that despite great diversity and considerable resource potential, Indonesia's economy struggled to modernize along the capitalist ideals of an Asian Tiger economy.[18] Economist Benjamin Higgins has even labeled Indonesia an "economic dropout."[19] This neoliberal perspective equates national success with economic growth and is prevalent among Western scholars.

The scholarly consensus for analyzing development through liberal economic indicators was reinforced by the World Bank's *East Asian Miracle* – a comprehensive study of newly industrializing countries (NICs) published in 1993. The report identified liberal economic policy, foreign investment, high savings, and cheap and skilled labor as the significant drivers of success for Indonesia and other East Asian economies between 1965 and 1990.[20]

The modernization theory emerged as a significant framework of development in the aftermath of World War II and has continued to influence many economists and political scientists. Modernization theory claims that all societies go through a similar development process, from

[16] Porter, Ketels "Indonesia."
[17] Booth, *The Indonesian Economy in the Nineteenth and Twentieth Centuries*.
[18] A tiger economy describes a country which undergoes steep economic growth and steady social development
[19] Lindblad, "Economic Growth and Decolonisation in Indonesia."
[20] World Bank, *The East Asian Miracle*.

traditional and agrarian to modern and industrialized. The theory suggests that as societies develop economically, they become more advanced, efficient, and democratic. Economist Walt Rostow argued that the "underdevelopment of the third world was not caused by capitalist exploitation but by the lack of incorporation of 'modern' institutions."[21] For Indonesia, modernization theory suggests that the country's economic growth and development can be achieved by incorporating Western-like policies and institutions, investing in technology, infrastructure, and industry, and promoting modernization and industrialization.

The notion of plural modernities challenged the Western-dominated modernization theory, which proposes a singular linear progression toward modernity. This alternative perspective contends that there are multiple and alternative modernities, each shaped by a given society's particular cultural, historical, and social contexts. It acknowledges the autonomy of non-Western nations in determining their path toward modernity and calls for a re-evaluation of development policies. Japan and South Korea are frequently cited as examples of successful modernization through swift transitions from import substitution to industrial export. In Indonesia, plural modernity is exemplified by the nation's recognition and embrace of its colonial past, diverse cultural heritage, and cautious engagement with contemporary global trends.[22]

Developmentalism is an economic theory, or some might argue a foreign policy tool that emerged in the 1950s and 60s as a response to the challenges posed by newly independent nations to classical economic models. It emphasizes the state's active role in promoting economic growth and development and, like modernization theory, posits a linear movement through stages of development. Additionally, developmentalism also uses capitalist indicators to define economic

[21] "W.W. Rostow, The Stages of Economic Growth."; Sherifat, "A Theoretical Analysis of the Concept of Informal Economy and Informality in Developing Countries."
[22] Bonnett, "Occidentalism and Plural Modernities."

success. Tony Smith noted that developmentalism was an American dominated school of thought to "containing the Soviet Union and dealing with national liberation movements throughout much of Asia and Africa."[23] Princeton Professor Donald L. Wyman added that "developmentalism emerged as a response to import-substitution industrialization" (ISI)[24] and led Latin American and Asian countries like Indonesia, to adopt export-based economic strategies in the 1970s.

During the 1970s, the modernization and developmentalism frameworks were challenged by the emergence of dependency theory. Tony Smith stated the "*dependencistas* … share the view that the power of international capitalism setting up a global division of labor has been … responsible for shaping the history of the South."[25] Dependency theory posits that the wealth of developed countries largely depends on the exploitation of resources and labor from poorer countries, which remain underdeveloped as a result. In this view, the global economic system is structured in a way that perpetuates this inequality, and emerging countries must break free from this dependency – non-align – to develop and become economically self-sufficient.[26]

Dependency theory is rooted in the ideas of communist theorist Vladimir Lenin, who highlighted the connection between capitalism and imperialism. In his book *Imperialism, the Highest Stage of Capitalism,* published during World War I, Lenin argued that control over foreign governments, capital, resources, and labor is the final stage of enterprises in a capitalist system. He maintained that imperialism creates a system based on coerced labor in the pursuit of cost minimization and profit maximization.[27] For newly independent nations like Indonesia, with recent memories of colonial oppression, the rejection of capitalism was a natural response post-independence. Lenin's theory and the later dependency perspective were seen as more suitable

[23] Smith, "Requiem or New Agenda for Third World Studies?," 534.
[24] Yu, *Dynamics and Dilemma*, 20–21.
[25] Smith, "Requiem or New Agenda for Third World Studies?," 544.
[26] Velasco, "Dependency Theory."
[27] Lenin, *V.I. Lenin*.

frameworks for developing nations like Indonesia.[28] Therefore, new nations' stage of development was analyzed not unit by unit but in the larger context of the world system.

In the context of world-system theory, American economist and historian Immanuel Wallerstein argued that the global economic system is divided into a core, a periphery, and a semi-periphery, with the core countries at the center of the global economy and the periphery and semi-periphery on the margins. He claimed that the global economic system is marked by uneven development and inequality, with the core countries benefiting disproportionately from the global economy. In contrast, the periphery and semi-periphery, and thus countries like Indonesia, are left behind.[29]

During the colonial period, there was a notable emphasis on extracting valuable resources from territories that had been conquered. The labor-intensive exploitation of resources resulted in economic difficulties for countries like Indonesia upon gaining independence. These colonial economies were heavily reliant on the exportation of natural resources, resulting in a lasting legacy of economies dependent on resource extraction. In addition to Wallerstein's argument about power dynamics, the Prebisch-Singer Hypothesis suggests that this reliance on primary commodity exports contributes to a structural tendency for developing countries to experience deteriorating terms of trade, particularly due to the expensive importation of manufactured goods.[30]

The concept of the resource curse emerged in economics during the 1950s, as scholars began to recognize a correlation between the abundance of natural resources and a country's economic performance. The basic premise is that there exists a close relationship between a country's resource abundance and poor economic growth.[31] According to economists Hal Hill and

[28] Smith, "The Underdevelopment of Development Literature."
[29] Wallerstein, *The Capitalist World-Economy*.
[30] Harvey et al., "The Prebisch-Singer Hypothesis," 367.
[31] Ross, "The Political Economy of the Resource Curse."

Donny Pasaribu from the Australian National University, Indonesia has largely been able to mitigate the effects of the resource curse due to its moderately open economy since the 1960s. In addition, they noted that during times of resource booms, economic nationalism, state intervention, and protectionist policies tend to increase.[32]

The theories of global patterns and systems bear significance in this study as they provide fundamental descriptions of power dynamics among nation-states. In this context, Indonesia's relationship with foreign direct investment and multinational corporations is shaped by the principles of these theories. While accepting foreign capital and infrastructure to extract resources for export can yield short-term economic gains, which may alleviate Indonesia's economic struggle and catalyze growth, relying on the extraction and export of resources for quick financial gains is neither sustainable nor advantageous. Given Indonesia's recent independence and aspirations for social welfare, economic sovereignty was a critical objective, and patterns of global dependence, including the reliance on foreign direct investment and multinational corporations, were generally opposed. The country's policies towards these principles, which will be examined in Chapters Three, Four, and Five, indicate the degree of dependence Indonesia was willing to accept in critical moments in Indonesia's modern history, including economic decolonization, political genocide, and financial crisis.

*Economic Decolonization in Indonesia*

As economic decolonization seeks to address the economic inequalities and imbalances created by and inherited from colonialism, it can be understood as a response to these various theories of global dependence, which highlight the disproportionate benefits enjoyed by the global

[32] Hill and Pasaribu, "Some Reflections on Indonesia and the Resource Curse."

north states at the expense of states in the global south. Thomas Lindblad, a prominent economic historian at Leiden University, researched economic globalization, economic development, foreign investment, and the political history and economy of Indonesia and Malaysia. Lindblad's critical analysis revealed that economic decolonization needs to be explored more in academic literature, warranting further attention and investigation.[33]

Economic sovereignty in newly independent nations like Indonesia proved challenging and did not coincide with political independence. Jeroen Touwen and Alicia Schrikker, economic historians at Leiden University, argued that for Indonesia "economic decolonization was a slower process than political decolonization and presented different problems."[34] Lindblad noted that Indonesia was "ill-prepared to manage a modern banking system, a smooth working industrial and trading sector, and an export-oriented estate agriculture"[35] following its independence. As a result, the legacy of the Dutch occupation had traumatizing and long-lasting effects on Indonesia's economy. Indonesian leaders faced the challenge of achieving economic self-sufficiency, functional national resources, and global positioning by negotiating a delicate balance between economic integration and national autonomy, capitalism and communism, and private foreign and state-controlled investments.

The need for a pragmatic approach to Indonesia's economic challenges is exemplified in President Sukarno's 1963 Independence Day speech, in which he declared, "I know that our economic problems do not have to be solved in a routine fashion. Our economic problems are the problems of the economy of a revolution."[36] This statement not only characterizes decolonization as an ongoing revolution but also challenges conventional economic ideologies such as neo-

[33] Lindblad, "Economic Growth and Decolonisation in Indonesia."
[34] Schrikker and Touwen, *Promises and Predicaments. Trade and Entrepreneurship in Colonial and Independent Indonesia in the 19th and 20th Centuries*.
[35] Lindblad and Post, *Indonesian Economic Decolonization in Regional and International Perspective*, 1.
[36] Siegel, "Revolutionary Stink and the Extension of the Tongue of the People," 16.

liberalism and classical statism, which advocate for a free-market economy with minimal state intervention and active state control over the economy. By rejecting these approaches, Sukarno suggested an alternative economic ideology that prioritizes economic sovereignty for Indonesia while not completely rejecting foreign investment and trade.

Despite declaring political independence in 1945 and achieving political sovereignty in 1949 after a four-year armed struggle against the Dutch colonizers, Indonesia, as a new nation-state, encountered significant challenges related to economic development and decolonization in the 1950s, 60s, and even 70s. Sukarno and his fellow political and economic leaders inherited an economy abundant in natural resources but deficient in production capabilities, infrastructure, and expertise. Regarding foreign direct investment and multinational corporations, Indonesia confronted a dilemma: prioritize economic growth and social welfare by accepting foreign investment and multinational corporations, thereby relinquishing some degree of national control, or prioritize economic sovereignty, national control, and self-sufficiency at the expense of economic gain.

The economic development of Indonesia presented a multifaceted dilemma to its leaders. This predicament manifested itself in various facets of governance, such as global integration, foreign policy, state form, and production (see Figure 2). This solution space, represented by non-binary sliders, illustrates the fluid and pragmatic nature of Indonesian leaders' attitudes and the resulting fluctuations in the alignment of the country's economy. This graphical representation will be used as a point of reference in Chapter Two. It can be applied throughout all chapters when analyzing the shifting of Indonesian leaders' attitudes and their effects on the policy pendulum and the national economy.

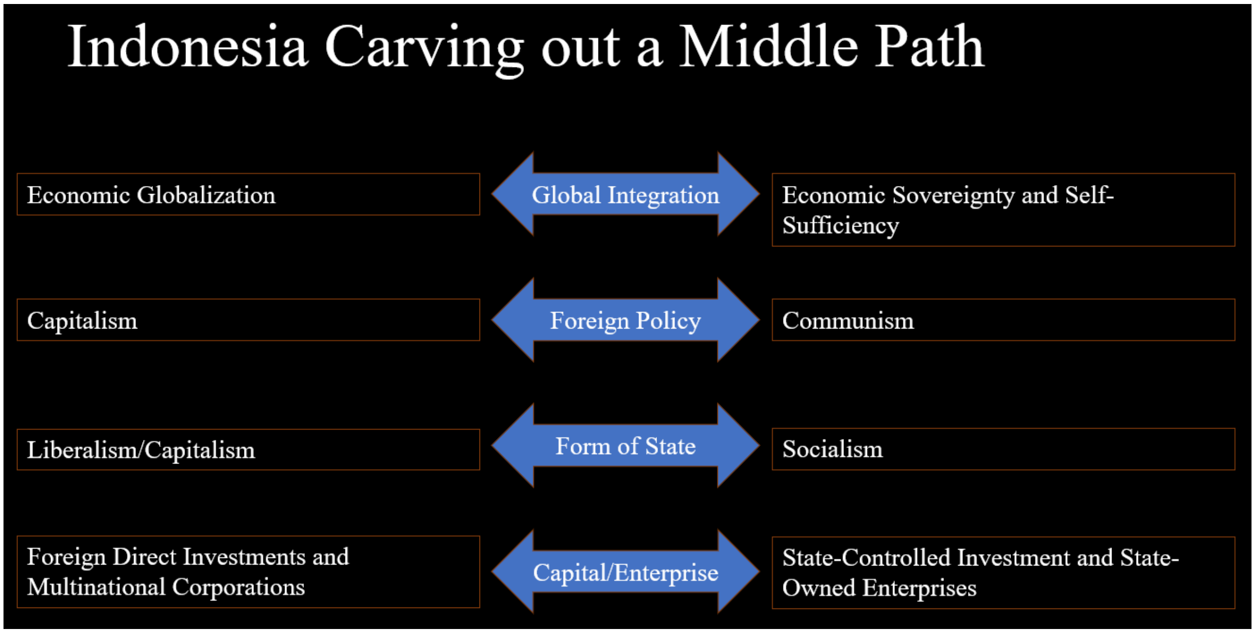


Figure 2: Indonesia Carving out a Middle Path: A visual illustration of the framework in which Indonesian leaders made decisions about foreign direct investment and private enterprises – own representation.

## Chapter Two:

## Watersheds: A Window into Indonesia's Economic Position

A thorough comprehension of the process of economic decolonization in Indonesia requires an examination of the historical and political context, including both external and internal trigger events that have influenced the country's development and positioning in relation to the economic poles and global integration described above. Authors Schrikker and Touwen argued that colonial Indonesia and independent Indonesia should not be viewed as two separate narratives but as an integral development path.[37] Some economists and economic historians situated their work in one of many eras, spanning late colonial (1870 – 1942), Sukarno and post-independence (1945 – 1965), Suharto (1968 – 1998), and post-Suharto (1998 – present).[38] However, Anne Booth proposed the use of trigger events as a way to understand Indonesia's economic history, identifying three major "watershed moments" in Indonesia's modern history since independence: the declaration of independence in 1945, the Indonesian mass killings and regime change in 1965 – 1968, and the Asian Financial Crisis and the emergence of democracy in 1997 – 1998.[39]

This chapter seeks to broaden Booth's framework by exploring foreign policy events that have influenced the views of Indonesian leaders regarding global integration and its associated economic policy. The level of integration in the global system at a particular moment indicates the degree to which the state allowed foreign direct investment and multinational corporations to operate. In addition to the internal watershed moments, this chapter evaluates the impact of foreign policy moments on economic openness or closeness, including events such as the 1955 Bandung

[37] Schrikker and Touwen, *Promises and Predicaments. Trade and Entrepreneurship in Colonial and Independent Indonesia in the 19th and 20th Centuries*.
[38] Schrikker and Touwen, *Promises and Predicaments. Trade and Entrepreneurship in Colonial and Independent Indonesia in the 19th and 20th Centuries*.
[39] Booth, *Economic Change in Modern Indonesia*.

Conference, Indonesia's participation in the Non-Alignment Movement (NAM), Confrontation (*Konfrontasi*) and the Crush Malaysia Campaign in 1963, and the establishment of the Association of Southeast Asian Nations (ASEAN) in 1967. These moments significantly shaped economic policy-making and impacted Indonesia's economic development and relations with other countries. The second half of this chapter examines the domestic economic reforms concerning foreign direct investment and private enterprises, particularly in the oil and gas sector, against the backdrop of these internal and external watershed moments. Figure 3 provides a visual timeline of these trigger events that impacted economic policymaking and shall serve as a reference throughout this chapter.

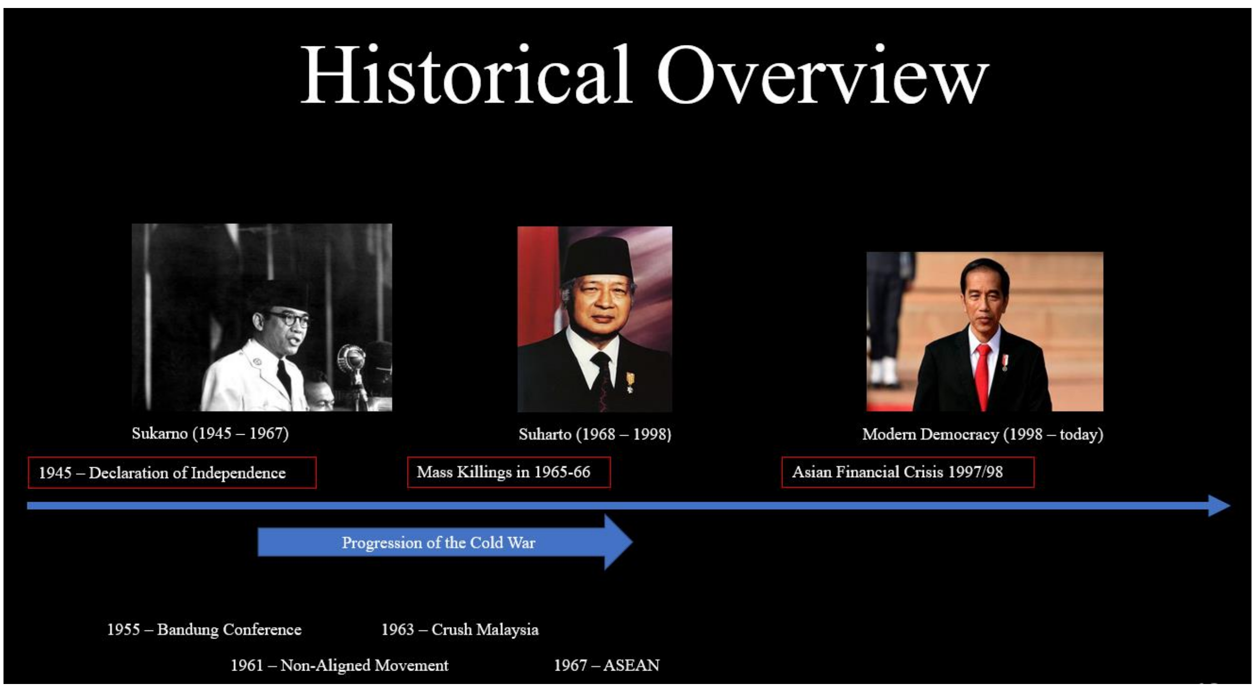


Figure 3: Key Historical Moments in Indonesia – own representation based on: Booth, Anne. *Economic Change in Modern Indonesia: Colonial and Post-Colonial Comparisons*. Cambridge: Cambridge University Press, 2016. https://doi.org/10.1017/CBO9781316271438.

### The 1945 Declaration of Independence

Following Indonesia's achievement of political autonomy in 1945 and its confirmation through a four-year armed struggle against Dutch colonizers in 1949, the new nation-state and its leaders faced a series of challenges related to economic development and decolonization. Under President Sukarno, the top priority was to regain control of the national economy, for which he implemented a range of economic policies. The government actively intervened through robust state measures, such as nationalizing critical industries like oil and banking, exerting bureaucratic control over manufacturing sectors, and introducing regulations to govern trade activities and reduce dependence on foreign markets. Additionally, diplomatic efforts increased through participation in the Non-Aligned Movement (NAM).[40]

During the 1950s, Indonesian leaders generally displayed hostile attitudes towards foreign investment and foreign private enterprises. Hla Myint, a Burmese economist, claimed that Indonesia became an "inward-looking country" under Sukarno, largely rejecting foreign investment, foreign aid, and immigration.[41] Anne Booth also noted that "most of the Dutch enterprises taken over in 1957 – 1958 became state enterprises, and the state-owned sector ... produced about 20 percent of GDP by 1960."[42] Stanford University political scientist Franklin Weinstein described Sukarno as pursuing an "all-out confrontation with the forces of exploitation."[43] These actions and attitudes strongly emphasized economic self-sufficiency and independence during this period and reflected the fear of substituting colonial oppression with capitalist or communist dependencies in the world system.

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[40] Booth.; Myint, "Inward and Outward-Looking Countries Revisited."
[41] Myint, "Inward and Outward-Looking Countries Revisited," 39.
[42] Booth, *Economic Change in Modern Indonesia*, 45.
[43] Weinstein, *Indonesian Foreign Policy and the Dilemma of Dependence*, 19.

The Declaration of Independence in 1945 marked a notable shift in the attitudes of Indonesian political leaders, as their focus shifted from global integration to prioritizing economic sovereignty (see Figure 2). In foreign policy, Indonesian leaders pursued an intermediate approach, steering clear of aligning with either pro-American capitalism or pro-Russian communism. Vice President Mohammed Hatta introduced the term *bebas-aktif* (free and active) to characterize Indonesia's efforts to balance the Cold War blocs while advocating for world peace and national unity.[44] Theoretically, Indonesia's post-independence shift towards economic sovereignty and its strategic balancing in foreign policy would imply increased state intervention and decreased activities related to foreign direct investment and multinational corporations. The impact of these shifting attitudes in Indonesia, under President Sukarno, on economic and legal reforms and, subsequently, on the oil and gas industry will be thoroughly examined in Chapter Three.

**The 1955 Bandung Conference**

Indonesia was not alone in facing questions about independence and dependency. Many other countries did so as well. Indonesian leaders' unwillingness to commit to and be influenced by either capitalist or communist dependencies is strongly represented in their foreign policy in the post-independence years. This is especially well captured in the history of the Non-Aligned Movement (NAM) and in the later creation of ASEAN – both organizations are rooted in the intellectual discourse that first emerged on a global scale at the Bandung Conference.

The Bandung Conference, held in Indonesia in 1955, was a significant event in the history of international relations. It brought together 600 leaders from mostly colonized and newly independent nations in Africa and Asia to discuss and promote socio-economic cooperation and

[44] Sukma, "Indonesia's *Bebas-aktif* Foreign Policy and the 'Security Agreement' with Australia," 232–36.

solidarity among these countries. The conference was influenced by a desire to assert independence and avoid dependency on either the capitalist or communist blocs during the Cold War. In other words, to be non-aligned.

Richard Wright, an African American novelist, traveled to Indonesia to observe the conference. His chronicles, *The Color Curtain*, have become an academic foundation for understanding the *zeitgeist* among formerly colonized nations and the unity of 'colored people.'[45] Wright observed that "Indonesia has taken power away from the Dutch, … but she does not know how to use it."[46] Here he referred to the numerous economic and political challenges Sukarno, the Indonesian government officials, and many other new nation-states' leaders faced in the 1950s. One economic challenge was the trade-off between gaining control over the national economy and the positive incorporation of foreign direct investments and multinational corporations.

The intellectual discourse at the Bandung Conference centered on issues of independence, economic decolonization, unity in rejecting Cold War ideology, advocating for peace, and fostering economic collaboration. This discourse was influenced by the ideas of Vladimir Lenin, who argued that capitalism, colonialism, and imperialism are interconnected and driven by the pursuit of profit maximization and cost minimization.[47] The participating countries at the conference, many of which recently gained independence from colonial rule, expressed a shared resentment of colonialism and, based on Lenin's analysis, a broader resentment of capitalism.

At the Bandung Conference, the concept of neo-colonialism emerged on the global stage as a common concern among the participating countries. Many political leaders, including Sukarno, felt strongly about avoiding the replacement of colonial oppression through other foreign

[45] Wright, *The Color Curtain*.
[46] Lee, *Making a World after Empire*, 53.
[47] Lenin, *V.I. Lenin*.

power politics. According to Ghana's first Prime Minister Kwame Nkrumah, neo-colonialism is the continued economic and political dependence of developing nations to the world system.[48] In Bandung, Sukarno famously stated that "colonialism also has its modern dress, in the form of economic, intellectual and physical control."[49] As such, the discussions at the conference were shaped by a desire to break free from former capitalist oppressors and catch up in development while also maintaining independence. This sentiment towards foreign control and dependence contributed to considering foreign direct investment and multinational corporations in Indonesia as cautionary tales seen ideologically as neo-colonial tools but practically as catalysts for growth.

**The Non-Aligned Movement**

The Non-Aligned Movement (NAM) emerged in 1961 as a direct consequence of the principles and concepts deliberated upon during the Bandung Conference of 1955. The participating nations aimed to establish a more peaceful and collaborative global order and demonstrated their sovereignty by refusing the Cold War's false choice between capitalism and communism. The organization significantly impacted the foreign policy of its member states and promoted dialogue and cooperation on a broad spectrum of issues such as development, disarmament, and human rights. For Indonesia, the NAM functioned as a crucial foreign policy tool, enabling its leaders to navigate the challenges of post-colonial economic dependence and development. Franklin Weinstein posited that Indonesia's perception of the global economy as hostile influenced its foreign policy, prioritizing independence.[50] This perception was shaped by

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48 Kwame, *Neo-Colonialism*.
49 Bandung, "Opening Address given by Sukarno (Bandung, 18 April 1955)."
50 Weinstein, *Indonesian Foreign Policy and the Dilemma of Dependence*.

Indonesia's historical context and apprehension towards neo-colonial dependencies, leading to a foreign policy stance aimed at averting new forms of economic reliance.

The NAM was not just a weapon of the weak but rather a vehicle for promoting its member states' specific interests and independence on the global stage. Professor of Southeast Asian Studies, Itty Abraham, challenged the commonly held view that the NAM was simply a tool used by weaker nations to protect themselves against the pressures of the bipolar international system during the Cold War. Abraham argued that the NAM was instead a bloc of 25 developing African and Asian nations, eventually growing to 120, that played a significant role in international decolonization and provided a platform for intellectual opposition to capitalism and communism.[51]

The Bandung Conference and the subsequent NAM significantly directed Indonesian leaders' attitudes away from global integration and towards integration and cooperation among newly independent nations (see Figure 2). The concept of neo-colonial dependence further fueled the rejection of capitalism as a foreign policy approach and form of governance. Theoretical implications suggest that the Bandung Conference and Non-Aligned Movement influenced the Indonesian leadership during the 1950s and early 60s to also reject capitalist elements such as foreign direct investment and private multinational corporations. As elucidated in Chapter Three, President Sukarno, in particular, actively resisted these factors to uphold principles of equality and respect on the global stage rather than risking financial dependency that could potentially result in embarrassment.[52]

[51] Abraham, "From Bandung to NAM."
[52] Sukarno, *Sukarno*, 297.

**Radical Confrontation**

The non-aligned foreign policy of Indonesia grew increasingly hostile in the late 1950s, as evidenced by the anti-imperialist discourse that emerged in light of the West New Guinea dispute and Indonesia's Crush Malaysia campaign (known as *Konfrontasi* or *Ganyang*). Firstly, from 1950 – 1962, Indonesia engaged in an armed conflict with the Netherlands over territorial claims in West New Guinea (also known as West Irian). This dispute, which involved a former colonial power, fueled anti-imperialist sentiments in Indonesia. Secondly, the creation of Malaysia in 1963 under British protection further heightened these sentiments, as it was perceived that former colonizers were influencing territories surrounding Indonesia. As a result, Indonesia launched the Crush Malaysia campaign in 1963, characterized by aggressive military intervention, particularly in the territories around Borneo (known as *Kalimantan* from an Indonesian perspective).[53]

In light of the *konfrontasi* policy, the perception of Indonesia in the international arena changed. Indonesia's role of standing up for the oppressed people of the third world turned into the role of an aggressor. Dewi Fortuna Anwar, a former foreign policy advisor to President Suharto, stated that Indonesia withdrew from the United Nations (UN) because they offered Malaysia, which was still strongly influenced by British capital, a seat on the General Assembly.[54] Geoffrey Robinson added that Indonesia's UN withdrawal was motivated by a disdain for the domination of the international organization by imperialist and neo-colonial powers.[55] Indonesia's relationship with Western capitalist nations and the international system further deteriorated as Sukarno withdrew from the World Bank, Interpol, and the International Monetary Fund (IMF) in 1965.[56]

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[53] Weinstein, *Indonesian Foreign Policy and the Dilemma of Dependence*, 301–30.
[54] Anwar, *Indonesia in ASEAN*, 28.
[55] Robinson, *The Killing Season*, 42.
[56] Ricklefs, *A History of Modern Indonesia since c.1200*, 316.

On August 17, 1965, President Sukarno's anti-imperialist discourse reached its zenith during Indonesia's Independence Day commemoration. In his speech, he proclaimed the establishment of an anti-imperialist axis encompassing Jakarta, Phnom Penh, Hanoi, Beijing, and Pyongyang. He advocated for the arming of the people and insinuated that the army generals were impeding his efforts. It is noteworthy that Sukarno sought to bolster Indonesia's relationships with the Soviet Union and China, both of which provided Indonesia with small arms during this period.[57]

The escalation of anti-imperialist discourse and the adoption of a confrontation policy by Indonesia in the 1960s moved the country toward a trajectory of economic sovereignty and a corresponding rejection of capitalism (see Figure 2). This shift in foreign policy led to closer ties with the communist bloc, as Sukarno sought support from China and the Soviet Union. Indonesia's more assertive foreign policy was accompanied by a growing aversion to foreign direct investment and multinational corporations within its domestic economy. In fact, from 1957 through 1962, Indonesia nationalized nearly all internationally-owned companies, exemplifying this rejection of foreign economic influence.

## Mass Killings and the Rise of Suharto

The *konfrontasi* policy, implemented by President Sukarno in the early 1960s, disrupted the balance of power within Indonesia and contributed to the military coup and mass killings starting in 1965 and the regime change in 1967 – 1968. General Suharto (*Soeharto*) and the army, who opposed communism and controlled significant parts of private production, were worried that Sukarno and especially the PKI (Communist Party of Indonesia) were using the confrontation as

[57] Ricklefs, 316.; Anwar, *Indonesia in ASEAN*.

a pretext to raise the Indonesian army's troops and consolidate domestic power.[58] As Sukarno sought to strengthen the Indonesian army in the face of perceived threats and the PKI gained political power, the country became increasingly politically unstable.[59] This domestic instability, combined with international isolation and the withdrawal of foreign investments, negatively affected the Indonesian economy.

A pivotal event during this period was the Indonesian Massacres of 1965 – 1966. The military, led by General Suharto, was implicated in the killing of an estimated 78'500 to 3 million individuals who were allegedly sympathetic to communism.[60] The political context of the Cold War played a role in fueling these atrocities. The mass killings and subsequent regime change from President Sukarno to President Suharto marked a significant turning point in Indonesia's political and economic landscape, characterized by heightened militant polarization and a shifted stance towards the global economy, capitalism, and the United States.[61]

One aspect that warrants further consideration, particularly in light of the impact of foreign investments, is the role of the United States during the Indonesian Mass Killings and subsequent regime change. This historical period was marked by anti-colonial nationalism and Cold War politics, during which various global powers, including the United States, Britain, China, and Russia, sought to exploit the instability in Indonesia to increase their influence in the region.

In alignment with its containment strategy and concurrent Operation Rolling Thunder in North Vietnam, the United States provided "direct military and financial support to armed rebels" and later pinned its hopes on the Indonesian Army, offering substantial military training and aid with the aim of eradicating the PKI and ousting Sukarno from power.[62] The involvement of the

58 Anwar, *Indonesia in ASEAN*, 28.
59 Robinson, *The Killing Season*, 38.
60 Robinson, 120.
61 Robinson, 82.
62 Robinson, 113–17.

United States in these events underscores the intricate international dynamics that were at play in Indonesia during this period.

The regime change from President Sukarno to General and President Suharto in the late 1960s signified a turning point in Indonesia's political and economic landscape (see Figure 2). The period's violence and political instability significantly framed Indonesia's foreign policy, as the new Suharto government sought to establish itself as a more reliable and stable partner in the international community to stimulate economic development.[63] Consequently, the regime change marked a shift in Indonesia's attitude towards integration into the regional and global economy, as President Suharto pursued policies that were more open to foreign investment and multinational corporations.

The Suharto government actively eradicated communism from various aspects of Indonesian society, including social, economic, and military domains. As a result, the government formulated its foreign policy and economic governance on principles more conducive to capitalism. Notably, the government had a vested interest in containing communism. Following the mass killings, it became beholden to the pro-capitalist stance of the United States, which provided significant support. Consequently, with Suharto's uprising, the pendulum swung towards capitalism.

The Suharto government adopting a more pro-capitalist stance directly and discernibly impacted Indonesia's economic policies, significantly changing the legal and economic frameworks on foreign direct investments and promoting multinational corporations. Hla Myint argued that this shift in policy engendered an outward-looking orientation for Indonesia, moving away from its previous anti-imperialist crusade.[64] Franklin Weinstein also observed that Indonesia

[63] Anwar, *Indonesia in ASEAN*, 33–45.
[64] Myint, "Inward and Outward-Looking Countries Revisited."

adopted a more favorable stance towards Western economic aid and capital investment, prioritizing regional and global cooperation.[65] Chapter Four will thoroughly examine the evolving attitudes toward foreign investment and multinational corporations, with a particular emphasis on the oil and gas sector and the resultant legal and economic reforms that ensued.

### The Birth of ASEAN

In the aftermath of the Indonesian Massacres and the regime change from Sukarno to Suharto, Indonesia's attitude towards the international system, capitalism, and specifically the United States, underwent a significant transformation. One of the most notable changes was Indonesia's increased openness to economic cooperation and integration with the regional and global economy, including founding organizations such as the Association of Southeast Asian Nations (ASEAN) in 1967 and the Indonesian Chamber of Commerce and Industry (KADIN) in 1968. Prior to this period, Indonesia had been largely hostile towards foreign investment and multinational corporations. However, the economic challenges faced by the country in the aftermath of the massacres and the desire to stabilize the political situation led to a shift towards a more pro-business and foreign aid stance.[66]

The Bandung Conference and the NAM established the groundwork for regional cooperation in Southeast Asia. However, tension among newly independent nations, driven by nationalism and resentment towards major powers and their ideologies, characterized the aftermath of World War II and hindered cooperation beyond these initiatives. Indonesia declined to join the Southeast Asia Treaty Organization (SEATO) in 1954, a pro-Western defense treaty that aimed to

[65] Weinstein, *Indonesian Foreign Policy and the Dilemma of Dependence*, 19.
[66] Weinstein, 225.

safeguard Southeast Asia from communist expansion.[67] In 1961, Indonesia refused to enter the Association of Southeast Asia (ASA), which Malaya, the Philippines, and Thailand established. In their book, Deputy Secretary Anwar and her father Khaidri noted that "Indonesia had formerly accused ASA of being nothing more than a colonial tool and an extension of SEATO; so, joining it seemed a deliberate violation of the *bebas aktif* [68] (free and active) foreign policy principle."[69] Anwar further argued that "Indonesia was too proud to become a junior member of an association in which it would be the largest and most populous state."[70] In 1963, tensions in the region dismantled Maphilindo, an initiative involving Malaya, the Philippines, and Indonesia, due to a territorial dispute over Sabah and the adoption of Indonesia's aggressive foreign policy of *konfrontasi*, following the formation of Malaysia under British oversight.[71] ASA and Maphilindo disintegrated due to a lack of leadership, rising tensions between Kuala Lumpur and Manila over the status of Sabah, and Indonesia's increasingly aggressive and confrontational foreign policy.[72]

Establishing ASEAN in 1967 was a significant development in the history of Southeast Asian regionalism, particularly given the context of hostility towards foreign powers and a focus on independence. The original member states of Thailand, the Philippines, Malaysia, Singapore, and Indonesia set aside their differences and signed the ASEAN Declaration in Bangkok, basing the organization on the principles of the Bandung Conference. According to Kishore Mahbubani and Jeffery Sng, the main factor driving these nations to join forces was a shared fear of communism, as all of the original ASEAN member states had experienced domestic conflicts with

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[67] Friend, *Indonesian Destinies*, 56–58.
[68] *Bebas aktif* was a foreign policy doctrine outlined by Indonesian Vice President Hatta that put Indonesia's independence first and reinforced a neutralist stance.
[69] Anwar, *Indonesia in ASEAN*, 50.
[70] Anwar, 50.
[71] Sussman, "Macapagal, the Sabah Claim and Maphilindo."
[72] Anwar, "ASEAN and Indonesia."

communist groups and were concerned about the spread of communism internationally.[73] Anwar further suggested that the new Indonesian President, Suharto, had special incentives to oppose communism and saw the creation of a weak regional institution like ASEAN as a way to restore regional and international order.[74] Siti Daulah Khoiriati Djaldan noted that as chair of ASEAN, Suharto felt he could participate in regional and foreign integration without giving up national economic control.[75]

The establishment of ASEAN marked a significant milestone in institutionalizing Indonesia's evolving attitudes and growing integration into the global and regional systems (see Figure 2). ASEAN served as a pivotal foreign policy instrument for Indonesia, bolstering cooperation among Southeast Asian nations that shared common concerns about communism and developed a pro-capitalist orientation. As such, ASEAN played a central role in facilitating Indonesia's connections with the international system, spurring foreign direct investment, and encouraging greater participation of multinational corporations in the country.

### The Asian Financial Crisis and Reformasi

In 1997, the Suharto government of Indonesia faced a surge of political instability and violence in regions such as Aceh, Iran Jaya, and East Timor, threatening economic stability. The army's brutal crackdowns in response drew criticism and heightened scrutiny of the government's actions. However, despite these challenges, renowned economists, and respected organizations, including the World Bank and the Asian Development Bank, lauded Indonesia's macroeconomic management, as discussed by Anne Booth.[76] Andrew Sheng noted that the country's economic

[73] Mahbubani and Sng, *The ASEAN Miracle*.
[74] Anwar, *Indonesia in ASEAN*, 33–45.
[75] Djaldan, "The Politics of Foreign Investment Liberalization in Indonesia with Particular Reference to the Early 1990's," 745.
[76] Booth, *Economic Change in Modern Indonesia*, 89.

growth under Suharto's leadership depended on its political stability and foreign debt. As such, the prevalence of political instability not only posed risks to the domestic economy but also undermined the confidence of loan lenders.[77]

Notwithstanding the favorable evaluation of Indonesia's macroeconomic management in 1997, the Asian Financial Crisis in 1998 severely affected the country's economy. The crisis, which originated in Thailand, resulted in a sharp depreciation of the national currency, widespread unemployment, and inflation. These economic challenges fueled protests, riots, and demands for political reform, further increasing pressure on Suharto's regime to address the nation's economic and political issues. Consequently, Suharto resigned from office in May 1998, leading to a transition of power to a new government under President B.J. Habibie.

According to Booth, the World Bank identified "a rapid build-up of private external debt, a flawed banking system, deteriorating standards of governance and rising corruption, and political uncertainty"[78] as the primary causes of the financial crisis in Indonesia. Additionally, Sheng stated that Suharto's liberalization policies, especially in the 1990s, led to "credit growth (coming) at the expense of credit quality."[79] The combination of Indonesia's historical association of political instability with market failure and the worsening of macroeconomic indicators caused investors to become concerned. Sheng noted that foreign lending fell as a result, and the International Monetary Fund (IMF) did not act as a creditor of last resort, leaving the overleveraged and overextended Indonesian economy vulnerable to the interconnected global economy.[80]

The aftermath of the Asian Financial Crisis in Indonesia witnessed a notable emphasis on democratic legitimacy and economic and legal reforms. As pointed out by Booth and IMF

[77] Sheng, *From Asian to Global Financial Crisis*, 224.
[78] Booth, *Economic Change in Modern Indonesia*, 91–96.
[79] Sheng, *From Asian to Global Financial Crisis*, 236–39.
[80] Sheng, 249–50.

economist Olivier Frecaut, one of the significant measures undertaken was the nationalization of most private banks by the Indonesian Bank Restructuring Agency (IBRA), as part of broader efforts to stabilize the economy.[81] These endeavors were geared towards addressing the root causes of the crisis and establishing a robust foundation for sustainable economic growth in the long term.

In 2004, Susilo Bambang Yudhoyono (SBY), who received part of his education in the United States, assumed office as Indonesia's first democratically elected president. During his presidency, SBY implemented a series of economic reforms that prioritized the role of private enterprises and foreign direct investment. These reforms encompassed business-friendly policies, a continuation of Suharto's ASEAN-centric and outward-looking foreign policy, increased foreign and private investments, as well as attempts to restructure and privatize state enterprises.[82] Despite challenges in privatizing state-owned enterprises, Indonesia's trade policies underwent a significant transformation, becoming less protectionist and more diversified compared to the Suharto era. Moreover, the Indonesian economy experienced growth fueled by high commodity prices leading up to the 2007 – 2008 Financial Crisis and could weather the subsequent Global Financial Crisis relatively well.[83]

In 2014, Joko Widodo (Jokowi) succeeded SBY as President of Indonesia. President Jokowi has since pursued a delicate balancing act, striving to attract foreign direct investment and promote economic openness and integration while also safeguarding key industries through active state intervention and addressing concerns of economic self-sufficiency. It is noteworthy that Indonesia's economy continues to depend on resource-based exports, a characteristic that persists despite ongoing efforts to diversify the economy.[84] In addition, Indonesia has actively engaged

[81] Booth, *Economic Change in Modern Indonesia*, 101.; Frécaut, "Indonesia's Banking Crisis."
[82] Booth, *Economic Change in Modern Indonesia*, 107–8.
[83] Booth, 107–18.
[84] Bland, *Man of Contradictions: Joko Widodo and the Struggle to Remake Indonesia*, 54–89.

with the global economic system, gaining leverage and even assuming leadership. An example of this engagement was Indonesia's hosting of the G-20 Summit in 2022, signifying the country's increasing prominence and influence on the international economical stage.

The Asian Financial Crisis significantly influenced the attitudes of Indonesian leaders toward global integration, particularly in light of the country's transition to democracy and the embrace of democratic values (see Figure 2). Initially, the state intervened in the aftermath of the crisis. However, subsequent economic and legal reforms have led to the re-privatization of significant portions of the economy, and capitalist principles have remained largely consistent with the approach during President Suharto's era. Notably, there has been an increase in foreign direct investment and the participation of multinational corporations since the Asian Financial Crisis, with foreign investments reaching record levels in 2022. However, as observed during the Suharto years, economic liberalization policies have often faced backlash, particularly in the export-oriented natural resource sector. These sentiments and policies in the aftermath of the Asian Financial Crisis will be closely examined in Chapter Five of this study.

The following three chapters are structured based on Anne Booth's delineated watershed moments: the declaration of independence in 1945, the Indonesian mass killings and regime change in 1965 – 1968, and the Asian Financial Crisis and the emergence of democracy in 1997 – 1998.[85] Each chapter contains an examination of political and economic leader's discourse towards foreign economic influence in a more comprehensive manner, an analysis of the primary legislative and economic reforms that framed foreign direct investment and multinational corporations, and the implications of the oil and gas sector, with the aid of practical illustrations. Through the combination of political discourse, policy analysis, and oil and gas, we will see that

[85] Booth, *Economic Change in Modern Indonesia*.

the dilemma of economic decolonization and Indonesia’s reliance and independence on foreign direct investment shifted over time in efforts to either increase economic sovereignty or catalyze economic growth.

## Chapter Three:

## Sukarno's Dilemma of Economic Decolonization and Nationalization

*Proklamasi; Strides to Break Free*

> We the people of Indonesia hereby declare the independence of Indonesia. Matters concerning the transfer of power and other matters will be executed in an orderly manner and in the shortest possible time.[86]


Image 1: The Proclamation Park (*Taman Proklamasi*) that displays President Sukarno and Vice President Hatta declaring independence – Image taken by Jan Wenger during field work in Jakarta in January 2023

The concise nature of the Declaration of Independence on August 17th, 1945, suggests that Indonesian leaders prioritized swift action over spending significant time crafting a lengthy document, indicating a sense of urgency. Australian historian Adrian Vickers wrote, "The substance was less important than the act."[87] The declaration coincided with the end of World War II, in which Japan, the colonizer of Indonesia at the time, was defeated. As a result, Indonesian

[86] The Indonesian Declaration of Independence in 1945
[87] Vickers, *A History of Modern Indonesia*, 99.

leaders took advantage of the power vacuum to assert control of their country. Indonesian historian M. C. Ricklefs stated that "for the first time in the lives of most Indonesians, the artificial restraints of foreign rule were suddenly lifted."[88] However, despite the departure of the Japanese, Indonesian leaders were apprehensive about the possibility of the former Dutch colonizers reclaiming power in Indonesia. This fear prompted a hasty declaration of independence. This unprecedented moment allowed the newly appointed Indonesian leaders, President Sukarno, and Vice President Hatta, to envision and draft their own policies, focusing on asserting sovereignty.

Although Indonesia defeated colonialism in 1949, evolving circumstances made developing policies a tricky business. Following the culmination of the Indonesian National Revolution, a prolonged armed struggle against Dutch colonialism that extended until 1949, the Indonesian leadership was tasked with steering the newly independent nation through the Cold War moment: this demanded a choice between capitalism and communism. President Sukarno's answer was: "*NEITHER*." In his autobiography, Sukarno argued that after 350 years of foreign control and oppression, Indonesia's most vital priority was independence and freedom, which was understandable from an ideological perspective but impossible from a geopolitical standpoint.[89]

In 1949, as Indonesia undertook a new struggle for economic independence, the Dutch still held significant economic power. According to economic historian Thomas Lindblad, "by the time of the transfer of political sovereignty in December 1949, large proportions of the modern sectors of the economy in Indonesia, about one-quarter of the total, were still controlled by private Dutch capital."[90] Indonesia's reliance on resource exports, which had grown by 40 percent between 1938 and 1957,[91] kept the country financially linked to the Netherlands.[92] The Dutch maintained their

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88 Ricklefs, *A History of Modern Indonesia since c.1200*, 248.
89 Sukarno, *Sukarno*, 275.
90 Lindblad and Post, *Indonesian Economic Decolonization in Regional and International Perspective*, 2.
91 Booth, *Economic Change in Modern Indonesia*, 47.
92 Lindblad and Post, *Indonesian Economic Decolonization in Regional and International Perspective*.

dominance in decolonization negotiations on the international stage, as evidenced by their retention of the right to interfere in Indonesian economic policy until the country had repaid its debt to the Netherlands.[93] By 1949, Indonesia was at the threshold of an economic revolution, still entangled in economic dependencies with both Dutch and global interests.

President Sukarno was resolute in his resolve to emancipate Indonesia from foreign subjugation and not replace Dutch colonialism with a new variant of neo-colonial reliance. He expressly invoked the "four freedoms of speech, worship, want, and fear" articulated by President Roosevelt and called for the "freedom to be free."[94] Sukarno astutely noted that while the American Declaration of Independence and the Communist Manifesto held timeless truths, Western powers would not tolerate a middle ground.[95] Guided by Sukarno's leadership, Indonesia emerged as a prominent advocate of the Global South and the Non-Aligned Movement. This international block rejected both ideologies and grew to involve more than 120 sovereign nations.

The Non-Aligned Movement rejected capitalism due to its inherent association with imperialism, as Indonesian political leadership emphasized. During World War I, Lenin published *Imperialism, the Highest Stage of Capitalism*, arguing that controlling foreign government, capital, resources, and labor is the conclusive stage of enterprises in a capitalist system. The relentless pursuit of growth and profits drives corporations to exert control over the entire value chain, from raw materials to finished products, across international borders.[96] Consequently, colonialism epitomizes the very essence of capitalism. Further, imperialism created a system founded on coerced labor to minimize costs and maximize profits. The Indonesian struggle for independence, fueled by vivid memories of subjugation, fostered a profound anti-colonial sentiment that naturally

[93] Lindblad, "From Java Bank to Bank Indonesia," 2–4.
[94] Sukarno, *Sukarno,* 275.
[95] Sukarno, *Sukarno*., 294.
[96] Lenin, *V.I. Lenin*., 667.

translated into a fear of capitalist dependency and continued exploitation perpetuated by Western nations.[97]

On the contrary, communism, the historically juxtaposed alternative, also failed to present a satisfactory system for Sukarno, particularly after Indonesia achieved its independence and gained national liberties., Sukarno viewed communism as incompatible with the country's aspirations, expressing that "in Socialist countries, what is known as freedom doesn't exist … even freedom from hunger doesn't always exist."[98] He referred to the famines that occurred in Russia in 1921 – 1922 and in China in 1959 – 1961 under communist governance. Sukarno recognized the inherent inadequacies of communism and held it responsible for the pervasive issues of poverty and hunger among the people. In other words, Sukarno found neither capitalism nor communism, neither the West nor the East, to offer a desirable model for Indonesia.

In addition, Sukarno's vision went beyond combating poverty and hunger; he aimed to inculcate a sense of national pride and identity among Indonesians. According to Sukarno, creating a unifying identity was crucial in maintaining the independence of the diverse nation. In his autobiography, he asserted that "Indonesia must overcome self-consciousness and inferiority. She needs confidence. That I must give her before I am taken away."[99] Consequently, Sukarno's Indonesia espoused a nationalist perspective, and the communist notion of creating a "one-nation world.,"[100] That is, internationalism, -was inconsistent with the newly independent nation's spirit.

Sukarno critiqued the unidirectional antagonism the Indonesian communist movements held towards Indonesian nationalist and Muslim groups. In his work, *Nationalism, Islam and Marxism*, he highlighted that Marx and Engels asserted that "the workers have no fatherland" and

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97 Booth, "I. The Colonial Legacy and Its Impact on Post-Independence Planning in India and Indonesia*."
98 Sukarno, *Sukarno,* 292.
99 Sukarno, 293.
100 SarDesai, *Southeast Asian History*.

"communism abolishes religions."[101] In view of Sukarno's aspiration for an accord of national unity, and religious tolerance, this variant of communism was deemed undesirable. Nevertheless, Sukarno posited that "the old tactical stance, which was violently anti-nationalistic and anti-religious, especially in Asia, changed radically."[102] Practically, Sukarno approved the implementation of contemporary communism in Indonesia, subject to the proviso that communist entities must avoid confrontation with nationalist or religious groups.

In accordance with his goal of achieving domestic harmony and unity, Sukarno formulated the political concept of *Nasakom*, which he defined as a tripartite coalition of "Nas" for non-communist nationalists, "A" for anti-communist religionists, and "Kom" for the Communist Party.[103] Despite communism's unsuitability as an ideological and economic framework for Indonesia during the 1950s, given its historical failures and internationalist orientation, Sukarno included the communist movement as a pillar of the delicate balance he had to manage. As a result, the third-largest communist movement was incorporated into the national system.

Indonesian leaders faced the complex challenge of balancing ideologies and shaping the country's unique political identity in the process of nation-building after gaining independence. Indonesia, like many other decolonizing nations, was founded on a mixed system with shifting beliefs. Indonesia's attempt to navigate a middle path between capitalism and communism is best reflected in its ambiguous stance towards the capitalist principles of foreign direct investment and multinational corporations. The degree to which a state controls these economic principles can be considered a key indicator of self-determination.

[101] Warouw, *Nationalism, Islam and Marxism*, 56.
[102] Warouw, 58.
[103] Sukarno, *Sukarno*, 294.

## Sukarno's Anti-Imperial Discourse

Simultaneously with developing a political identity, President Sukarno and his fellow political and economic leaders faced the challenge of formulating suitable economic policies. The discourse surrounding economic decision-making in post-independent Indonesia revolved around a fundamental dilemma: should the country prioritize justice by reclaiming control over economic production and distribution, or should it prioritize prosperity by allowing foreign entities to facilitate economic development? This dilemma centered on whether the government should acquiesce to capitalist processes, such as foreign direct investment and multinational corporations, in pursuit of increased productivity, living standards, and employment opportunities or instead pursue greater national autonomy in economic matters, potentially eliminating foreign interests, despite the risk of potential inefficiencies and fiscal constraints.[104]

Through examining the discourse on foreign financial influence and economic independence, it becomes evident that Sukarno's leadership in Indonesia opted for a hybrid economic system to balance greater national control and economic prosperity. In his influential opening address at the Bandung Conference in 1955, Sukarno expounded on the shared intellectual affinities between colonialism and capitalism, elucidating the phenomenon now commonly referred to as neo-colonialism. He stated that colonialism should not be perceived solely in its original form of direct political and economic dominance but also in contemporary manifestations where "economic, intellectual, and physical control are exercised by a small but alien community within a nation."[105] With this observation, Sukarno referred to the continued presence of capitalist elements in Indonesia's economy, such as foreign direct investment and multinational corporations, which posed a significant challenge to the nation's pursuit of economic self-reliance

[104] Feith, Castles, and Asia Society, *Indonesian Political Thinking, 1945-1965*, 378.
[105] Bandung, "Opening Address given by Sukarno (Bandung, 18 April 1955)."

and independence.[106] In effect, foreign direct investment was limited to the oil and gas sector, highlighting the complexities of Indonesia's economic policies under Sukarno's leadership.[107]

In Indonesia, the concepts of capitalism or economic liberalism were not typically associated with the diligent efforts of indigenous small and medium private enterprises (*pribumi*)[108] earning modest profits. Instead, they evoked images of colossal foreign multinational corporations that continued the foreign exploitation of the country. In his autobiography, Sukarno voiced this concern stating that "Indonesia's riches were stripped for hundreds of years by private enterprise" with little reinvestment in the land.[109] He contrasted this with the deep love that patriots had for their homeland and suggested that colonialists had not shown the same level of respect, leading to damage to the land. Foreign direct investment, which aimed at maximizing profits, was thus juxtaposed with domestic investment that aimed at strengthening the nation. Due to negative historical experiences, Sukarno deemed foreign investment and production channels as nonviable means to establish a production system in the economy.[110]

However, Sukarno recognized that he needed to balance exerting control over the national economy and resources while fostering economic stability and increasing production levels, especially given the challenges faced by the post-independence Indonesian economy. This was evident in his statement to the Indonesian Parliament (*Ichtisar Parlemen*) in 1950, where he acknowledged the significance of foreign investment:

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[106] Abraham, "From Bandung to NAM."
[107] Myint, "Inward and Outward-Looking Countries Revisited," 43.
[108] The term "Pribumi," meaning "first on the soil," refers to native Indonesians whose ancestry can be traced primarily to the archipelago. This group is differentiated from individuals of known (partial) foreign descent, such as Chinese Indonesians (Tionghoa), Arab Indonesians, Indian Indonesians, and Indo-Europeans (Eurasians).
[109] Sukarno, *Sukarno*, 291.
[110] SarDesai, *Southeast Asian History*., 291.

> In the first phase after the transfer of sovereignty to the Indonesian nation, the interests of the state and of alien business still largely run parallel. Antagonism between the state's interests and those of alien business will begin to be more apparent when Indonesian nationals are gradually able to form national capital themselves. At present our state still needs assistance from foreign capital, if we do not want a drop in the standard of living for all sectors of our society.[111]

Other political leaders adopted an even more pragmatic approach and discerned among different types of private enterprises, intending to achieve economic stabilization.[112] In 1951, Prime Minister and Islamic scholar Mohammad Natsir articulated "the expulsion of foreign manpower and personnel from Indonesia will not bring about a sound national economy but, on the contrary, will mean killing the hen that lays the golden eggs."[113] This statement highlights the recognition among Indonesian leaders that developing a national economy was a gradual process that depended on foreign production support to ensure the well-being of its citizens.

In 1955, after Natsir's tenure, Wilopo, who succeeded him as Prime Minister, debated with Indonesian economist Widjojo Nitisastro on the principles of production and ownership outlined in the Indonesian Constitution.[114] Private investments and enterprises were a key focus of the discussion. Wilopo argued that the constitutional text "rejected economic liberalism, advocating instead for collective economic activity in the form of joint endeavors."[115] Widjojo, on the other hand, emphasized the importance of "raising income per capita" and distinguishing between corporations like BPM (Royal Dutch Shell) and "the small peasant with a holding of no more than 0.1 hectare" who also engages in private enterprise. Therefore, private enterprise serving as the "legal basis of economic liberalism", it cannot be easily dismissed.[116]

[111] Sutter, "Indonesianisasi; Politics in a Changing Economy, 1940-1955. Volume IV," 1108.
[112] Lindblad and Post, *Indonesian Economic Decolonization in Regional and International Perspective*, 4.
[113] Booth, *Economic Change in Modern Indonesia*, 133.
[114] For reference: This was Article 38 of the Provisional Constitution of 1950
[115] Feith, Castles, and Asia Society, *Indonesian Political Thinking, 1945-1965*, 379–81.
[116] Feith, Castles, and Asia Society, 382–85.

Sjafruddin Prawiranegara, the President of the central bank, soundly dismissed the ideological argument of the "Dutch lion having his claws still embedded in the body of Indonesia." He observed that "these feelings of hatred date back to colonial days and the subsequent revolution and are based on a false notion of the position and function of foreign capital in the present-day Indonesian economy." For Sjafruddin, "foreign capital and labor were nothing more than a means to an end … to achieve prosperity for our people."[117] Sjafruddin argued that foreign direct investment and multinational corporations should be treated as economic instruments rather than being influenced by historical or political forces. This highlights the overlapping interests of the Indonesian political economy in the 1950s, which foreshadowed the contemporary scenario where expert opinions are often disregarded in favor of particular interest groups in shaping economic policy.

However, during the 1950s, a growing trend of economic nationalism in Indonesia, characterized by state intervention, import and investment controls, and a perception of foreign involvement as a threat to national independence, aligned with the broader nationalist rhetoric of the country's political leadership. In 1964, Sukarno famously told the United States to "go to hell with your aid", referring to a six-hundred-million-dollar aid package.[118] Sukarno despised the fact that the United States government attached a series of foreign policy conditions – stop confrontation against Malaysia and do not engage with communism – and interests to the financial support. This reinforced the neo-colonial sentiments against the financial dependencies on the so-called "free world" that Indonesia tried to shed since its independence. Moreover, Sukarno felt that

[117] Feith, Castles, and Asia Society, 385–89.
[118] "Defiance of U. S. Repeated."

the United States had “embarrassed him around the world” by promoting their aid program in the news.[119]

Sukarno contrasted these experiences with his dealings with the communist bloc, which did not engage in public displays of aid diplomacy. I argue that this contributed to his increasingly anti-Western stance and the rejection of economic liberalist policies due to the lasting impact of neo-colonial mechanisms such as foreign direct investment and multinational corporations during the 1950s and 1960s. It was this sentiment that reinforced the desire for national control through socialist principles, which some interpreted as aligning with communist ideology during the height of the Cold War.[120] One constitutional lawyer stated that Indonesia’s Constitution of 1945 is socialist in nature.[121] However, Sukarno separated the two and stated he “became a Socialist. Not a Communist.”[122]

## An Economic System in Revolution

During the 1950s and 60s, Indonesian leaders envisioned an “economy in revolution,” seeking to assert control over the national economy, promote economic decolonization, and boost production levels. This shift towards greater economic autonomy fueled nationalistic sentiments that strongly influenced economic decision-making. As a result, there was a rejection of Western economic liberalism perceived as neo-colonialist; anti-capitalist, anti-Western, and nationalist attitudes intensified. This led to a shift towards socialist processes in directing production, with a growing emphasis on socialist policies and a rejection of continued Western influence in the Indonesian economy of that era. In other words, economic nationalism deepened.

[119] Sukarno, *Sukarno*, 297–98.
[120] Sukarno, 297–300.
[121] Wenger Interviews, Jakarta 2023
[122] Sukarno, *Sukarno*, 75.

*1945 State Constitution of the Republic of Indonesia*

After the proclamation of independence, the formulation of national law, goals, and identity in Indonesia was a critical and extensively debated issue. The initial 1945 State Constitution (1945 UUD) was a working document that underwent revisions over the following decades. It was abrogated by the Federal Constitution of 1949 and the Provisional Constitution of 1950 but was eventually reinstated in 1959. Throughout its existence, the 1945 UUD faced challenges as Indonesia's leaders debated the philosophical basis of the constitution, explicitly choosing between Islam and *Pancasila* (*Pantja Sila*) as the guiding principle.[123]

Pancasila, which comprised the five principles of "belief in God, nationalism, humanitarianism, social justice, and democracy,"[124] was the vision of Indonesia's founding President, Sukarno, and was intended to be the fundamental identity of the Indonesian people. However, Islam was the dominant religion in the country, and Islamic leaders expressed dissatisfaction with its perceived limited role in the constitution.[125] The 1945 UUD was based on the five pillars of Pancasila but underwent significant revisions only after Indonesia transitioned to a modern democracy in the reform years following the fall of Suharto and the Asian Financial Crisis in 1998.

In his 1945 Birth of the Pancasila Address, Sukarno expanded on the fourth pillar of social justice within Pancasila, emphasizing the significance of social welfare through a socialist system known as *Kesejahteraan Sosial*. This ideological stance had profound implications for implementing foreign direct investment and multinational corporations in Indonesia's economy,

[123] Ricklefs, *A History of Modern Indonesia since c.1200*, 297.
[124] Ricklefs, 246.
[125] Ricklefs, 246.

as it advocates for increased state control over key economic sectors and resources while limiting the influence of foreign and private stakeholders. Article 33 of the 1945 UUD most notably reflects the philosophy of state control over the economy, outlining the principles of Indonesia's state controlling natural resources and economic production.

*Article 33: State Control of Natural Resources*

In the Indonesian economy, the political and economic leaders of the Indonesian Revolution manifested their aspirations of economic control through Article 33 of the 1945 UUD. The period of Japanese occupation from 1942 through 1945, followed by the struggle against the Dutch until 1949, severely disrupted Indonesia's production and commodity export infrastructure. As highlighted by Lindblad, the "country's export production volumes in 1947 were only a fraction of those in 1941, with only 12 percent in oil, 5 percent in estate rubber, and 1 percent in palm oil."[126] The recovery of national control over production and resources became a top priority for Sukarno, with Article 33 of the 1945 UUD serving as a supreme expression of this goal. This article stipulates that the fundamental economic sectors of Indonesia are subject to state control. Notably, Article 33(3) specifically addresses natural resources, stating that "the land, the waters, and the natural resources (of Indonesia) shall be under the control of the state and shall be used to the greatest benefit of the people" (translation).[127] The primary motivation behind drafting Article 33 was to grant economic control to the state to safeguard Indonesia from two perceived threats: foreign private enterprises and domestic private business owners. In the political discourse of Indonesia, liberalism is closely associated with "unrestrained capitalism."[128] Therefore, under the

[126] Lindblad, Leiden, and Lindblad, "Macroeconomic Consequences of Decolonization in Indonesia," 4.
[127] Boyd et al., "A Note on Policies for the Oil and Gas Sector," 240.
[128] Feith, Castles, and Asia Society, *Indonesian Political Thinking, 1945-1965*, 227.

banner of Democratic Socialism, Sukarno assumed authority over the nation's critical economic industries and resources.

The state's objective to exercise control over the economy and its natural resource production and distribution in Indonesia had two main dimensions. Firstly, it aimed to break free from global economic dependence through multinational corporations and foreign direct investment that exploited Indonesia's resources for profit. This objective stemmed from the country's history of colonial economic exploitation and political oppression and the economic destruction during the struggle for independence. Secondly, during the political discussions at the time, the interpretation of Article 33 of the 1945 UUD reflected the significant dilemma of gaining greater national control or increasing economic productivity. According to Giri Taufik, a PhD candidate at Griffith Law School, two major factions debated Article 33.[129] Supporters of the nation's first Minister of Justice, Soepomo, believed that the language of Article 33 granted complete state control of the key economic sectors in Indonesia. However, Soepomo's supporters recognized the need for private ventures' participation in these sectors as long as it was in the state's best interests, meaning the people's best interests. Soepomo referred to his interpretation as "state socialism." On the other hand, Vice President Hatta's interpretation of the original language of Article 33 allowed for more flexibility in the operation of free enterprises. He suggested using efficiency as a criteria to define the roles of the state and private initiative in the economy.[130]

In the 1950s, particularly as economic nationalism gained political momentum, the Indonesian state pursued a strategy of assuming complete control over all aspects of production and distribution within the country. The political leadership was mindful of the anti-Dutch and

[129] Taufik, "The Interpretation of Article 33 of the Indonesian Constitution and Its Impact on Independent Regulatory Agencies," 318–19.
[130] Taufik, 318–19.

anti-Chinese sentiments prevailing at that time, as these groups were perceived to have dominated private operations and owned a significant portion of land and wealth. President Sukarno advocated for a shift towards state ownership in order to benefit all the people and emphasized the need to retool instruments of state power, production, and distribution to align with the principles of Article 33 of the 1945 UUD. This shift was accompanied by the use of increasingly authoritarian mechanisms as a driving force to achieve these objectives.[131]

The discourse surrounding the interpretation of Article 33, particularly its third paragraph, which pertains to natural resources, reflects a broader national debate in post-independent Indonesia. This debate revolves around the competing priorities of macroeconomic efficiency, which involves incorporating foreign direct investment and multinational corporations to extract and export natural resources for profit, and social justice, which entails promoting greater national control over these resources with the aim of equitable distribution of profits among Indonesians.[132] This dilemma pits economic efficiency against economic control and equity: it has been a critical factor in shaping Indonesia's policy decisions since its independence and continues to influence contemporary policy-making processes.

### *Nationalization Reforms*

A series of decolonization reforms have driven the pursuit of economic independence in Indonesia. Burmese economist Hla Myint characterized the country's economic strategy in the 1950s as inward-looking. Myint used five categories of inward- and outward-looking policies to measure Indonesia's economic stance (see Figure 4).[133]

[131] Feith, Castles, and Asia Society, *Indonesian Political Thinking, 1945-1965*, 106–7.; Booth, *Economic Change in Modern Indonesia*, 136.
[132] Feith, Castles, and Asia Society, *Indonesian Political Thinking, 1945-1965*, 378.
[133] Myint, "Inward and Outward-Looking Countries Revisited."

| | Pure Outward-looking Case | | Pure Inward-looking Case |
|---|---|---|---|
| O1 | Free trade and export expansion policies | I1 | Protectionist and import substitution policies |
| O2 | ‘Open’ type domestic economic policies | I2 | ‘Insulating’ type domestic economic policies |
| O3 | ‘Open door’ polices towards foreign aid and official capital flows | I3 | Reliance on domestic savings and resource self-sufficiency |
| O4 | ‘Open door’ policies towards direct private foreign investment | I4 | Restriction of direct private foreign investment |
| O5 | ‘Open door’ policy on immigration | I5 | Restriction on immigration |

Figure 4: Myint’s Inward and Outward-looking Metric

He noted that under Sukarno’s leadership, Indonesia displayed tendencies of protectionist and import substitution policies (I1), insulating type domestic policies (I2), reliance on domestic economic policies (I3), mixed policies towards direct foreign private investment (I4/O4), and restrictions on immigration (I5). Myint distinguished Indonesia from Latin American countries with struggling economies in their approach to foreign direct investment utilization. While Latin American countries allowed foreign investment in the manufacturing sectors while discouraging it in the primary resource sectors as part of their import substitution policies, Myint observed that in Indonesia, private foreign investment was severely discouraged, except in the oil sector where foreign investment was permitted to operate on a profit-sharing basis. Consequently, the balancing act between inward and outward orientation is most evident in Indonesia’s policies toward foreign direct investment. Myint argued that Sukarno pursued a “mixed strategy” with a “greater degree of inward orientation.”[134]

The concept of *indonesianisasi* implemented positive discrimination policies for Indonesians in economic life. The PhD dissertation of Political Scientist John Sutter described *indonesianisasi* as follows:

[134] Myint, 42–43.

> Indonesianization may imply not only transition (either permanent or provisional) in those sectors of the economy once controlled by foreigners (part-time residents) or other aliens (i.e., lifetime residents of Indonesia ) and their gradual replacement by Indonesians, but, in some instances parallel to the points last cited above, even the replacement of non-indigenous Indonesians by Indonesian citizens of more "indigenous" (autochthonous) ancestry.[135]

The hierarchy of indigenous ancestry in Indonesia, distinguishing between *pribumi* and *non-pribumi*, classified native Indonesians as the highest, followed by Chinese Indonesians, Eurasian Indonesians, and finally, the Dutch. Sutter divided *indonesianisasi* into nine pillars of economic reforms, which among others, focused on the increasing participation and promotion of Indonesian's business people and the transfer of private enterprises and their land owning to the Indonesian government.[136]

The first policies of Indonesia's economic decolonization focused on gaining national control over the financial system and trade, as hundreds of Dutch firms continued to operate in the country. One of the initial policies was the nationalization of the Java Bank, the central bank of the former Dutch colony, in 1952.[137] According to Nicholas J. White, the transition was successful because the international community recognized that the control of money and credit was essential to sovereignty.[138] Additionally, in the early 1950s, President Sukarno launched the Benteng Program, which aimed to reduce the economic influence of the Dutch and Chinese and build up an indigenous class of Indonesian entrepreneurship (*pribumisasi*) through a bundle of affirmative action policies. According to Lindblad, the program focused on import trade, targeting the dominance of the "Big Five" Dutch firms who controlled trade in the 1950s.[139] However, despite

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[135] Sutter, "Indonesianisasi; Politics in a Changing Economy, 1940-1955. Volume I," 2.
[136] Sutter, 2.; Lindblad, "The Importance of Indonesianisasi during the Transition from the 1930s to the 1960s," 52.
[137] Lindblad, "From Java Bank to Bank Indonesia."
[138] White, "Surviving Sukarno," 1283.
[139] Lindblad and Post, *Indonesian Economic Decolonization in Regional and International Perspective*, 4.

its ambitions, the Benteng Program was largely considered a failure as it only reached a small proportion of the formal economy.[140]

Concerning foreign direct investment and multinational corporations, the discourse in Indonesia centered on the ownership and control of production and resource extraction and the practical implementation of policies based on Article 33 of the 1945 Constitution. Sutter's analysis of *indonesianisasi* focused on the debates and speeches in the 1950 Cabinet of the Republic of Indonesia (*Kabinet Republik Indonesia*). The government's discussions, which primarily aimed at promoting socialism and defending against capitalism, were highly significant to the ongoing influx of foreign direct investment and the operations of multinational corporations.

The discussions within the Central Indonesian National Working Committee (KNIP) on implementing economic policies based on Article 33 of the 1945 UUD yet again highlighted the dilemma of Indonesia's economic dependence. On one side of the spectrum, political and economic leaders advocated for the complete nationalization of key economic sectors, given the rise of economic nationalism, anti-capitalism, and anti-foreign sentiments reinforced by the 1949 Round Table Agreement that favored Dutch interests. On the other side, Indonesian political and economic leaders promoted a pragmatic approach that allowed foreign and private operations under Article 33 for greater economic efficiency.[141]

According to Sutter's analysis of the discussions within the KNIP, there were divergent views on interpreting Article 33 of the 1945 UUD. Asrarudin and SUDIJOHO Djojoprajitno of the *Partai Buruh* (Labor Party) advocated for the complete nationalization of foreign enterprises to fulfill Article 33. Conversely, DJAETOEN Dirdjowijoto of the PKI (Communist Party) argued that opening up factories, estates, and mines under government ownership would suffice. In

[140] Booth, *Economic Change in Modern Indonesia*, 134–40.
[141] Central Indonesian National Committee

response, Prime Minister Halim expressed a pragmatic approach, indicating that the government would nationalize where necessary and feasible, but disagreed with the dogmatic emphasis on nationalization by the aforementioned speakers. Instead, he proposed building up a private domestic industry to exploit Indonesia's natural resources, which he believed would raise national income and state capital. SIDIK Djojosoekarto of the PNI (National People's Party) cautioned against the interference of foreigners in the country's economic affairs, which could lead to, in his eyes, dangerous national capitalism. Halim countered by suggesting that private enterprises should have as much freedom as possible to develop in non-essential industries, as specified in Section 2 of Article 33.[142]

The electoral outcome of the 1955 elections revealed a significant increase in the influence of both the nationalist (PNI) and communist (PKI) parties in Indonesia. While the PNI maintained its position as the most popular party, the PKI gained roughly one-quarter of the votes in Java, thus underscoring the growing power of Sukarno's PNI-PKI alliance and the prevalence of nationalist and socialist ideologies. Concurrently, Indonesia experienced modest advancements in domestic industrialization. Nonetheless, anti-capitalist and anti-foreign attitudes, primarily towards Dutch and Chinese interests, intensified.[143]

Starting in 1957, Indonesia shifted its economic strategy towards an inward-looking approach, resulting in the nationalization of foreign corporations, especially those under Dutch ownership. Economic nationalism, anti-capitalist, anti-Dutch, and anti-imperial sentiments drove that radical change. Additionally, foreign policy disputes intensified anti-Dutch sentiments in Indonesia, as the Dutch refused to yield control of Papua New Guinea to Indonesia, and Indonesia

[142] Sutter, "Indonesianisasi; Politics in a Changing Economy, 1940-1955. Volume IV," 1112–18.
[143] Ricklefs, *A History of Modern Indonesia since c.1200*, 289–319.; Booth, *Economic Change in Modern Indonesia*, 136.

was reluctant to repay the debt obligations negotiated under the 1949 Round Table Conference.[144] Consequently, the growing nationalist and socialist views in Indonesia, along with modest progress in domestic industrialization, prompted the country to undertake the nationalization of almost all privately owned Dutch enterprises between 1957 and 1959.[145]

The Indonesian government implemented the Act for the Nationalization of Dutch Enterprises (Act No. 86 of 1958) to provide legal support for the nationalization policy. Booth's research indicated that more than 700 Dutch-owned enterprises were expropriated,[146] with most becoming state-owned enterprises, while indigenous Indonesian or Chinese Indonesian owners acquired some. At the same time, British and American companies were nationalized as part of Indonesia's confrontation strategy against Malaysia. Indonesian technocrats justified the nationalization policy by arguing that an Indonesian economy could only be truly considered "national" if it was based on the "country's spiritual and material identity." [147] In their view, foreign direct investment and multinational corporations were seen as neo-colonial tools and incompatible with these concepts.

Following the nationalization of Dutch enterprises, a new foreign investment law was introduced in parliament in 1958 to guide joint operations moving forward. However, this development occurred amidst a changing political and economic landscape, where Indonesia achieved the ultimate *indonesianisasi*, and state control over the economy increased. At the same time, privileges for foreign investors were eliminated. Moreover, Sukarno consolidated his power in a more authoritarian manner, and his speeches during 1958 – 1959 emphasized the persistent affliction of the Indonesian economy by colonial capitalism that had drained the country.[148] Given

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[144] Lindblad and Post, *Indonesian Economic Decolonization in Regional and International Perspective*, 9.
[145] Lindblad, "The Importance of Indonesianisasi during the Transition from the 1930s to the 1960s," 59–61.
[146] Booth, *Economic Change in Modern Indonesia*, 137.
[147] Lindblad and Post, *Indonesian Economic Decolonization in Regional and International Perspective*, 5.
[148] Weinstein, *Indonesian Foreign Policy and the Dilemma of Dependence*, 212–13.; White, "Surviving Sukarno," 1291.

this context, it is unsurprising that the proposed Foreign Investment Law (Law 78/1958), which exhibited liberal tendencies, faced significant opposition and was crushed. In particular, representatives of the PKI viewed the foreign investment law as a threat to the recently acquired power of the proletariat and the state through nationalization.[149]

In a report presented by Indonesian communist politician D. N. Aidit at the Sixth National Congress in 1959, it is evident that the communist party was dissatisfied with the aftermath of the nationalization period. Aidit articulated that after the nationalization process, the self-centered "middle-of-the-roaders" made efforts to acquire ownership of these enterprises for themselves, and elites endeavored to occupy positions previously held by Dutch officials.[150] Consequently, even after the expulsion of foreign capitalist institutions, i.e., privately owned Dutch enterprises, apprehension regarding domestic capitalism persisted. The indigenous Indonesians and ethnic Chinese who replaced Dutch officials rationalized their actions by stating that "the government and workers were incompetent and private businessmen were more competent."[151] Additionally, Aidit contended that the takeover of "imperialist businesses had immense political significance, but only a small number of bureaucratic capitalists benefited from it."[152] Therefore, the nationalization of foreign enterprises, mostly of Dutch origin, did not entirely fulfill the expectations of political leaders. Moreover, as foreign companies left Indonesia, their capital and technical know-how went with them, and production output decreased. This led Indonesia to experience a phase of economic stagnation, which contributed to political instability and ultimate regime change.

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[149] Feith, Castles, and Asia Society, *Indonesian Political Thinking, 1945-1965*, 263.; Lindblad, "Foreign Direct Investment in Indonesia," 219.
[150] Feith, Castles, and Asia Society, *Indonesian Political Thinking, 1945-1965*, 261.
[151] Feith, Castles, and Asia Society, 262.
[152] Feith, Castles, and Asia Society, 275.

**Indonesianisasi: The Case of Oil and Gas**

The oil and gas industry keenly illustrates Indonesia's dilemma of economic decolonization and development and has been a major focus of the country's policies towards foreign direct investments and private enterprises. Several significant developments marked the Indonesian oil industry in the 1940s and 1950s. In 1947, oil, rubber, and sugar were significant reasons for the return of the Dutch to Indonesia, whose economy was drained after World War II and in desperate need of resources. Despite losing the revolution for political power in Indonesia, the Dutch regained control of most of the export-oriented economy. Indonesia's exports experienced a slow recovery, but by 1957, oil production had reached twice the level it had been in 1940. While not all of this production was exported, it contributed to Indonesia's growing economy. During this period, non-Indonesian interests remained essential players in the oil industry, with the Anglo-Dutch company Shell/BPM and the American companies Stanvac and Caltex controlling most of the production and Dutch organizations managing inter-island shipping and exporting.[153]

Despite the political independence of Indonesia, foreign direct investment and multinational corporations retained control and partial ownership of the country's oil and gas sector, contradicting Article 33(3) of the 1945 UUD, which asserts state control. Historian Nicholas White noted that "Shell/BPM, Stanvac, and Caltex extracted and refined oil from Indonesian fields in South Sumatra and East Kalimantan under the "Let Alone" agreements dating from 1948, which exempted the oil producers from foreign exchange controls and profit transfer restrictions."[154] In the 1950s, the Sukarno government increasingly restricted foreign investment in manufacturing and natural resources, except for oil and gas, which was largely left to operate

[153] Ricklefs, *A History of Modern Indonesia since c.1200*, 262–75.
[154] White, "Surviving Sukarno," 1283.

privately.[155] The oil and gas sector highlights an example of the Indonesian state's prioritization of economic development and state revenue over national control, demonstrating a degree of reliance on foreign operations and exports.

Nevertheless, starting in 1957, the prevailing anti-Dutch sentiments led to the nationalization of 700 Dutch enterprises, including the Dutch-owned oil and gas fields. The petroleum sector, previously operated and owned by Shell/BPM (*Bataafse Petroleum Maatschappij*), NIAM (*Nederlandsch-Indische Aardolie-Maatchappij*), and other Dutch corporations, fell under the control of the Indonesian state.[156] Initially, communist insurgents took control of these assets, but by December 1957, the Indonesian government established Pěrmina, a state-owned oil enterprise, and effectively nationalized the fields. The Indonesian army played a leading role in Pěrmina, and thus nationalization strengthened the army's involvement in the oil industry.[157] Thus, despite initially prioritizing economic development, the Indonesian state ultimately completed the process of *indonesianisasi* in the oil and gas sector. By 1963, the Anglo-Dutch company Shell sold all its shares to the Indonesian state and exited Indonesia entirely by 1965.[158]

However, the nationalization of Indonesia's oil and gas sector primarily targeted Dutch companies, while American oil companies were allowed to continue their operations. The historical context of Dutch colonialism influenced the government's more favorable stance towards American oil companies, resulting in shared-production agreements. One significant entity in this regard was the army-controlled Pěrmina, which operated under the regulations of Law No. 44 of 1960, serving as the first oil and gas law governing exploration. Pěrmina entered

[155] Myint, "Inward and Outward-Looking Countries Revisited," 42–43.
[156] Lindblad and Post, *Indonesian Economic Decolonization in Regional and International Perspective*, 53.
[157] Vickers, *A History of Modern Indonesia*, 185.
[158] Booth, *Economic Change in Modern Indonesia*, 137.

into fixed profit-sharing agreements with Caltex and Stanvac, which proved to be crucial frameworks in the subsequent decades.[159] Booth stated that "non-Dutch firms in the petroleum sector continued to operate, although some British and American firms were taken over during the 'Crush Malaysia' campaign launched in the early 1960s."[160] Thus, despite the country's socialist leanings, the nationalization period from 1957 to 1959 did not completely undermine the oil and gas sector. Instead, under the economically pragmatic leadership of the military, the sector survived, allowing for the continuation of highly profitable foreign and private exploitation. The next chapter will delve into the increasing influence of the American-backed Indonesian military on the political and economic spheres and how this shift in power dynamics led the country to embrace foreign direct investment. Additionally, it will explore how multinational corporations operating in the oil and gas industry acted as catalysts for economic growth.

[159] Ricklefs, *A History of Modern Indonesia since c.1200*, 275–300.
[160] Booth, *Economic Change in Modern Indonesia*, 137.

## Chapter Four:

## Suharto's Developmental Authoritarianism

*Mass Killings and a New Order*

In 1965, the 30 September Movement carried out an unsuccessful coup d'état in Indonesia, assassinating six army generals. This event triggered a turbulent era of social, political, and economic instability in the country. General Suharto, attributing the coup to the Communist Party (PKI), initiated a period of violent persecution against all communist affiliates. This political genocide claimed the lives of approximately 500'000 to 1'000'000 alleged communist supporters, ultimately leading to a military coup and the removal of Indonesia's first President, Sukarno. Suharto assumed the presidency and established his New Order Government in 1967 and 1968.[161]

Like Indonesia's decolonization process, the political revolution was followed by an economic reorientation. The political genocide and military coup in Indonesia between 1965 – 1968 played a pivotal role in the country's integration into the global capitalist system. On the eve of 1965, Indonesia's economy was weak, characterized by hyperinflation and a 900 percent increase in the price of rice in 1965.[162] Richard Robison noted that the growing popularity of the PKI during the 1950s and 1960s prompted a shift towards capitalism as a deliberate strategy to secure a victory for the propertied classes over the landless and urban workers. Moreover, the army elites in Indonesia held sway over profitable private enterprises, including oil and gas, and perceived socialism as a threat. Thus, the combination of the macroeconomic crisis and the army's vested interests in preserving their privileges contributed to the political genocide of the PKI and the overthrow of Sukarno's regime and led to the favoring of global capitalism.[163]

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[161] Robinson, *The Killing Season*.
[162] Ricklefs, *A History of Modern Indonesia since c.1200*, 316.
[163] Farid, "Indonesia's Original Sin," 5.; Robison, *Indonesia*.

Rather than socio-cultural, economic, or religious motivations, the mass killings were primarily caused by the character of the army leadership, international influence, and the existing historical context. Western powers, foremost the United States, played a pivotal role in overthrowing the Communist Party as part of their Cold War containment strategy. The United States and its allies fought communism throughout Southeast Asia since the 1950s and actively sought to weaken Sukarno's PNI-PKI alliance in the build-up to the 1965 coup. According to Geoffrey Robinson, recent evidence indicated that Western powers encouraged the military to take forceful measures against leftist groups, facilitated extensive violence, including mass killings, and aided in the military's consolidation of political power. These actions resulted in the decimation of the PKI and its affiliated organizations, the removal of Sukarno and his associates from authority, and a tremendous shift in Indonesia's foreign policy towards alignment with the West and its capitalist ideology.[164]

The economic and political transformations that occurred in the aftermath of the 1965 coup in Indonesia deepened the country's integration into the global capitalist system, effectively opening up the economy to foreign direct investment and multinational corporations. Under the leadership of General Suharto, the New Order government implemented policies aimed at attracting foreign investment and facilitating the operations of multinational corporations in Indonesia. I argue that this shift towards a more global capitalist economic framework had far-reaching implications for the country's political landscape and policy-making, as the government prioritized economic growth and sought to secure international economic support. This new economic openness will be examined in this chapter, notably by looking at the new foreign investment law and the heavy presence of multinational corporations in oil and gas.

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[164] Robinson, *The Killing Season*, 82–117.

**Suharto's Alignment**

In the aftermath of Indonesia's bloody regime change, the new Suharto government found itself indebted to Western powers and the IMF, with the former in support of overthrowing the PKI and Sukarno and the latter bailing out Indonesia from an economic crisis. To meet the debt qualifications, President Suharto introduced economic reforms aimed at realigning with the Western political system and rebuilding relationships that suffered during Sukarno's anti-imperialist, non-aligned, and pro-independence rhetoric. A group of technocrats known as the "Berkeley Mafia"[165] – a group of American-educated Indonesian economists in technocratic positions under Suharto – developed these reforms. The Suharto government sought to attract foreign direct investment and multinational corporations. Indonesia's leadership restored its relationship with Western powers through a shift economic policy and political discourse. According to a *New York Times* article from May 29, 1970, President Suharto said in a speech to the Asia Society that while "Indonesia must assume the burden of economic development, the Indonesian government favored private foreign investment "without the slightest doubt or ambivalence.""[166] In light of this newly aligned attitude, favorable policies, and dearth competition with other Southeast Asian nations in the late 1960s, Indonesia attracted foreign investment at a rapid pace.[167]

Having fought hard for their independence, many Indonesians were wary of opening the economy too much. Internal resistance resurfaced as politicians, civil servants, and student groups voiced opposition to opening up the country to foreigners, relinquishing control of the nation's economy, and disposing of its resources on unfavorable terms of trade. Indonesian leaders across

[165] The Indonesian members of the Berkley Mafia distinguished themselves from the Chicago Boys in Latin America by being mindful of the opposition to economic liberalization and globalization. They adopted a "half opening the door" approach, which involved a cautious introduction of global integration instead of embracing full-fledged neoliberalism.
[166] "Suharto Invites Foreign Capital."
[167] Booth, *Economic Change in Modern Indonesia*, 141.

various segments of life expressed concern about the impact and control of foreign investment and multinational corporations. They worried that the country had returned to a colonial model of dependency in which capitalist forces exploited its resources without improving the domestic economy.[168] Clearly, Sukarno's arguments were not forgotten. Between 1970 and 1973, foreign affairs expert and author Franklin B. Weinstein conducted a series of interviews with Indonesian leaders across various segments of life and found that the government's outward-looking strategy towards foreign investment was one of the major concerns in public discourse. The interviews demonstrated that many remembered the 1950s debates on economic decolonization and the struggle for economic self-sufficiency. Overall, officials, politicians, and student groups were concerned that increasing foreign economic presence would allow foreign capitalists to exploit the country's resources on deteriorating terms and reinforce capitalist inequalities in the domestic economy. In other words, economic nationalism was on the rise.[169]

According to Weinstein's interviews, anti-foreign and anti-capitalist attitudes in Indonesia resurged as the country's economy rebounded from the aftershocks of political violence. Army generals and leaders from the PNI and Muslim parties expressed concerns about a new foreign investment law, which they felt was too liberal and created by individuals lacking practical experience. Additionally, foreign ministry officials and technocrats were worried about the reluctance of foreign investors to build processing facilities, perpetuating colonial patterns that encouraged resource extraction rather than manufacturing. Foreign ministry officials and technocrats claimed too much was invested in capital-intensive extractive industries for export as compared to investing in domestic production and industries. It was crucial for Indonesian leaders that small-scale investments support the development of a national economy and provide jobs for

[168] Booth, 142.
[169] Lindblad, "Foreign Direct Investment in Indonesia."

Indonesians. In addition, joint ventures between foreign investors and indigenous Indonesian business partners were criticized. Islamic leaders argued that such ventures were not truly joint because Indonesians had no capital, production infrastructure, or expertise. They called for joint enterprises that shared control and utilized Indonesian resources. There was a general fear among Indonesians that the country would be sold to foreigners at a disadvantage. In 1973, one of Suharto's closest advisors acknowledged that, in the eagerness to attract foreign direct investment, the government had concluded many investment agreements that were not beneficial to Indonesia.[170]

The described tensions and anxieties of renewed foreign dominance and dependence culminated in the Malari incident in 1974. This incident involved a student demonstration and riot; it was the first significant protest that expressed discontent with Suharto's economic policies and tolerance of corruption, high prices, and inequality in foreign investments. The demonstrations, which rapidly turned into rioting, were triggered by the arrival of Japanese Prime Minister Tanaka on January 15, 1974, and primarily targeted Japanese investors and their toleration of fraud and corruption by Indonesian New Order officials. However, the Malari incident in 1974 was not solely directed at the Japanese; it also reflected the increasing economic nationalism and dissatisfaction with foreign, including Western, influence in the Indonesian production chains. Despite the Suharto government's crackdown on the protests and the banning of twelve media outlets displaying the authoritarian character of the regime, the incident prompted economic reforms to improve participation by the *pribumi* and tighten the foreign investment climate by imposing stringent tax codes and ownership regulations for joint ventures.[171]

[170] Weinstein, *Indonesian Foreign Policy and the Dilemma of Dependence*, 279–82.; Weinstein, 279–84.
[171] Sahrasad and Ridwan, "The Malari 1974, Press and the Soeharto's New Order."

In parallel to increasing economic nationalism and investor tightening economic reforms, Indonesia's oil windfalls in the 1970s reduced the country's reliance on foreign capital for economic development.[172] However, President Suharto reassured the international community that Indonesia remained welcoming to foreign investors, as evidenced by his statement in the South China Morning Post on August 17, 1976, when he emphasized that their efforts to obtain a fair share of natural resources did not alter the government's attitude towards foreign capital investment and its participation in Indonesia's development.[173] Nevertheless, the macro-economic well-being of Indonesia increased the country's confidence and led to certain protection of the domestic economy.

While the technocrats were receiving international praise for their economic reforms of the 1980s, the rise of domestic elites had social, economic, and political consequences. The rise of conglomerates, corruption, and abuse of power accompanied the rhetoric in favor of promoting businesses owned by weaker economic groups. According to a foreign commercial lawyer, Indonesia's expensive and exclusive economy was constructed around the oil revenues, which had few positive effects on the surrounding economic clusters.[174] Suharto's lack of support for *pribumi* business further exacerbated the situation, as it ignored the grievances of Indonesian businesspeople who felt excluded from the rich pickings scooped up by the privileged few. Consequently, observers' anti-foreign capitalist attitudes soon transferred to anti-domestic capitalist attitudes. Booth noted that by the early 1990s, the "economic nationalism of the 1950s Benteng Program had been replaced by an economy of entrenched monopolies and privileges with lucrative shares absorbed by a well-connected elite of Chinese capitalists and a tiny *pribumi* elite

[172] Lindblad, "Foreign Direct Investment in Indonesia," 220.
[173] "Suharto."
[174] Wenger Interviews, Jakarta 2023

sustained by ties to Suharto and the state."[175] Despite Suharto's official rhetoric and a few economic reforms to promote business owned by the weaker economic groups, the reality was that Indonesian business between the 1970s and 1990s came to be dominated by foreign multinational corporations and domestic conglomerates owned by the elites. Booth noted that "in 1996, the total sales of the top twenty-five conglomerates amounted to Rp. 171,853 billion, which was almost twice the size of total government domestic revenues in the financial year 1996/1997."[176] As a result, the negative sentiments towards both foreign control along colonial patterns and domestic domination by a handful of elites fueled economic nationalism and anti-Suharto sentiments.

Economic nationalism in Indonesia did not end with the fall of Sukarno but evolved over time. The government's eagerness to attract foreign investment has also led to the perception that the country has been sold to foreigners at a disadvantage. In light of Suharto's alignment, many Indonesians remembered their struggle for independence, advocated for decreased foreign control and increased domestic participation in value creation. Moreover, the rise of domestic elites and their ties to Suharto's authoritarian regime contributed to a sense of exclusion among the majority of Indonesian businesspeople. This led to renewed anti-foreign, anti-capitalist, and anti-Suharto sentiments. However, policymaking under the authoritarian regime increasingly aligned with global capitalist integration and rapid economic development.

## Suharto's Developmentalism

After the regime change from President Sukarno to President Suharto, a series of economic reforms stabilized the Indonesian economy. Suharto alleviated food prices and calmed the financial

[175] Booth, *Economic Change in Modern Indonesia*, 145.
[176] Booth, 145.

system through increased state intervention and liberalized export and foreign investment channels to catalyze growth. With regard to global capitalist integration, Hla Myint described this shift from inward-looking economic policies towards outward-looking ones. Indonesia's policies can be described as a mixed strategy, consisting of protectionist and import substitution policies (I1), insulating type domestic policies (I2), open door policies towards foreign aid (O3), open policies towards direct foreign private investment (O4), and restrictions on immigration (I5) (see Figure 4). Thus, Suharto's Developmentalism maintained some inward-looking strategies while opening its policies toward international aid and investments as part of its effort to promote economic development.[177] The balancing act between national control and economic growth continued under Suharto's aligned set of rules.

Yet, the new regime remained loyal to the foundations of the 1945 Constitution, as Suharto demonstrated an unwavering adherence to its tenets. Drafted during the presidency of Sukarno, the 1945 Constitution partly incorporated socialist principles as part of its attempts to minimize Indonesian economic dependency. Most notably, Article 33 granted the government the authority to exert control and influence over Indonesia's key economic sectors, resources, and production, as demonstrated in the preceding chapter. Despite implementing significant economic policy reforms after the change in regime in 1967, the Suharto government remained fundamentally protective of the constitutional principles governing the economy. This exemplifies Suharto's commitment to Indonesian sovereignty and economic self-reliance, with a balanced approach to economic nationalism and growth, and reflects the intricate political and economic ambiguity of post-independence Indonesia.[178]

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177 Myint, "Inward and Outward-Looking Countries Revisited," 44–51.
178 Taufik, "The Interpretation of Article 33 of the Indonesian Constitution and Its Impact on Independent Regulatory Agencies."

*Foreign Investment Liberalization*

In contrast to the socialist tenets of the constitution, President Suharto's Law 1/1967 on Foreign Investment and its stern implementation signaled a significant change in Indonesia's attitude to global capital integration. This new law allowed foreign investors to invest in any non-restricted sector of the economy through a limited-liability company established under Indonesian law, with approval from the government.[179] Thus, while adhering to the fundamental constitution, Suharto also sought to solve Indonesia's economic problems and saw the openness of this new foreign investment law as a tool to promote economic growth and development. This liberalization policy was part of the New Order's deal with the IMF and the World Bank to receive financial support. After the economic downturn in the 1960s under Sukarno and the following regime change, Indonesia was bankrupt. In exchange for the IMF acting as a lender of last resort and supporting Indonesia, Suharto implemented this strikingly liberal foreign investment law. In addition, Suharto was now chair of ASEAN and had a special incentive to appear as a regional leader, pursuing global integration.[180]

To attract both domestic and mainly foreign investment while retaining control, the Indonesian government utilized two primary bodies: State-Owned Enterprises and the Investment Coordinating Board (BKMP).[181] IMF economists raised concerns about the government's interventionist policies and their potential adverse effects on foreign investment, especially in the manufacturing sector. This was due to factors such as import-substitution industrialization policies, unfavorable trade terms, and the bureaucratic landscape in Indonesia that remained even in light of liberalization.[182]

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[179] Hornick and Nelson, "Foreign Investment in Indonesia," 727–28.
[180] Lindblad, "Foreign Direct Investment in Indonesia," 219.
[181] Djaldan, "The Politics of Foreign Investment Liberalization in Indonesia with Particular Reference to the Early 1990's."
[182] Booth, *Economic Change in Modern Indonesia*, 143.

Despite the government's stringent oversight of foreign investment dealings, the growing participation of multinational corporations and international organizations such as the IMF has generated apprehensions regarding foreign economic dominance. During the 1970s, the allure of Indonesia's abundant natural resources and permissive legislation attracted investors globally, resulting in a perceived excessive presence exemplified by the Malari incident in 1974. In response to political pressures, various amendments were made to foreign investment regulations, including tax reforms, the exclusion of specific sectors for foreign entities, and the imposition of a requirement for joint ventures with Indonesian partners. These joint venture agreements frequently entailed provisions mandating the transfer of 51 percent of production share to the Indonesian partner over a 20-year duration.[183]

Suharto's developmentalism was marked by rigorous adherence to the 1945 Constitution and a pragmatic liberalization of capital flows. This approach, often referred to as the "half-open door" policy, facilitated collaboration between the Indonesian government and multinational corporations in pursuit of economic profits and overall growth. The oil and gas sector serves as a notable illustration of how ambivalent policies derived from the Constitution and foreign investment regulations were implemented practically. The ensuing two subsections will examine the economic advantages accruing to the central state and juxtapose them with the social and economic challenges experienced at the provincial level, focusing on Aceh.

[183] Djaldan, "The Politics of Foreign Investment Liberalization in Indonesia with Particular Reference to the Early 1990's," 76.

## The “Golden Years”

*Production Sharing Contracts*

Following the nationalization of Dutch assets and the establishment of Pěrmina in 1958, the military took control of significant portions of Indonesia’s oil and gas sector. By 1965, the country’s economy remained highly dependent on oil exports, with non-oil exports making up only four percent of GDP.[184] As such, discussions during the regime change in 1966 – 1967 focused on the regularization of Pěrmina and the industry. However, Suharto ultimately supported the military’s control of the company and placed Ibnu Sutowo in charge under the President’s direct oversight. Suharto and Sutowo consolidated power in the oil and gas sector by approving the creation of a single national company, PERTAMINA, resulting from the merger of Pěrmina and Pěrtamin in 1971.[185] This move granted Sutowo and Suharto’s controlled company a state monopoly on oil production and the ability to negotiate with foreign or domestic parties.[186] PERTAMINA entered into several profit-sharing agreements with companies such as Mobil Oil, Caltex, and Chevron, which marked the beginning of the oil windfalls. Professor Richard Robison described these developments as follows:

> PERTAMINA constituted the channel through which the bulk of the state’s revenue flowed, as well as the largest and most concentrated source of contracts for construction and supply. PERTAMINA therefore was the strategic focus of economic power and the crucial source of revenue. The autonomy and hegemony of the military was closely dependent upon its ability to maintain its control over this terminal and to prevent its absorption by any regularized state apparatus.[187]

[184] Sheng, *From Asian to Global Financial Crisis*, 219.
[185] Ricklefs, *A History of Modern Indonesia since c.1200*, 300–334.
[186] Friend, *Indonesian Destinies*, 167–69.; Resosudarmo, *The Politics and Economics of Indonesia’s Natural Resources*, 180.
[187] Robison, *Indonesia*, 234.

The impact of the new foreign investment law and generally a more favorable attitude towards foreign operations was reflected in the relationship between multinational oil companies and oil-exporting Indonesia. Oil and gas extraction was governed under the so-called Production Sharing Contracts (PSC) that involved three parties: a multinational corporation, state-owned PERTAMINA, and the Indonesian government. These PSCs provided Indonesia with a sound framework that lasted three decades and allowed for maximum participation in the 1970s oil boom, significantly contributing to the country's economic development.

In more technical terms, the utilization of PSCs was primarily concentrated within Indonesia's upstream sector, which necessitated a substantial influx of foreign capital due to the capital-intensive nature of exploration. Article 33(3) of the country's constitution defined that the natural resources, including oil and gas, were under the state's control. Therefore, multinational corporations were required to establish contractual agreements with the government to operate and participate in production based on output. These contracts allowed the Indonesian government to outsource some of the exploration and fiscal risks to the multinational corporations while still profiting from the operations as well as tax revenues paid by the multinationals and PERTAMINA. According to Daniel Yergin, a renowned authority on the global oil industry and the author of several publications on the subject, including *The Prize: The Epic Quest for Oil, Money, and Power*, Indonesia played a pioneering role in the evolution of the oil industry on a global scale. He stated the following:

> At the same time that the "great concessions"[188] were being terminated, a new relationship was emerging between various petroleum exporting countries and international oil companies. Instead of being "concessionaries," with ownership rights to the oil in the ground, the companies were now becoming mere "contractors," with "production sharing" contracts that gave them rights to part of any stream of oil they discovered. This new type of relationship was pioneered by Indonesia and Caltex in the late 1960s. The "services happened to be the familiar ones of exploring for, producing, and marketing oil. But the shift in terminology reflected an all-important political change: The sovereignty of the country was recognized (…). The lingering aura of a colonial past was banished; after all, the companies were there merely as hired hands. By the mid-1970s, such production sharing contracts were being common in many parts of the world.
>
> Meanwhile, the amount of oil sold directly by the exporters themselves into the market, without benefit of the companies in their traditional role as middlemen, was increasing dramatically – quintupling from 8 percent of total OPEC output in 1973 to 42 percent by 1979. In other words, the state.-owned companies of the oil-producing countries were moving downstream, beyond production into the international oil business outside their own borders.[189]

Under Suharto's leadership, the Indonesian government sought to balance adherence to the country's constitution with the incorporation of foreign investment, as reflected in the production-sharing model. This approach involved multinational corporations entering into contracts with PERTAMINA, which was state-owned and under Suharto's direct oversight, allowing the government to maintain control over oil and gas development. Suharto's interpretation of these agreements was that they conformed to Article 33 of the 1945 Constitution, and the economic benefits that ensued from the partnerships reinforced the government's commitment to its developmental agenda.

Like many other countries, Indonesia experienced significant oil windfalls following the 1973 Arab Oil Embargo, which resulted in a substantial increase in oil prices (see Figure 5) and a corresponding escalation in the earnings of both the state-owned PERTAMINA, and the Indonesian government. Economist Peter Warr observed that "during the height of the oil boom,

[188] "Great concessions" in the oil and gas industry refer to large, lucrative contracts or licenses granted by a government to an oil and gas company to explore, develop, and produce hydrocarbons within a specific area.
[189] Yergin, *The Prize*, 652.

oil contributed to almost three-quarters of the country's export earnings and over 60 percent of the government's revenues."[190] American historian Theodore Friend also noted that during this period, "Pertamina's budget surpassed that of half of the entire national government."[191] While PERTAMINA continued to borrow in international markets to maximize and expand its operations, the government's dependence on the company posed a significant challenge. The establishment of the Organization of the Petroleum Exporting Countries (OPEC) embargo and the end of the gold standard in 1976 caused a shock to the international system, resulting in an increase in loan prices and soaring interest rates. This exposed PERTAMINA's and the Indonesian government's overleveraged debt and vulnerability.

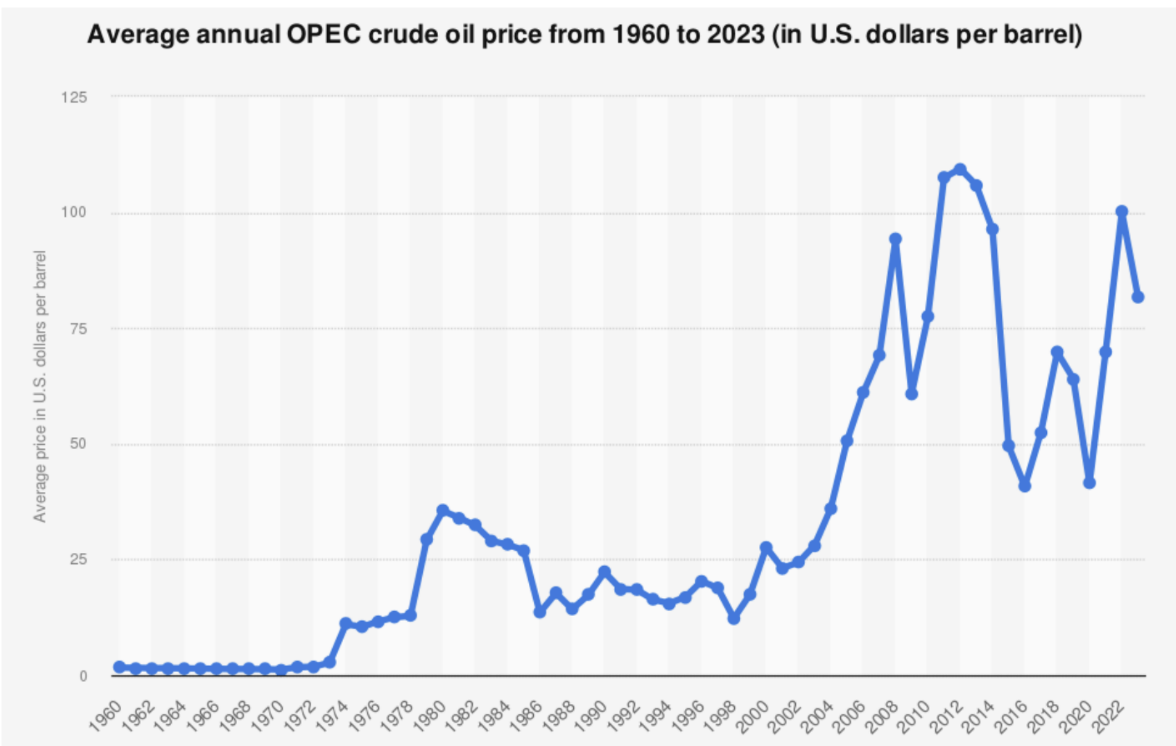


Figure 5: OPEC Oil Prices 1960 – 2023[192]

[190] Warr, *Indonesia's Other Dutch Disease*, 1.
[191] Friend, *Indonesian Destinies*, 167.
[192] "OPEC Crude Oil Price Statistics Annually 1960-2023."; en2x. "Average annual OPEC crude oil price from 1960 to 2023 (in U.S. dollars per barrel)." Chart. April 18, 2023. Statista. Accessed May 09, 2023. https://www.statista.com/statistics/262858/change-in-opec-crude-oil-prices-since-1960/

In contrast to many other OPEC counties, Indonesia, despite its reliance on foreign oil companies in oil extraction, experienced sustaining economic development from oil and built complementary and separate industries. The country's reserves constituted a substantial source of revenue and played a vital role in driving economic growth. The revenues generated from oil and gas facilitated reinvestment, which included substantial agricultural and rural developments.[193] As Friend pointed out, these investments played a significant role in the limited success of the Suharto government, which to a degree, succeeded in diversifying the economy and mitigating some of the oil dependence.[194]

Indonesia's oil windfalls brought several challenges due to the lack of regulation of PERTAMINA, the state-owned oil company that lacked legal and public accountability. The company's ambitious leader, Ibnu Sutowo, utilized the oil revenues to establish a vast conglomerate with subsidiaries in various industries. Anne Booth observed that Ibnu Sutowo believed it was legitimate to establish a 'state within a state' because of his seniority and higher military rank than that of President Suharto. As PERTAMINA expanded, it became increasingly corrupt and even indulged in criminal activities.[195] Simultaneously, the state-owned enterprise accumulated enormous debts, mostly beyond the government's control.[196] Friend highlighted that by 1975, PERTAMINA owed $120 million to the government and $2.3 billion[197] overseas, ultimately leading to the company defaulting on debt in 1975. The government had to rescue PERTAMINA. Although the debt and oil-financed stimulated investments and development in Indonesia, it also heightened the country's dependence on foreign investments and the global

[193] Friend, *Indonesian Destinies*, 338–41.
[194] Friend, 167–69.
[195] Booth, *Economic Change in Modern Indonesia*, 143.
[196] Ricklefs, *A History of Modern Indonesia since c.1200*, 338.
[197] Approximately $12 billion in 2023

economic system, including its commodity prices and investor sentiments.[198] In addition, the centralized and authoritarian nature of the PSCs, controlled by PERTAMINA and the Indonesian government, often ignored the interests of decentralized provinces and communities surrounding the oil extractions. As a result, provinces such as Aceh felt exploited by multinational corporations, PERTAMINA, and the Indonesian government, leading to far-reaching consequences that outlasted the Suharto regime, provincial tensions and placed the new democracy under stress. The following study shows that although the authoritarian state could suppress the contradictions between the socialist and nationalist Article 33 and the foreign investment law at the central level, it was unable to do so regionally.

### Production Sharing Case Study: ExxonMobil in Aceh

The International Labor Rights Fund (ILRF) filed a lawsuit against ExxonMobil in June 2001, alleging that the American oil giant was complicit in human rights abuses, including murder, torture, kidnapping, and sexual abuse, committed by the Indonesian military in Aceh. ExxonMobil denied these accusations.[199] The case was part of the 1976 – 2005 insurgency in Aceh, a struggle for independence from central and foreign control. Aceh, located in northwest Indonesia, has a long history of resistance to foreign exploitation, and foreign enterprises have been extracting the region's natural oil and gas deposits since the late 19th century.[200] The Acehnese independence movement and the hostility surrounding ExxonMobil's involvement in 2001 highlight the tensions created by foreign private enterprises and their investments in the region.

[198] Friend, *Indonesian Destinies*, 168–69.
[199] Banerjee, "Lawsuit Says Exxon Aided Rights Abuses."
[200] Ricklefs, *A History of Modern Indonesia since c.1200*, 184–90.

Since the colonial age, Aceh was exploited for its resources, especially oil and gas. Under Dutch rule, multinational companies such as Royal Dutch Shell and Standard Oil operated the Aceh fields from 1873 – 1913.[201] When Indonesia declared independence in 1945, and its first President Sukarno promised to regain control of the national economy, the Acehnese hoped to regain ownership of their resources. However, independent Indonesia's second President, Suharto, who ruled an authoritarian regime from 1967 – 1998, took control of Aceh's oil and gas deposits in 1971. In a quest for capitalist growth, the Suharto regime and its state-owned oil and gas company PERTAMINA contracted exclusive rights to these resources to Mobil Oil under a production-sharing contract. After Exxon merged with Mobil in 1999, ExxonMobil, then the largest American private company, took over the rights and continued the foreign operations in Aceh as the new subcontractor of PERTAMINA. As a result, Aceh's resources have been controlled by either a foreign enterprise or a joint operation between the central state and a foreign company since their discovery in the 19th century.[202]

In addition to joint control by foreign enterprises and the Indonesian government, Aceh's resources were further exploited as the profits generated were not been reinvested in the region. According to Michael Renner of the Worldwatch Institute, the Indonesian government's outsourcing of Aceh's land and resources in 1971 did not involve any compensation to the province.[203] Similarly, UCLA Professor Geoffrey Robinson stated that the Indonesian government did not reinvest any of the revenues generated from Aceh's oil and gas operations back into the province.[204] This means that not only were the Acehnese not compensated for giving up control of

[201] Vickers, *A History of Modern Indonesia*, 18.
[202] Robinson, "Rawan Is as Rawan Does," 129.
[203] Renner, "ExxonMobil in Aceh."
[204] Robinson, "Rawan Is as Rawan Does," 134.

their resources, but they were also excluded from the profits and reinvestments funded by these operations. Aceh was clearly exploited by Exxon, PERTAMINA, and the Indonesian government,

ExxonMobil, PERTAMINA, the Indonesian government, and President Suharto profited significantly from Aceh's lucrative oil and gas operations. For ExxonMobil, business in Aceh accounted for a fifth of the company's offshore revenues and was cost-effective. The Indonesian government and its representatives also benefited, collecting a fifth of all its oil and gas streams from ExxonMobil's operations in the region.[205] According to Professor Kerrie M. Taylor, the Suharto regime provided military units of the Indonesian army, known as *Tentara Nasional Indonesia* (TNI), as security for ExxonMobil's operations in exchange for blank shares in the company.[206] This deal illustrates that the state supported the PSC and reflects Suharto's personal ambition for growth. In contrast, Aceh's villagers lost control of their resources to the TNI.

The exploitation and control of Aceh's resources by ExxonMobil and the Indonesian state created a hostile environment that contributed to the emergence of the Free Aceh Movement in 1976. According to UCLA Professor Robinson, the combination of energy exploitation by foreign companies and the Indonesian government, along with cultural and religious oppression – President Suharto promoted secularity while the Acehnese are predominately Muslim – were central factors in the insurgency.[207]

The struggle for independence involved three main actors: the Free Aceh Movement and its guerilla force, the Gerakan Aceh Merdeka (G.A.M.), on one side, and the Indonesian government's Suharto-trained military (TNI), known for its brutality, on the other. ExxonMobil also became an increasingly significant player in this conflict. As ExxonMobil extracted oil and

[205] Coll, 95
[206] Taylor, "Thicker Than Blood: Holding Exxon Mobil Liable for Human Rights," 274.
[207] Robinson, "Rawan Is as Rawan Does."

gas under a government contract in Aceh, it began to create a 'state within a state' with its own agency. According to Michael Renner, Exxon's facilities were fenced off from surrounding communities, and expatriate management and engineering staff enjoyed luxurious living quarters. The company also possessed its own landing strip and caused gas flaring and chemical spills that harmed the community.[208] These actions, most of all the high-speed energy extraction and the emergence of an independent movement, ultimately led to ExxonMobil being targeted and involved in the Aceh insurgency.

The testimonies gathered in the context of the Aceh insurgency and ExxonMobil's relationship with Aceh, the G.A.M., and the Indonesian government offer valuable insights into the complexity of Indonesia's cooperation with private enterprises and foreign capital. In his book *Private Empire*, academic journalist Steve Coll examined ExxonMobil's recent history and geopolitical power and argued that considering the economic motivations behind the Aceh insurgency and the historical and contemporary memories of resource exploitation, ExxonMobil became a symbolic target for the G.A.M.. Di Tiro, the Aceh guerrilla leader, saw the removal of ExxonMobil as part of his war strategy and wanted "to prevent them from further stealing our oil and gas,"[209] highlighting the importance of resource nationalism. On the other hand, ExxonMobil became an active player in the war by contractually obligating the Indonesian military to defend its employees and infrastructure. The Aceh insurgency and ExxonMobil's involvement illustrate the complex and often contentious interactions between multinational corporations, foreign capital, and local communities in the pursuit of economic development in Indonesia.[210]

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[208] Renner, "ExxonMobil in Aceh."
[209] Coll, *Private Empire,* 96.
[210] Coll, 96–120.; Coll, 399–407.

In 2001, the situation between the Indonesian military, the G.A.M., and ExxonMobil reached a critical point. While ExxonMobil's resource extraction fueled the G.A.M.'s violence, the operations were vital to Indonesia's economy and three-year-old democracy. ExxonMobil had become a semi-active actor in the war and decided to shut down its operations to protect its employees. According to Steve Coll, this decision "provoked an outcry in Indonesia's parliament" and representatives threatened to nationalize the gas fields, demonstrating that resource nationalism was not limited to Aceh and reflecting the government's dependence on steady revenue flows.[211] Additionally, ExxonMobil's increasing authority over the operations contradicted Article 33, which requires state control over such production-sharing arrangements.[212] This in theory ensured that multinational companies contributed to the economic well-being of Indonesia or risk being perceived as a threat. The insurgency in Aceh reveals the various layers of resource nationalism at play. The Acehnese primarily resent the exploitation by the central government, while the nation as a whole, in light of its colonial history, resists foreign control and dependency.

The hostile situation between ExxonMobil, the Indonesian military, and the G.A.M., along with the pressure to maintain high yields, also placed the United States government in a delicate position. While the Indonesian government sought a quick restart of ExxonMobil's operations, the American administration under President George W. Bush prioritized protecting American lives and corporate interests. However, ExxonMobil's operations contributed to violence and human rights abuses. The threat to ExxonMobil's staff and infrastructure became so severe that the United States government under Bush sided with the Indonesian government and military and threatened to label the G.A.M. as a terrorist group, which could have resulted in the involvement of American

[211] Coll, *Private Empire*, 113.
[212] Butt and Lindsey, *The Constitution of Indonesia*.

soldiers. This threat of potential military involvement by the United States forced the G.A.M. to accept the oil and gas extraction and to focus its attacks on the Indonesian military rather than ExxonMobil.[213]

The hostility in Aceh resulted in harm to villagers and human rights abuses. According to Coll, ExxonMobil's presence continued to incite violence even after 2001. In 2003, two years after the diplomatic dispute with the United States government, Baharuddin, a local villager, was brutally beaten and tortured by the Indonesian military after walking down from his farm in the mountains. Coll described a scene after five days of torture when Baharuddin spoke to the commander: "You have an hour" to confess, he announced. "Why don't you shoot me now," Baharuddin recalled answering. "Okay, dig a hole," the commander finally said.[214] The Indonesian military suspected Baharuddin of being involved with the G.A.M. and saw him as a threat due to the location of his farm in the same mountains where ExxonMobil operated its gas and oil fields. Instead of killing Baharuddin, the military tortured him until he managed to escape and join the G.A.M. force.[215] According to Human Rights Watch, thousands of Acehnese suffered similar torture, were killed, or had to flee.[216]

The 2001 lawsuit filed by the ILRF on behalf of eleven Acehnese against ExxonMobil has been the subject of ongoing debate in the Federal District Court of the District of Columbia and the Supreme Court of the United States. Several independent organizations have also examined ExxonMobil's involvement and agency in the Aceh insurgency. The most recent ruling, in 2015, allowed the case to proceed. On July 27, 2022, a U.S. judge ruled that the lawsuit could go to trial,

[213] Coll, *Private Empire*, 99–120.
[214] Coll, 397.
[215] Coll, 396–99.
[216] "Aceh Under Martial Law."

ending a legal stalemate that had lasted for 21 years. The ExxonMobil case in Aceh is now moving forward.[217]

According to Coll, ExxonMobil "failed to anticipate the consequences of its operations in Aceh, and had failed to move actively to protect civilians as best it might."[218] This highlights the importance of understanding the historical context in which a corporation is operating, particularly in post-colonial countries. Multinationals involved in resource extraction must be particularly mindful of how their activities may trigger historical resentment and contribute to violence.

The case of ExxonMobil's involvement in the Aceh insurgency highlights several key concepts regarding the involvement of multinational corporations in Indonesia's oil and gas exploration. Firstly, the Indonesian government's reliance on the high yield of the Aceh fields emphasizes the significance of oil and gas in terms of modernization and national security. Secondly, the insurgency against the Suharto regime, which was perceived as more capitalist in nature, and ExxonMobil's presence in the region, suggests a general antipathy towards capitalist foreign control. Thirdly, the hostility towards ExxonMobil reveals a strong emotional attachment to national resources in a decolonizing economy and reemphasizes questions about the prioritization of economic growth versus national control over the economy and production. Fourthly, the Aceh War also demonstrates that cooperation between the Indonesian government and foreign companies is subject to international pressures and domestic regime changes. Finally, nationalists such as G.A.M. may view this cooperation to assert their own identity in opposition to the establishment and the capitalist world system.

[217] "US Judge Rules That ExxonMobil Case about Allegations of Complicity in Violence in Indonesia Can Go to Trial after 21 Years."
[218] Coll, *Private Empire*, 404.

In sum, this chapter has examined Suharto's Developmentalism, which balanced the liberalization policies of technocrats with the economic nationalist ideals of state control. Article 33 and the 1967 Foreign Investment Law created an environment that allowed Suharto to pursue economic growth through foreign direct investment and multinational corporations while retaining state control through contracts. Despite moderate diversification in the Indonesian economy, the country remained heavily reliant on oil and gas exports and global terms of trade. Economic nationalist sentiments resurfaced as foreign direct investment and multinational corporations gained greater control over the economy, particularly during the oil boom when the country was flush with cash and less dependent on foreign capital. While PSCs were legally sound contracts, the nature of PERTAMINA and its increased political and economic power led to economic inefficiencies due to abuses of power and corruption. Lastly, while the central government welcomed multinational corporations and their high-yielding oil and gas exploration projects, the provinces resented the exploitation of their resources and did not benefit from local operations. Their options to fight the authoritarian regime through legitimate channels were limited, and violence emerged. The next chapter will consider Indonesia's successful liberalization from the authoritarian rule of Suharto. Contrary to expectations, this democratization did not entail an absolute liberalization of foreign investments. Instead, a distinct paradigm of developmentalism emerged, wherein the state preserved its authority over vital resources, including oil and gas.

# Chapter Five:

## Reformasi, Democratization, and Developmentalism

*From Economic to Political Crisis*

By 1996, Indonesia had enjoyed an impressive three-decade streak of steady and robust economic growth that garnered praise from IMF and World Bank economists for its solid underlying fundamentals. During the last decade of Suharto's regime, the country was yet again a favored destination for foreign investors in the 1990s. However, investors always cautiously observed the political situation due to the crucial interconnectedness with the economy in Indonesia's history.[219] In 1997, conflicts erupted across Indonesia. Incidents of ethnic and religious violence rocked the provinces of Aceh and East Timor. These events reflected and increased dissatisfaction with the authoritarian Suharto government and caused political instability. As a result, the political and economic situation in Indonesia became increasingly precarious, and investors were inclined to withdraw their funds.

The Asian Financial Crisis that broke out in the same year exaggerated things further, originating in Thailand and resulting in rampant hyperinflation. The Suharto government's inadequate response to the economic crisis fueled the mounting political unrests and protests even more, contributing to the already fragile political environment. The rapid devaluation of the Indonesian rupiah immediately impacted the country's economy, and fuel and food prices became unbearable. Investor confidence plummeted, resulting in a decline in foreign investment by a substantial amount of $1.3 billion[220] in 1998 alone.[221] Amid public unrest, President Suharto was forced to step down in May 1998, and Vice President B.H. Habibie assumed power. Thus, the

[219] Sheng, *From Asian to Global Financial Crisis*, 218–24.
[220] Approximately 1.5% of total GDP in 1998
[221] Lindblad, "Foreign Direct Investment in Indonesia," 227.

economic crisis contributed to political instability and led to Suharto’s sudden downfall, marking another tipping point in Indonesian politics and signaling the beginning of a new era of political and economic reforms.

The underlying causes of the Asian Financial Crisis, particularly Indonesia’s vulnerability to it, have been the subject of extensive debate among scholars. Anne Booth, for instance, noted that the World Bank identified four “microeconomic causes of the crisis: the rapid accumulation of private external debt, a flawed banking system, deteriorating standards of governance and increasing corruption, and political uncertainty resulting from Suharto’s age and health and the lack of a clear successor.”[222] In addition, Andrew Sheng argued that the liberalization policies of the 1990s, particularly in the banking sector, led to “credit growth at the expense of credit quality” and increased vulnerability to the global system.[223] Overall, the Asian Financial Crisis exposed Indonesia’s weak institutions and poor governance, with capitalism and global economic dependency playing a central role. Domestically, the Suharto government prioritized political stability and economic growth, permitting excessive corruption and debt accumulation among the capitalist elite while striving for capitalist integration, leaving the country vulnerable to crises. In the aftermath of the Asian Financial Crisis, Indonesia’s stance towards foreign direct investment and multinational corporations remained ambiguous as the country underwent political democratization and economic recapitalization. While the country initially required foreign capital to recover from the severe economic shock, Indonesia began to adopt a more protective stance towards its economy, particularly in the natural resource sector, with the onset of the second resource boom in 2003.

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[222] Booth, *Economic Change in Modern Indonesia*, 92.
[223] Sheng, *From Asian to Global Financial Crisis*, 231.

The following section presents an analysis of the political discourse that emerged in the aftermath of the Asian Financial Crisis and throughout the democratically elected presidencies. Additionally, I conducted a series of interviews with industry experts in January 2023, which provided additional insights into the political economy surrounding foreign investment and the oil and gas industry. The economic policies concerning foreign direct investment and multinational corporations have remained ambiguous and continue to be contested by the Constitutional Court. Moreover, despite the end of the second resource boom in 2012 and the government's renewed need for foreign capital, resource nationalism has continued to rise, and Indonesia is pursuing policies of "no strings attached." This suggests that the state takes an active part in the economic development of the country.

## Campaign Promises vs. Political Economy

In 1998, Suharto's opponents rallied under the banner of *reformasi*, a movement calling for political and economic reforms in Indonesia. At the very end of his presidency, Suharto made agreements with the IMF to rescue the Indonesian economy and maintain his grip on power. These IMF policies were designed to implement neoliberal reforms and re-establish macroeconomic control. Despite this, many Indonesian citizens, particularly the *pribumi*, viewed these reform packages as unconstitutional and threatening their livelihoods.[224] In addition, a foreign government official disclosed that Indonesian political leaders were infuriated by the IMF's insistence on linking reform conditions to the financial bailout.[225] This provoked widespread rioting and looting, fueling anti-capitalist and anti-foreign sentiments. The violence during these protests targeted

[224] *Indonesia - Financial Crisis*.
[225] Wenger Interviews, Jakarta 2023

Suharto's regime politically, while the economic front was aimed at Chinese Indonesians and foreigners who dominated the capitalist private sector. Consequently, many Chinese and foreigners fled the country. Ultimately, the political unrest and economic turmoil forced Suharto to resign in 1998.[226]

The policies implemented by the three *reformasi* presidents, B.J. Habibie, Abdurrahman Wahid, and Megawati Sukarnoputri, who assumed office after Suharto's regime between 1998 and 2004, were more inclined towards nationalization and less focused on economic liberalization policies. As Booth observed, the resistance to privatization was significant, in the parliament and among bureaucratic circles. All three presidents exhibited a limited willingness to confront this resistance. Additionally, powerful interest groups maintained their control over government agencies and courts, protecting their interests. According to the World Bank, corruption escalated between 1996 and 2005, making the country remain high-risk and uninviting to foreign investors.[227]

In the aftermath of Indonesia's economic and political crises, foreign direct investment and multinational corporations were not initially a major focus of the *reformasi* discourse. However, as foreign investment became a vital indicator of the economy's resilience and recovery, Indonesia's attitude toward foreign investment shifted. Apart from the Chinese riots in 1998, Indonesian political discourse, in a state of crisis, did not focus on driving out foreign capital; instead, the country had the onus of attracting foreign investors by demonstrating that it was a safe and secure location for investment. One foreign commercial lawyer observed that "after the financial crisis, Indonesia was looking for credibility and welcomed any kind of foreign

[226] Murphy, "Indonesia and Globalization."
[227] Booth, *Economic Change in Modern Indonesia*, 123.

investment, across all sectors."[228] However, foreign investors were cautious and adopted a "wait-and-see" approach, closely monitoring Indonesia's political developments and associated risks based on past negative experiences.[229]

The election of Susilo Bambang Yudhoyono (SBY) in 2004 marked the end of the transition from the Suharto era and the Asian Financial Crisis and signaled hope for a new direction. On October 4th, 2004, Dr. Priyambudi Sulistiyanto from the Southeast Asian Studies program at the National University of Singapore stated toward the newspaper *TODAY* that "the region has been waiting for Indonesia to have a leader they think would improve the relationship (with foreign investors) by improving political stability that will lead to economic recovery in Indonesia."[230] This was also a democratic milestone in Indonesia's history as it was the first time that Indonesians elected their leaders directly. SBY's education in the United States and his commitment to creating a 'business-friendly, modern, democratic, outward-looking, open, and tolerant Indonesia' added to the optimism surrounding his presidency. His national development plan prioritized the need for an increase in private investments and sought to attract foreign capital through large-scale infrastructure projects.[231]

Despite SBY's proclamations of support for restructuring state enterprises and increasing foreign investment, Indonesia's post-2004 economic recovery was mainly due to favorable trade conditions rather than a series of effective reforms. Indonesia's economy rebounded as a result of advantageous global commodity prices between 2003 and 2012 that were driven by the rising demand from China and India. Indonesia's economy benefited from substantial export revenues. This second resource boom was more diversified than its predecessor was in the 1970s. Strikingly,

[228] Wenger Interviews, Jakarta 2023
[229] Lindblad, "Foreign Direct Investment in Indonesia," 227.
[230] "High Hopes for New Indon Leader."
[231] Booth, *Economic Change in Modern Indonesia*, 107–10.

the country's export was not solely reliant on oil and gas. In fact, Indonesia became a net importer of crude oil in 2003.[232] Other commodities, such as palm oil, gas, coal, and metals, gained significance.[233] While the make-up of Indonesia's exports diversified, its reliance on export and resource extraction continued to derive its economy.

Joko Widodo's election as President in 2014 yet again raised hopes for significant changes in Indonesia. Promising to "tame the octopus of the oligarchy,"[234] Jokowi pledged to deliver inclusive and sustained economic growth, development, and social welfare for the Indonesian people. However, nearly a decade into his presidency, it has become evident that he has been unable to fulfill these campaign promises. According to foreign correspondent Ben Bland, the Jokowi government demonstrated "a disregard for expert advice, a lack of trust in civil society, and a failure to develop a coherent strategy."[235] Bland's opinion was shared by journalists, think tank academics, and independent businesspeople, who in interviews all indicated that the Indonesian government lacks capital and requires certain qualifications, such as technology transfer, to promote foreign investments.[236] In contrast, the elites' interests continue to dominate the Indonesian political economy. There remains a pressing need for foreign investment, which is set against a culture of protectionism and historical skepticism toward economic liberalization.

The bottlenecks inherent in Indonesia's slow bureaucracy pose yet another obstacle to the effectiveness of foreign investment in the country. One demonstration of the "strings attached" to foreign investments in Indonesia is the significant capital requirements. According to a foreign commercial lawyer, the Ministry of Investment (BKPM), which oversees all foreign investment, mandates that foreigners must deposit 10 billion rupiahs ($681'478) in the bank to establish a

[232] Hill and Pasaribu, "Some Reflections on Indonesia and the Resource Curse."
[233] Booth, *Economic Change in Modern Indonesia*, 107–10.
[234] Bland, *Man of Contradictions: Joko Widodo and the Struggle to Remake Indonesia*, 11.
[235] Bland, 12.
[236] Wenger Interviews, Jakarta 2023

company, and can only truly invest through shared contracts with Indonesian companies. Additionally, Indonesians resist foreign personnel and aim to develop their own skilled workforce. Consequently, the Indonesian government obliges only a select few affluent foreigners and multinational corporations to engage in long-term commitments via substantial capital investments.[237]

The Jokowi administration employs a strategy of attracting private domestic and foreign investment through personal hand-shake deals and on its own terms. One of Jokowi's ministers noted that "Indonesian politics is about seducing people with profits, not ideas and ideology."[238] These arrangements can be advantageous for both parties, especially given the country's abundant natural resources. However, foreign investors and corporations are subject to the whims of the Indonesian political economy, bureaucracy, and economic disparities resulting from patronage and clientelism. Consequently, the Indonesian investment climate is weakened by constant political and legal uncertainty, as well as an unreliable bureaucracy and corruption. According to the Jakarta Post, "the BKPM canceled the licenses of 6'541 foreign direct investment projects worth $23 billion between 2007 and 2012 due to difficulties in land acquisition and getting permits from local governments."[239] Currently, the realization of foreign investment in Indonesia stands at only 30 to 40 percent.[240] An industry consultant summarizes Indonesia's investment realization issues as the 3C's: credibility, consistency, and clarity.[241]

Although foreign investors face various challenges in Indonesia, including regulatory and bureaucratic hurdles, there is no significant anti-foreign sentiment exhibited by the Indonesian people. A foreign investment lawyer confirmed that he had not encountered such sentiment,

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237 Wenger Interviews, Jakarta 2023
238 Bland, *Man of Contradictions: Joko Widodo and the Struggle to Remake Indonesia*, 13–46.
239 Post, "Reinvigorating Investment."
240 Warburton, "A New Developmentalism in Indonesia?," 359.
241 Wenger Interviews, Jakarta 2023

despite the unfavorable regulatory environment since the 1998 Chinese riots.[242] In 2018, Professor Diego Fossati conducted a study on national identity and public support for economic globalization in Indonesia. The study surveyed 1'422 Indonesians from diverse backgrounds. Fossati discovered that although respondents were more skeptical of the benefits of foreign investment to the national economy than the benefits of international trade, the majority (72 percent) still regarded foreign investment as an opportunity. However, the sample was divided as to whether foreign investment should be increased, with a slight majority (50.5 percent) suggesting that it should generally be limited.[243] The absence of widespread public dissatisfaction with foreign investment in Indonesia implies that the regulatory constraints, which are detrimental to foreign investors, are sustained by influential interest groups in the country's political economy.

Foreign investors have witnessed a significant reduction in high-impact business challenges in Indonesia over the past few years, particularly since the outbreak of Covid-19. Indonesia relaxed its regulatory regime towards foreign investment during the pandemic to attract capital and stabilize its economy. President Jokowi delegated overall management oversight to Luhut Pandjaitan, one of his most trusted advisors, to reduce decision-making bureaucracy and streamline the licensing process for foreign investors to improve realization rates.[244] According to a survey by Australian Business in ASEAN, the Omnibus Law on Job Creation (Law No. 11/2020) passed in 2020 has significantly improved and opened business opportunities for foreign investors. The Omnibus Law is a bill that aims to create jobs and raise foreign and domestic investments by reducing regulatory barriers. Think tanks have emphasized the bill as it simplifies the process of obtaining licenses and land ownership for firms, which have previously been among the main

242 Wenger Interviews, Jakarta 2023
243 Fossati, "National Identity and Public Support for Economic Globalisation in Indonesia."
244 Post, "Reinvigorating Investment."

hindrances for investors. Despite public protests and the Indonesian Constitutional Court ordering the government to amend the law within two years, industry experts suggest that it is unlikely that the government will completely reverse the measures.[245]

In the context of business operations in Indonesia, foreign investors have identified several factors that make the country an appealing destination for international investments. These factors include a sizable domestic market, a growing middle class, abundant natural resources, and a stable economy. Despite these advantages, however, foreign investors have also reported certain challenges that diminish Indonesia's attractiveness as a destination for foreign investment. Challenges include government bureaucracy, widespread corruption, and inadequate infrastructure. According to the results of a survey conducted in 2022, the highest obstacle to foreign investment in Indonesia was thought to be government bureaucracy, as mentioned by 31 percent of the respondents. This figure represents a significant decline from the 62 percent reported in 2021. The second and third highest barriers to foreign investment listed were access to skilled labor and the tax system, respectively.[246]

The improved investment climate in Indonesia resulted in an increase in foreign direct investment. According to an ASEAN Briefing, "Indonesia received a record-breaking $43 billion in foreign investment in 2022, representing a 44 percent increase from 2021." The report also observed that "the metal mining industry mainly drove this growth, as the Indonesian government aims to enhance its downstream capabilities, particularly for nickel."[247] In real terms, foreign direct investment in Indonesia has been increasing in recent years. Notably, foreign direct investment incorporation is sector-specific, and the government prioritizes downstream projects over

[245] Wenger Interviews, Jakarta 2023
[246] Wenger Interviews, Jakarta 2023
[247] "Indonesia's Breakthrough Year for Foreign Investment in 2022."

upstream initiatives to increase Indonesia's role in value creation.[248] Nevertheless, the resource extraction continues.

Unsurprisingly, the growth in foreign direct investment was accompanied by a surge in economic nationalism and state intervention, especially in the natural resource sectors. A global consultant indicated that despite Jokowi's pro-business aspirations, during his campaign for re-election in 2019, which happened to coincide with Chevron's discontinuation of its oil exploration contract, he shifted to a discourse that portrayed him as the one ousting Chevron and regaining national control over the oil and gas industry. The consultant observed that this rhetoric was not essential for Jokowi's re-election, but the President aimed to appease the political economy of resource nationalist and ensure political stability.[249] In the case of oil and gas, resource nationalism led the government to diminish the control of multinational corporations while augmenting state control.

In the context of sustainable development and increased demand for minerals such as lithium, nickel, and cobalt, resource nationalism has become even more widespread in mining and metal extraction. In 2014, Indonesia imposed a ban on nickel exports and is now on the verge of entering into a car production contract with Tesla and BYD, the world's largest electric vehicle manufacturers. President Jokowi attributed this opportunity to his efforts to capture domestic value creation (downstreaming). In a January 28, 2023 article with *The Economist*, he stated that "this success will be replicated for other commodities."[250] A journalist from Indonesia noted that President Jokowi is currently "obsessed with downstreaming" and creating value and employment

[248] Downstream refers to the stages of a production process that involve the processing, refining, and distribution of raw materials. Regarding global supply chains, developing countries aim to capture more of the created value within domestic borders. Upstream refers to the exploration and extraction of raw materials, such as oil and gas.
[249] Wenger Interviews, Jakarta 2023
[250] "Indonesia Embraces Resource Nationalism."

opportunities for Indonesians.[251] Indonesia continues to safeguard its national resources and maximize their economic values within its borders. International and multilateral organizations have criticized the Indonesian government's protectionist policies. The World Trade Organization (WTO) and the European Union (EU) condemned investments with strict conditions, such as Indonesia's nickel export ban. Nonetheless, Jokowi affirmed that "This is what we want to do: be independent, independent, independent."[252] This rhetoric echoes the anti-imperial and self-sufficiency-oriented discourse of Indonesia's first President, Sukarno. Consequently, the foreign investment climate in natural resources in Indonesia deteriorated.

A few of the Indonesian government's recent foreign policy decisions reflect a return to non-alignment through protectionist behavior in the natural resource economy. Indonesia abstained from the recent United Nations General Assembly Resolution ES-11/3, which called for the suspension of Russia's membership in the United Nations Human Rights Council. Additionally, during the G-20 Summit held in Bali in November 2022, Jokowi, in his opening address, called for peace, cautioned against another Cold War, and refrained from condemning Russia. I am not suggesting that Indonesia has completely abandoned its pro-Western and capitalist integration stance, as Indonesia aligned with the West on other recent General Assembly Resolutions and acted as a leader in promoting cooperation during the G-20. However, certain Indonesian foreign policy decisions suggest a more non-aligned approach and the attitudes toward resource export resemble the protectionist tendencies that have characterized Indonesia's economic history. Regarding foreign investment operations, these non-aligned tendencies have manifested themselves in increasingly emphasizing the constitutional text and role of the state, as we will consider in the next section.

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[251] Wenger Interviews, Jakarta 2023

[252] "Indonesia Embraces Resource Nationalism."

## The Rise of the Constitutional Court

After the fall of Suharto and the Asian Financial Crisis in 1998, Indonesia faced a tumultuous period marked by economic challenges, corruption, and rapid changes in leadership. Evidence indicates that influential parliamentary groups exerted undue influence over government restructuring agencies and courts, favoring businesses associated with the old Suharto clan.[253] This harmed foreign investment. Nevertheless, Indonesia's status as a destination for foreign investment has seen a marked improvement, with a substantial increase in inward investment flows since 2005. Between 2008 and 2012, Indonesia received the second-highest amount of foreign direct investment among Southeast Asian countries after the much smaller Singapore. However, despite election campaign pledges to enhance Indonesia's outward-looking stance, the country's approach to cooperation with foreign investors and multinational corporations remains ambiguous and industry specific.[254] The post-Suharto era in Indonesia has been identified by scholars as a form of new developmentalism. Eve Warburton stated that this new developmentalism is "characterized by a normative commitment to an activist state that can engineer fast economic growth, direct industrial upgrading, and ensure economic redistribution." In contrast to the old developmentalism alluded to in the literature review, this new form "responds to and embraces globalization" and thus implements neoliberal reforms in the economy, while at the same time displaying high level of state intervention in specific sectors through a renewed empowering to the state-owned enterprises.[255]

[253] Booth, *Economic Change in Modern Indonesia*, 104.
[254] Booth, 104–9.
[255] Warburton, "A New Developmentalism in Indonesia?"

For example, after the Asian Financial Crisis, the state implemented select political, economic, and legal reforms that exhibited neoliberal characteristics. These reforms were largely driven by the IMF, which acted as a lender of last resort. In an attempt to restore lost momentum, the Habibie government pursued further liberalization of the banking system in 1999. This included allowing 99 percent foreign equity ownership in banking and permitting foreign banks to establish offices throughout Indonesia. However, the Indonesian Bank Restructuring Agency (IBRA), which had quasi-nationalized many existing banks, remained in control of the financial system and was guided by interest groups associated with the old Suharto regime.[256] Nonetheless, these reforms increased foreign influence within Indonesia's financial network.

Yet, regulatory reform in Indonesia continued to exhibit a degree of ambiguity and pragmatism, and the legislation towards investment was only revised in 2007. Under the SBY government, the Indonesian parliament finally enacted Law 25/2007 on Investment, which combined both domestic and foreign investment under one legal framework. This measure was intended to enhance investor guarantees by replacing the outdated investment laws from 1967 and 1968. Moreover, the new law enabled foreign investors to enjoy 100 percent ownership in sectors that were not included in the negative investment list. The legislation also envisioned offering more fiscal incentives and streamlining investment procedures. Thus, the retention of the central coordination role by the BKMP was viewed by many as a disappointment.[257] According to a foreign commercial lawyer, the BKMP had been further centralized over the years to the extent that it now oversees the licensing of millions of investments, resulting in a slow and inefficient investment process.[258]

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[256] Lindblad, "Foreign Direct Investment in Indonesia," 229.; Bennett, "Banking Deregulation in Indonesia: An Updated Perspective in Light of the Asian Financial Crisis."
[257] Lindblad, "Foreign Direct Investment in Indonesia," 229.; USINDO, "The Investment Negative List."
[258] Wenger Interviews, Jakarta 2023

Later in 2007, the BKMP issued and revised the negative investment list, which outlined the sectors closed to foreign investment and the percentage of foreign ownership allowed. Despite the intended purpose of increasing investor certainty, the implementation of the new investment law and the negative investment list had the opposite effect, leading to increased legal uncertainty. The United States-Indonesia Society (USINDO) even stated that these measures served as a deterrent to foreign investment.[259] Only recently, in 2020, the Indonesian legislature (DPR) passed the 2022 Omnibus Law to replace the negative investment list to rehabilitate the economy amid the Covid-19 crisis. Except for "seven strategic sectors," the Omnibus Law liberalized the regulatory framework for both domestic and foreign investment in Indonesia and reduced barriers to private business operations.[260] The law was deemed "conditionally unconstitutional," and the Constitutional Court ordered that it be revised. The implementation of the Omnibus Law in 2023 remains to be determined, though think tanks claim significant changes are unlikely.[261]

Although legal and political reforms are limited, the attitude towards foreign investment shifted in Indonesia, and the regulatory framework, in general, became more welcoming to both foreign and domestic investment. Simultaneously, the Constitutional Court has gained increasing influence over economic policymaking ever since its establishment in 2003. In light of the government's efforts to promote investment by removing impediments, the Constitutional Court has contested these measures by advocating for the literate interpretation of Article 33, which mandates that the Indonesian state exercise direct control over the nation's natural resources, including oil and gas.[262]

[259] USINDO, "The Investment Negative List."
[260] "Indonesia."
[261] "Court."
[262] Butt and Lindsey, "Economic Reform When the Constitution Matters."

*The Constitutional Court, Article 33, and the Oil and Gas Law*

During the *reformasi* period, Indonesia exhibited a keen interest in attracting foreign investment and sustaining operations in the extractive industries to rehabilitate the economy and generate revenue. As a result, Law 22/2001, also known as the Oil and Gas Law, was enacted in 2001 to supersede its predecessor from the 1960s. These laws were founded on Article 33(3) of the 1945 Constitution, which stipulates that "the land, waters, and natural resources within them shall be subject to state authority and utilized for the maximum benefit of the people."[263] The fundamental distinction between the 1960s and 2001 versions of the law centers on the entity designated to act on behalf of the Indonesian state. Prior to 2001, the state was represented by the state-owned oil and gas enterprise PERTAMINA, which typically executed projects by way of production-sharing contracts (PSC) with multinational corporations, such as Exxon in Aceh. The revised 2001 law relieved PERTAMINA of its administrative responsibilities and introduced the regulatory body BP MIGAS, which assumed the role of overseeing and regulating oil and gas exploration contracts in Indonesia.[264] Thus, foreign companies now entered into contracts with an independent regulatory body tasked to mitigate corruption and improve corporate governance.

In 2002, the Indonesian national legislature enacted four constitutional amendments, including the 2003 establishment of the Indonesian Constitutional Court (*Mahkamah Konstitusi*). The primary objective of the court was to regulate the roles of private enterprise and state intervention, effectively relieving the parliament of its duty to determine the appropriate level of state intervention and dividing power between the state and businesses. The court was tasked with making the final decision in the review of statutes to resolve disputes involving state organs.

[263] Butt and Lindsey.
[264] Karim, "A Controversial Decision of the Constitutional Court on the Indonesian Oil and Gas Law."

Moreover, the court was designed to embody the spirit of the 1945 constitution and de-emphasize the state's development goals.[265]


Image 2: The Constitutional Court (*Mahkamah Konstitusi*) in Jakarta – Image taken by Jan Wenger during field work in Jakarta in January 2023

The Indonesian Constitutional Court assumed a significant role in the country's political economy, particularly in 2011 when a challenge was mounted against the 2001 Oil and Gas Law. Critics argued that the law favored foreign companies and was formulated under the influence of international pressure, notably from the IMF, which presumed the necessity of a competitive regulatory framework for oil and gas and provided financial assistance in the wake of the economic crisis. An international consultant observed that the law was composed by a member of the so-called "Berkeley Mafia." He further noted that his influence was indirectly exerted, as USAID simultaneously paid the Indonesian government 7 million dollars.[266] Accordingly, as Indonesia

[265] Booth, *Economic Change in Modern Indonesia*, 154.; Butt and Lindsey, "Economic Reform When the Constitution Matters," 240–41.
[266] Wenger Interviews, Jakarta 2023

sought to recover from the Asian Financial Crisis, it found itself once again dependent on foreign investments and aid, leading to compromises in the drafting of the oil and gas law that favored multinational corporations. Despite Sukarno's warning half a century ago, the paradigm of "strings attached to aid" played a significant role in shaping the trajectory of the oil and gas law.[267]

In 2012, the Indonesian Constitutional Court ruled that some 2001 Oil and Gas Law provisions were inconsistent with Article 33(3) of the constitution because the law was crafted in response to IMF recommendations and favored foreign interests. The court focused on the interpretation of the term "control" and whether independent regulatory oversight was sufficient to satisfy Article 33(3) or if direct state control was necessary. The court ruled for the former and declared that BP Migas was impeding state control over oil and gas, resulting in inefficiencies and the potential for abuse of power. As a result, BP Migas was stripped of its functions, which were transferred to the Minister of Energy and Natural Resources, who established the Special Task Force for Upstream Oil and Gas Activities, known as SKK Migas. SKK Migas assumed the same administrative responsibilities as BP Migas but is directly accountable to the Ministry of Energy and Natural Resources and, as of 2018, reports directly to the President.[268]

Since the annulment of the Oil and Gas Law in 2012, the absence of a proper legal and regulatory framework has resulted in the guidance of business operations in the oil and gas sector through executive orders issued by the President and the special task force (SKK Migas). For instance, in 2017, the government introduced a new scheme for PSC contractors in response to a dearth of foreign investment. This scheme, known as the gross-split PSC, replaced the cost-recovery scheme. Under this new arrangement, the PSC contractor could obtain a greater share of the gross production of oil and gas than under the cost-recovery scheme, but at the expense of

[267] Karim, "A Controversial Decision of the Constitutional Court on the Indonesian Oil and Gas Law."
[268] Karim.; Magnar, Junaenah, and Taufik, "Tafsir MK Atas Pasal 33 UUD 1945."

bearing all operational costs. According to an oil and gas consultant, the ramifications of this change are yet to be fully determined.[269] The next section will consider how this lack of regulatory consistency and certainty has already significantly affected foreign operations in the oil and gas industry in Indonesia.

**Big Oil Exit**

In April 2023, PERTAMINA, the Indonesian state-owned enterprise, is on the verge of acquiring Royal Dutch Shell's 35 percent ownership of the Masela gas block, one of Indonesia's most extensive and strategically significant liquified gas blocks. The Masela operations have experienced a standstill since the Jokowi government mandated a transition from high-risk, high-yield offshore development to smaller, less risky, and less economically efficient onshore development.[270] An international consultant noted that the onshore project's objective was to establish a development cluster to support the economic welfare of the provinces surrounding the Masela block and create employment and growth opportunities for Indonesians.[271] It appears that the national and provincial development interests are superseding the focus on economic efficiency and high yields.

Indonesia's PERTAMINA also transitioned from offshore to onshore exploration due to its technological inability to extract gas reliably from offshore fields. In 2015, newly elected President Jokowi rejected a development plan proposed by Japan's Inpex and Royal Dutch Shell, which sought to use Shell's floating liquefied natural gas technology (FLNG) to extract gas from the Masela block. With PERTAMINA now acquiring Shell's stake, production output is expected

[269] Wenger Interviews, Jakarta 2023
[270] Mcbeth, "Indonesia in Big Flip-Flop on Floating LNG Technology."
[271] Wenger Interviews, Jakarta 2023

to decline. The company will have to procure $6.3 billion in capital expenditures to develop a field that market analysts deem uneconomic at present.[272]

PERTAMINA's efficient exploration and production of oil are subject to significant pressure due to limited technical expertise and substantial capital expenditures. In contrast, international oil companies (IOC), owing to their extensive size and technological proficiency, can manage exploration risk and exposure to capital expenditures more effectively. An international consultant has reported that the IOCs' advanced 3-D deep-sea drillers enable them to predict the location of oil and gas pockets with remarkable accuracy. He also stated that this technology requires a team of engineers and experts that is costly to maintain, and the IOCs do not share it with companies like PERTAMINA.[273] Despite PERTAMINA's technological advancements, the state-owned enterprise remains reliant on the Ministry of Energy and Mineral Resources' budget and cannot compete with the private IOCs. Consequently, PERTAMINA faces high exploration risk and limited capital capabilities and must pursue low-risk and low-yielding oil and gas operations.

The conclusion of Shell's Masela block operations would not be the first instance of the Indonesian government, PERTAMINA, and an international oil company terminating collaboration. In the previous ten years, PERTAMINA had essentially nationalized the Mahakam gas fields in East Kalimantan, previously operated by French oil company Total, and the Rokan oil block in southern Sumatra, where America's Chevron had developed a deepwater project. According to an international consultant, production in the Rokan field dropped by 40 percent when Chevron exited.[274] In addition, since the enactment of the new oil and gas law in 2001,

[272] Mcbeth, "Indonesia in Big Flip-Flop on Floating LNG Technology."
[273] Wenger Interviews, Jakarta 2023
[274] Wenger Interviews, Jakarta 2023

ExxonMobil, one of the remaining IOCs, PERTAMINA, and the Indonesian government have been embroiled in a dispute over the management and revenue-sharing of the CEPU oil block in East Java.[275]

The energy sector in Indonesia has experienced a significant reduction in both exploration endeavors and production output, particularly in oil. This predicament was further compounded by a continuous rise in energy demand. Remarkably, Indonesia became an oil net importer in 2003, and in 2004, its oil production declined significantly below the historical benchmark of one million barrels per day.[276] Although gas production has shown a relatively slower deceleration rate due to easier discovery, the Ministry of Energy and Mineral Resources projects that Indonesia will become a net gas importer by 2040. The decrease in production is primarily attributed to the natural depletion of oil and gas fields, with some in operation for as long as five decades. Additionally, exploration activities have become increasingly expensive and risky, and technology and expertise intensive rendering them less appealing to investors, as advised by an international consultant.[277] However, natural challenges in exploration are not the only cause of declining oil production output in Indonesia.

A noteworthy pattern of frequent exits by international oil companies has accompanied and amplified the declining trend in Indonesia’s oil and gas production. To comprehend this phenomenon, one must first understand the organizational structure of these oil giants. As noted by an international consultant, IOCs have access to global pipelines and teams of experts who evaluate fiscal terms of oil and gas exploration projects worldwide, allowing them to cherry-pick the most financially attractive regions and countries.[278] In addition, Indonesia’s oil and gas

[275] Boyd et al., “A Note on Policies for the Oil and Gas Sector.”
[276] Davidson, “The Demise of Indonesia’s Upstream Oil and Gas Regulatory Agency,” 120.
[277] Wenger Interviews, Jakarta 2023
[278] Wenger Interviews, Jakarta 2023

operations have become fiscally unappealing due to increasing state intervention in development plans. For example, the Indonesian government unilaterally insisted on laying a 180-kilometer pipeline from offshore to onshore in Shell's Masela block project, adding an extra USD 4 billion to the venture project.[279] According to analysts cited in the *Asia Times* on April 6, 2023, "if Indonesia wants to compete with the production-sharing regimes of other countries, especially new frontier areas like West Africa and Latin America, it needs a drastic paradigm shift." These analysts further explained that "it currently takes up to two years for an exploration firm, new to Indonesia, to open an office, secure financial and technical approvals, tender for goods and services, and acquire seismic data, and it can take another two years to prepare for drilling an offshore well."[280] Therefore, the decreasing trend in IOCs' exploration operations in Indonesia can be attributed to multiple factors, including declining oil reserves, more financially attractive global alternatives, increased state intervention by the Indonesian government, and inefficient bureaucracy. As a result, IOCs have refrained from pursuing new development projects and renewing their contracts, leading to their exit from the Indonesian market.

While Indonesia's oil and gas reserves are in decline, the country still holds significant exploration potential, particularly in the deep waters of its eastern regions, requiring the involvement and technical expertise of international corporations, according to an Indonesian energy society.[281] Although exploration has decreased by an average of 23 percent over the past decade, Indonesian officials continue to take pride in the 68 unexplored oil and gas basins in the country, as highlighted by John McBeth of *Asia Times*.[282] Nonetheless, the critical matter pertains

[279] Mcbeth, "Indonesia in Big Flip-Flop on Floating LNG Technology."
[280] Mcbeth, "How Nationalism Destroyed Indonesia's Oil and Gas."
[281] Wenger Interviews, Jakarta 2023
[282] Mcbeth, "How Nationalism Destroyed Indonesia's Oil and Gas."

to the selection of the entities selected for extracting and selling the oil and gas, as well as the timing of such activities.

An energy expert in Indonesia has presented two conflicting views on the country's remaining oil and gas resources. One perspective suggests that the Indonesian government should collaborate with IOCs to share capital expenditures, mitigate exploration risks, and curb the ongoing decline in oil production. This approach recognizes the steady decline in oil production coupled with increasing domestic consumption as a significant threat to the country's energy security, trade balance, and national income. Although oil revenue no longer contributes 60 percent of the government's total revenue as it did during the first oil boom in the 1970s, it still accounted for 20 percent of its revenue in 2010. On the other hand, some argue that Indonesia's remaining oil and gas reserves will not vanish and can be extracted later and under the country's terms. This faction advocates for the extraction and sale of oil and gas under the control of the Indonesian state, as stipulated by Article 33(3). According to an international consultant, interest groups that support this position significantly impact the country's political economy. By prioritizing the pressures of Article 33(3) and adhering to what some consider resource nationalism, the Indonesian government has intentionally maintained an unfavorable economic and legal environment that discourages IOCs from pursuing further exploration in the country. He noted that by accepting domestic oil and gas exploration constraints, the government leaves millions of dollars in tax revenue daily and prioritizes economic sovereignty and political stability.[283]

The impact of Article 33(3) on government decision-making and policies regarding oil and gas resources is significant, with the political economy playing a crucial role in shaping these decisions. The global empire of IOCs has amassed market power, enabling them to influence

[283] Wenger Interviews, Jakarta 2023

regulatory regimes worldwide, leading to a global convergence of tax standards in oil and gas operations. However, Indonesia has been an exception, as it is unwilling to conform to the industry's global norms of tax standards. Article 33(3)'s political economy has successfully created resistance against the Indonesian government's efforts to provide favorable deals to IOCs.[284] Given the country's colonial past, history of exploitation, and constitutional law, a regulatory framework that prioritizes foreign interests and allows for oil and gas extraction at higher efficiency is not politically viable. The abolition of the Oil and Gas Law in 2012 played a significant role in this development, as it shifted control and accountability over oil and gas resources from regulatory bodies back to the Indonesian state. Therefore, I argue that establishing the Constitutional Court in 2003 has further empowered the political economy around Article 33(3), strengthening the state's power and domestic influence. Paradoxically, rather than enhance independence, it has promoted a new dependency through oil imports.

In Indonesia, Article 33(3) has become a rallying point for various interest groups, including political Islam, resource nationalists in both Jakarta and the provinces, and import interest groups. Their shared objective is to expel foreign capital and corporations from the oil sector, and their political clout in Indonesia has increased significantly over the past two decades. Political Islam bases its financing and investment on Sharia Law, which rejects the "political and economic dominance of the West"[285] and advocates for sustainability over extraction. Resource nationalists, drawing from Indonesia's history of colonial exploitation, demand absolute control of the country's resources and their development by the Indonesian state and people. Meanwhile, import interest groups have been running a profitable business, benefiting from growing energy needs and declining domestic oil and gas production. As a result, the rise of political Islam,

[284] Wenger Interviews, Jakarta 2023
[285] Uusmani and ʻUs̲mānī, *An Introduction to Islamic Finance,* 6.

resource nationalists, and import business elites has exerted significant political pressure on the Indonesian government to prioritize domestic and state-controlled exploration of natural resources, including oil and gas, and to drive out multinational corporations.[286]

In order to incentivize international oil corporations to return to Indonesia, the country would require a significant paradigm shift in its economic and legal regulatory environment, or the discovery of new resources. Over a decade after the Constitutional Court annulled the 2001 Oil and Gas Law, the Indonesian parliament has yet to pass a new law to replace it. Economically, the participation of IOCs would undoubtedly increase exploration efforts and production output in Indonesia's oil and gas sector, generating more revenue for the state and benefiting the social welfare of the Indonesian people through job creation. This would require relinquishing national control over oil and gas, a politically contentious decision. Despite technical improvements and numerous foreign contract acquisitions during the 2003 – 2012 resource boom, the state-owned enterprise PERTAMINA remains limited in its production capabilities due to high exploration risks and limited capital. According to an energy expert, PERTAMINA is directly subject to the budget of the Ministry of Energy and Mineral Resources, which limits their exploration efforts due to fiscal constraints, even if they were to build up technical expertise.[287] Nevertheless, Indonesia is currently the second-largest oil producer and contributes 20 percent to the total oil and gas production.[288] Thus, the dilemma for Indonesia remains the same: should it prioritize justice by securing control over economic production and distribution, or should it prioritize economic prosperity by allowing foreign entities to facilitate economic development?

[286] Wenger Interviews, Jakarta 2023
[287] Wenger Interviews, Jakarta 2023
[288] "Resource Nationalism in Post-Boom Indonesia."

## Our Resources: "No Strings Attached"

Indonesia has adopted a pragmatic approach that balances national interests and global integration, as well as capitalism and socialism, in the context of economic decolonization and globalization. Since Indonesia's independence, foreign direct investment and multinational corporations were simultaneously perceived as tools for growth and threats against national control and self-determination. This explains the ambiguous sentiments and policies towards foreign investments, as illustrated by the oil and gas sector.

Mohammad Sadli, a prominent Indonesian economist under Suharto, developed the concept of "Sadli's Law," which states that "good times lead to bad policy and bad times lead to good policy."[289] In the context of foreign investment in natural resources, Sadli's Law suggests that economic nationalism tends to increase during resource booms – 1970s and 2000s – when the government has abundant cash flow from export revenues and can pick and choose foreign investment contracts. Conversely, during economic downturns and crises such as the late 1950s and 1960s, after the 1998 Asian Financial Crisis, or during the Covid-19 pandemic, when Indonesia's economic growth was stagnant, the government seeks to attract foreign investors by offering more favorable conditions. These fluctuations in policy attitudes suggest that Indonesia's aspirations for independence and economic growth are intertwined with the state of the global economy, which is linked to investment inflows and commodity export outflows. I concur with Sadli that economic downturns and crises in Indonesia have historically led to more open markets and globally integrated policies, which have been favorable for foreign investment. Conversely, moments of economic upswings reflected more state-heavy and protectionist policies, which were less favorable for foreign investment. However, I refrain from categorizing what is "good or bad"

[289] "Resource Nationalism in Post-Boom Indonesia."

for Indonesia, as it depends solely on the country's decision to either maximize economic growth in the short term or economic sovereignty in the long term. Additionally, I support Eve Warburton's analysis that resource nationalism, state intervention, and protectionist policies have not diminished, despite the end of the second resource boom in 2012 and less favorable terms of trade. Thus, Sadli's law holds, with the exception of the resource sector post-2013.[290]

The development of democracy in post-authoritarian Indonesia demonstrated the enduring political and economic leverage of resource nationalism, even after the commodity boom mainly driven by emerging markets such as China and India ended in 2013. During this commodity boom, both state-owned enterprises and domestic businesses were able to increase their economic and influential positions over natural resource extraction by acquiring many of the contracts previously owned by foreigners. In Indonesia's political arena, which is characterized by few ideological differences, resource nationalism gained popular public support and is increasingly utilized by politicians to secure votes. As a result, resource nationalism, as an economic ideological tool, revived its ideological significance based on a history of foreign exploitation and gained economic significance through an expanding domestic business group with political influence in natural resources, making it resistant to macroeconomic dependencies on the global stage regarding commodity exports and capital inflow.

Indonesia has largely avoided the worst consequences of the resource curse, a paradoxical situation where countries with abundant natural resources tend to perform poorly economically. Despite experiencing various crises, Indonesia has managed to develop a robust and increasingly diverse domestic economy in recent decades. The country's dependence on natural resources, especially oil and gas, has significantly decreased (see Figure 6 and 7).

[290] "Resource Nationalism in Post-Boom Indonesia."

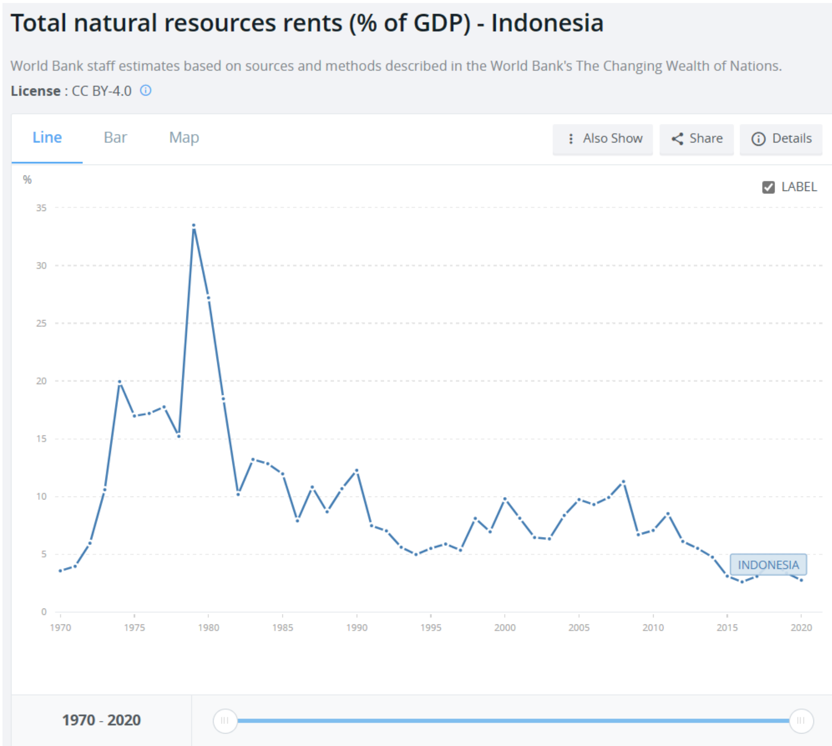


Figure 6: World Bank Data on Indonesia's total Natural Resource Rents (excess profits), 1970 – 2020[291]

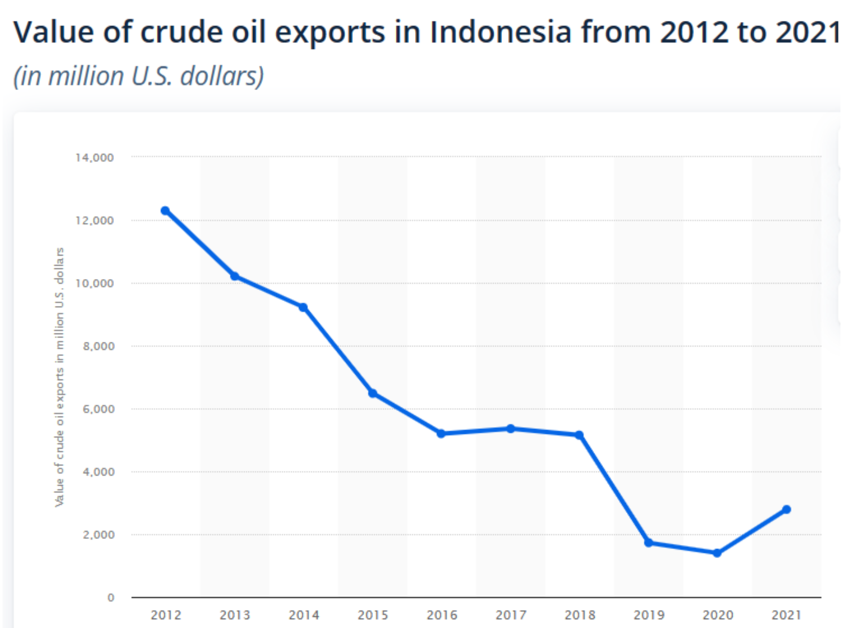


Figure 7: Statista Data on Indonesia's total Crude Oil export value, 2012 – 2021[292]

291 "World Bank Open Data."
292 "Indonesia."; Statistics Indonesia. "Value of crude oil exports in Indonesia from 2012 to 2021 (in million U.S. dollars)." Chart. February 25, 2022. Statista. Accessed May 09, 2023. https://www.statista.com/statistics/878701/crude-oil-exports-indonesia/

Moreover, Indonesia's economy, together with India's, is expected to be among the fastest growing in 2023, according to an article in *The Economist* on March 29 of that year. The article also stated that the "two countries are pioneering strategies for economic growth in a complex global context characterized by de-globalization, geopolitical tensions, automation, and energy transitions while seeking to balance electoral considerations and social stability."[293] Indonesia's recent hosting of the G-20 summit in Bali and its perceived leadership role underscore these developments. Consequently, the directions and outcomes of Indonesia's economic policies will significantly affect other resource-rich countries that face similar challenges, such as those with colonial legacies, recent independence, and non-alignment. Despite the country's overall openness to globalization, close to 75 percent Indonesians believe that economic self-sufficiency is essential, as revealed in a survey cited by *The Economist*.[294] This reflects the ambiguity and contradictions of President Jokowi's economic policies, which mirror a desire for economic growth, independence, and especially control over national resources. Over the past two decades, it has become evident that Indonesia is placing greater emphasis on asserting its authority over its natural resources through national regulations and governance.

## Natural Resources and the Energy Transition

Our Resources. Our Rules. This study examined the oil and gas sector as a case study to demonstrate how post-colonial Indonesia has balanced its reliance and independence on foreign investment in the natural resource industry. In Indonesia's modern history, foreign direct investment and multinational corporations have been attracted to Indonesia to facilitate economic

[293] "Which Will Grow Faster."
[294] "Resource Nationalism in Post-Boom Indonesia."; "League of Nationalists."

development and growth. In the production-sharing regulatory regime of the oil and gas sector, multinational corporations were able to assume the capital expenditure and exploration risk for the Indonesian government while providing technical and operational expertise and generating revenue. Consequently, foreign direct investment was historically welcomed in the technical upstream sector (exploration), but not as much in the more labor-intensive downstream sector (transport and refineries), which aimed to create more jobs for Indonesians. However, the resource nationalist ideology, supported by the Indonesian government, seeks to drive out foreigners from the upstream sector and end the practice of exploration and export exploitation despite high government revenues, hoping to push foreign investments downstream and increase value creation and employment opportunities for Indonesians.

A similar trend can be observed in other natural resource industries in Indonesia. In mining, the country's forceful industrial downstream policy focuses on implementing punitive measures rather than incentives to compel multinational corporations to construct refineries within the nation by prohibiting exports of specific raw materials like nickel. Therefore, the Indonesian government aims to exploit its resource wealth to attract a portion of the value creation chain to Indonesia through inward-looking policies. Balancing resource management and the appropriate utilization of foreign investment in Indonesia will remain relevant in the future, particularly in the context of the sustainable energy transition. According to an international consultant, the Indonesian government is keen on attracting foreign investment in renewables, establishing favorable deals for collaboration. Nevertheless, he also noted that political tension is already brewing in Indonesia regarding the nationalization of water, sun, and wind based on the principles of Article 33(3).[295]

[295] Wenger Interviews, Jakarta 2023

This suggests that the challenge of reliance and independence on foreign investment will persist in Indonesia’s natural resource sector.

The actions taken by the Indonesian government to exert control over its natural resources are legally justified under Article 33(3) of the country’s constitution, which mandates state control of these resources for the benefit of the people. However, the application of regulatory regimes toward foreign investment and multinational corporations based on this article is not consistently applied. A constitutional lawyer and foreign counselor pointed out that the term “control” in Article 33 is subject to varying interpretations. For instance, while Article 33(2) asserts government control over manufacturing, foreign presence in this sector has not been raised in the Constitutional Court. In the natural resource sector, resource nationalists have successfully advocated for state ownership of these resources based on an interpretation that only the state and state-owned enterprises can control their development.[296] These inconsistencies in the interpretation of the term “control” in different sectors of the economy have implications for how Indonesia’s natural resources will be managed in the future, particularly with the country’s shift towards sustainable energy and renewable sources.

From a geopolitical perspective, a crucial question revolves around Indonesia's degree of leverage and its influence over its foreign investment counterparts, given its abundant resources. The Indonesian government strives to strike a delicate balance between maintaining its independence and fostering economic growth, and it is anticipated to continue adopting a pragmatic and somewhat unpredictable approach in its actions (see Figure 2). One valuable lesson learned from the oil and gas sector, particularly the departure of IOCs, is that the Indonesian government cannot unilaterally implement resource-nationalist policies or dismantle regulatory

[296] Wenger Interviews, Jakarta 2023

frameworks without facing repercussions. The interconnectedness of the world, driven in part by multinational corporations, empowers these entities to exert political pressure and encourage regulatory convergence on their terms. Nevertheless, the Indonesian government remains determined to harness its natural resources and maximize value creation within the country, ultimately benefiting the Indonesian people. Thus, the spirit of economic decolonization persists as Indonesia endeavors to forge a third path in an era where the tides of globalization are receding. Indonesia's ongoing balancing act is characterized by its adoption of a new developmental model that prioritizes economic sovereignty and growth. The constitution upholds the socialist principles rooted in Indonesia's independent origins, while an active state guides the economy toward rapid growth. Simultaneously, the private sector, particularly in manufacturing and downstream value chain activities, is gaining significance, and there has been a recent focus on sustainable industrialization. The foreign direct investment climate has generally improved, except in the natural resource sectors.

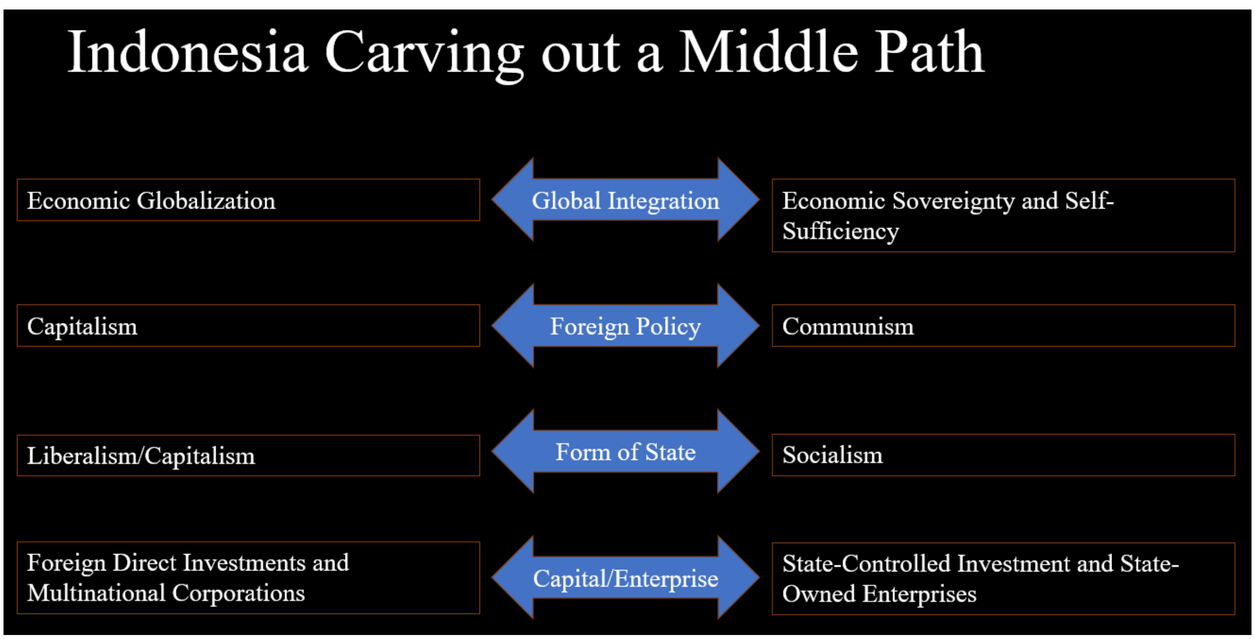


Figure 2: Indonesia Carving out a Middle Path: A visual illustration of the framework in which Indonesian leaders made decisions about foreign direct investment and private enterprises – own representation.

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