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FM AMCONSUL MEDAN
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INFO AMEMBASSY JAKARTA
AMEMBASSY KUALA LUMPUR
AMEMBASSY SINGAPORE
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CONFIDENTIAL SECTION 01 OF 06 MEDAN 00228

12356: DECL: OADR
TAGS: PGOV, PINS, ECON, ETRD, EINV, KPRP, ID

SUBJECT: SUMATRA'S TRADE AND INVESTMENT: JAKARTA INCORPORATES
THE WORLD'S SIXTH LARGEST ISLAND

REFS: 89 MEDAN 00153, B) 89 MEDAN 110

1. (C) SUMMARY AND INTRODUCTION: DURING THE SOEHARTO ERA,
SUMATRA'S TRADITIONAL TRADE AND INVESTMENT PATTERNS HAVE BEEN
REORIENTED TO FIRMLY INTEGRATE THIS NATURALLY WEALTHY ISLAND
INTO INDONESIA'S ECONOMIC WEB. THE INSTRUMENTS FOR THE GRADUAL
ACCRETION OF JAKARTA'S DOMINANT ECONOMIC INFLUENCE HAVE BEEN
INDONESIA'S NATIONAL (AND SEVERAL FOREIGN) PETROLEUM AND
MINERALS COMPANIES, AND, MORE RECENTLY, JAKARTA-BASED ETHNIC
CHINESE CONGLomerates. MINERAL WEALTH, WHICH UNTIL 1987
PROVIDED OVER HALF THE VALUE OF INDONESIA'S EXPORTS, IS
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NATIONALLY OWNED. THUS, JAKARTA DECIDES HOW TO EXPLOIT
SUMATRAN OIL, NATURAL GAS, TIN, AND COAL, AND REAPS THE
PROFITS. HOWEVER, THE PALM OIL, RUBBER, AND OTHER
AGRICULTURAL PRODUCTS THAT FILL THE WORLD'S SECOND MOST
PRODUCTIVE PLANTATION BELT ARE NOW OFTEN OWNED BY EITHER STATE COMPANIES OR ETHNIC CHINESE, WHO NOW TEND TO REPATRIATE PROFITS NOT TO SINGAPORE BUT TO JAKARTA. FINALLY, INDUSTRIES WHICH PROCESS NATURAL PRODUCTS, BOTH IN CITIES AND IN ISOLATED ENCLAVES, ARE ALSO USUALLY OWNED BY THE CENTRAL GOVERNMENT OR BY JAKARTA-BASED CHINESE WITH TIES TO INDONESIA'S FIRST FAMILY. THUS HAND IN HAND WITH INCREASED DEVELOPMENT OF SUMATRA'S RESOURCES HAS COME INCREASED CENTRAL CONTROL OF THE ECONOMIC DECISIONS THAT AFFECT THE LIVES OF THE FORTY MILLION INDONESIANS LIVING ON SUMATRA.

2. (C) FROM A NATIONAL POINT OF VIEW, JAKARTA HAS BEEN SUCCESSFUL IN INTEGRATING SUMATRA AND ESTABLISHING A NATIONAL DIVISION OF LABOR, CONCENTRATING INDUSTRY ON JAVA AND TRANSFERRING EXCESS LABOR TO SUMATRA TO HELP THAT ISLAND SERVE AS THE CENTER FOR INDONESIA'S TROPICAL AGRICULTURAL PRODUCTION. FROM A REGIONAL PERSPECTIVE THE OUTCOME IS LESS APPEALING. IN TWENTY FIVE YEARS, SUMATRANS HAVE SEEN THEIR ECONOMIC LOT IMPROVE MARKEDLY. HOWEVER, THEY HAVE ALSO SEEN SUMATRAN PER CAPITA INCOME, GENERALLY ESTIMATED AT 20 PERCENT ABOVE THAT OF THE JAVANESE IN THE MID-1960S, SLIP SLIGHTLY BELOW THE JAVANESE (INCLUDING JAKARTA) AVERAGE. MOREOVER, IF PRESENT TRENDS CONTINUE, INDONESIANS LIVING ON SUMATRA MAY BE CAUGHT IN A TIME WARP - A PLANTATION ECONOMY RESEMBLING MALAYSIA'S OF THE 1960S - BUT, UNLIKE MALAYSIA'S, ONE WITHOUT THE AUTONOMOUS DECISION-MAKING OR THE INVESTMENT CAPITAL NECESSARY TO ENSURE PARTICIPATION IN INDONESIA'S RAPID INDUSTRIALIZATION. END SUMMARY.

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HISTORY

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3. (U) FOR HUNDRED OF YEARS, SUMATRA WAS ORIENTED CULTURALLY, ECONOMICALLY, AND POLITICALLY TO THE STRAIT OF MALACCA AND THE MALAY PENINSULA, NOT TO JAVA. GOLD AND OTHER PRECIOUS MINERALS FLOWED DOWN FROM THE MOUNTAINS TO THE VARIOUS TRADING KINGDOMS, BASED ALTERNATIVELY IN SUMATRA OR THE MALAY PENINSULA, WHICH CULTIVATED PEPPER AND OTHER PRECIOUS SPICES AND RAISED AND TRADED THROUGHOUT THE CRUCIAL STRAIT LINKING CHINA TO INDIA. GREAT STATES SOMETIMES AROSE, INCLUDING THE SRIVIJAYA EMPIRE (AD 600 -1300), MALACCA, AND ACEH. THIS WORLD BEGAN TO CHANGE WHEN THE DUTCH BECAME THE DOMINANT COLONIAL POWER IN THE REGION, BUT IT IS IMPORTANT TO REMEMBER THAT THE DUTCH ONLY STARTED TO ASSERT CONTROL IN VARIOUS PARTS OF
SUMATRA IN THE 1850S AND THAT DUTCH CONTROL WAS NOT FIRMLY
ESTABLISHED THROUGHOUT THE ISLAND UNTIL 1908, AFTER THIRTY YEARS
OF THE MOST COSTLY WAR IN DUTCH COLONIAL HISTORY. ONLY THIRTY
ODD YEARS LATER, IN WORLD WAR II, THE JAPANESE ARMY SEPARATED
SUMATRA FROM JAVA, UNITING IT INSTEAD WITH MALAYA AND
SINGAPORE. AFTER FIGHTING FOR INDEPENDENCE, SUMATRANS TOO
CONSIDERED THEMSELVES INDONESIANS, BUT MANY OF SUMATRA'S ETHNIC
GROUPS STAGED SHORT REVOLTS AGAINST JAKARTA IN THE MID-1950S.
MORE IMPORTANT FOR OUR STORY, THROUGHOUT THE WAR FOR
INDEPENDENCE SUMATRANS SMUGGLED PLANTATION PRODUCTS TO MALAYA
AND SINGAPORE IN EXCHANGE FOR WEAPONS AND CONSUMER GOODS
DURING THE SUBSEQUENT RULE OF PRESIDENT SUKARNO, WHEN REGIONAL
POLITICAL LEADERS AND ARMY COMMANDS ATTEMPTED TO AMELIORATE THE
CONSEQUENCES OF SUKARNO'S DISASTROUS ECONOMIC POLICIES,
SUMATRANS STRUGGLED TO MAINTAIN THEIR TRADITIONAL TRADING LINKS
WITH MALAYA AND SINGAPORE. ONLY UNDER THE SOEHARTO GOVERNMENT
HAS JAKARTA GRADUALLY IMPOSED ITS CONTROL OVER THE SUMATRAN
ECONOMY AND SLOWLY REORIENTED THE GROWING STREAM OF
SUMATRAN-PRODUCED WEALTH TO THE CENTER.

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E.O. 12356: DECL: OADR
TAGS: PGOV, PINS, ECON, ETRD, EINV, KPRP, ID
SUBJECT: SUMATRA'S TRADE AND INVESTMENT: JAKARTA INCORPORATES

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4. (U) SUMATRA STRETCHES 1100 MILES FROM SABANG TO THE TIP OF LAMPUNG ACROSS FROM JAVA. ALONG THE WEST COAST RUNS A MAJOR MOUNTAIN RANGE, THE BUKIT BARIAN, THE HOME OF THE BATAK AND MANDAILING ETHNIC GROUPS. THESE MOUNTAINS PRODUCE LITTLE OF ECONOMIC VALUE EXCEPT FOOD. INSTEAD, SUMATRA'S NATURAL WEALTH IS FOUND IN THE COASTAL PLAIN, OFTEN MORE THAN 150 MILES WIDE, THAT RUNS DOWN THE ENTIRE EAST COAST ALONG THE STRAIT OF MALACCA AND THEN PAST SINGAPORE FOR ANOTHER FIVE HUNDRED MILES TO JAVA. IN THE NORTH, IN ACEH, LIES SOUTHEAST ASIA'S LARGEST NATURAL GAS FIELD AND LIQUEFIED NATURAL GAS PLANT; IN NORTH CONFIDENTIAL

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SUMATRA, WITH ITS CAPITAL AT MEDAN AND PORT AT BELAWAN, MORE OF INDONESIA'S PALM OIL AND NATURAL RUBBER IS PRODUCED THAN ANYWHERE ELSE, AS WELL AS COFFEE AND TOBACCO; RIAU PRODUCES HALF OF INDONESIA'S OIL, SOME NATURAL GAS (AND WILL PRODUCE MUCH MORE WHEN THE NATUNA FIELDS COME ON LINE), AND IS RAPIDLY EXPANDING TO OVERTAKE NORTH SUMATRA IN PALM OIL AND PERHAPS RUBBER, WHILE USING UP ITS TIMBER RESOURCES; LITTLE JAMBI'S FORESTS WILL ALSO BE CLEARED FOR PLANTATIONS; SOUTHERN SUMATRA'S OIL, TIN, COAL, RUBBER, PALM OIL, AND FOOD FLOWS DIRECTLY TO NEIGHBORING JAVA. OVERALL, SUMATRA PRODUCES BETWEEN 80 AND 90 PERCENT OF INDONESIA'S TOTAL EXPORTS OF COFFEE, RUBBER, AND PALM OIL, AND A SIZEABLE PORTION OF ITS PLYWOOD EXPORTS.

5. (C) SUMATRA'S PLANTATIONS ARE MANNED BY JAVANESE MIGRANTS, BROUGHT EITHER AS COOLIES BY THE DUTCH OR LATER SENT BY JAKARTA AS "TRANSMIGRANTS," AND THEIR DESCENDANTS, WHO NOW CONSTITUTE PERHAPS TEN MILLION PEOPLE. THE SOPHISTICATED EXTRACTION OF SUMATRA'S PETROLEUM AND OTHER MINERAL WEALTH IS LARGELY CARRIED OUT BY "OUTSIDERS" LIVING AND WORKING IN ENCLAVES. SUMATRA'S ETHNIC CHINESE CONTINUE AS SUCCESSFUL BUSINESSMEN, BUT HAVE OFTEN BEEN RELEGED TO THE ROLE OF MIDDLEMEN FOR THE LARGE CHINESE JAKARTA-BASED CONGLOMERATES HUDDLED AROUND PRESIDENT SOEHARTO AND HIS FAMILY.

6. (U) STATISTICS ON INTER-REGIONAL TRADE AND INVESTMENT IN INDONESIA ARE NOT AVAILABLE. THUS, MUCH OF THE INFORMATION BELOW IS NECESSARILY IMPRECISE AND ANECDOAL.

ECONOMIC RESOURCES: MINERALS
7. (C) OIL AND NATURAL GAS ABOUT 60 TO 70 PERCENT OF
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INDONESIA'S CRUDE OIL, CONDENSATE AND NATURAL GAS, WHICH IN FY
L989/90 CONTRIBUTED NEARLY USD 6 BILLION TO INDONESIAN
GOVERNMENT COFFERS, IS PRODUCED IN SUMATRA. WHEN SOUTHEAST
ASIA'S LARGEST GAS FIELD, ESSO'S 45 TSCF NATUNA FIELD COMES ON
LINE IN THE LATE 1990S, THE PERCENTAGE OF INDONESIA'S OIL AND
GAS PRODUCED IN SUMATRA MAY INCREASE. ALL PROFITS GO DIRECTLY
TO JAKARTA. FROM SUMATRAN OIL AND GAS, INDONESIA'S TREASURY
RECEIVED, IN 1989/90, BETWEEN USD 3.6 AND 4.2 BILLION.
SUMATRANS VIEW WITH ENVY THE MALAYSIAN SYSTEM, WHERE INDIVIDUAL
STATES RETAIN 5 PERCENT OF THE EARNINGS FROM OIL/GAS PRODUCED
WITHIN THEIR BOUNDARIES. MORE SENSITIVE ISSUES ARE LIMITED
EMPLOYMENT OPPORTUNITIES FOR ETHNIC ACEHNESE AND MALAYS IN THE
EXTRACTION OF LOCAL PETROLEUM AND GAS RESOURCES AND THE LIMITED
DOWN-STREAM IMPACT OF EX extractive INDUSTRIES, EXCEPT WHERE
RESERVES OF NATURAL GAS ARE UTILIZED AS THE BASIC FEEDSTOCK FOR
THE PRODUCTION OF FERTILIZER IN LARGE COMPLEXES. MAJOR
FERTILIZER PLANTS ARE LOCATED IN LHOKSEUMAWE, ACEH (P.T. ASEAN
AND P.T. ISKANDAR MUDA) AND IN PALEMBANG, SOUTH SUMATRA
(PUSRI). PUSRI, INDONESIA'S LARGEST FERTILIZER PLANT, EXPORTS
70 PERCENT OF ITS PRODUCT TO JAVA. P.T. ASEAN IS DESIGNED TO
EXPORT ABROAD.

8. (U) NON-OIL/GAS MINERALS: INDONESIA'S NON OIL/GAS MINERALS
ARE ESTIMATED TO COMprise ONLY 1.2 PERCENT OF INDONESIA'S GDP.
OF INDONESIA'S TIN, CONCENTRATED ON THE ISLANDS OF BANGKA AND
BILITONG OFF THE COAST OF SOUTH SUMATRA, EIGHTY PERCENT IS
PRODUCED BY THE GOVERNMENT-OWNED P.T. TIMBANG TIMAH. FOR THIS
OVERSTAFFED COMPANY, PROFITS HAVE VARIED ACCORDING TO THE
INTERNATIONAL PRICE OF TIN, WHICH HAS NOT BEEN HIGH SINCE THE
EARLY 1980S. TWO-THIRDS OF THE TIN (SMELTED IN SUMATRA) IS
STILL DESTINED FOR THE SINGAPORE MARKET, THOUGH MUCH OF THIS
TIN IS PROBABLY REEXPORTED. TOTAL TIN EXPORTS IN 1989 WERE
VALUED AT USD 214 MILLION.

9. (U) THOUGH NEW MINES IN KALIMANTAN MAY SOON OUTPRODUCE
SUMATRA'S, INDONESIA'S CURRENT COAL PRODUCTION IS CONCENTRATED
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AT BUKIT ASAM IN SOUTH SUMATRA. A SMALL PERCENT IS USED FOR
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REFS: A) 89 MEDAN 00153, B) 89 MEDAN 00110

LOCAL POWER GENERATION; BUKIT ASAM SENT 3.4 MILLION TONS IN
1989 AND PLANS TO SEND 5 MILLION TONS IN 1990, OF UNDETERMINED
VALUE, DOWN THE NEWLY REFURBISHED RAILWAY TO THE TIP OF LAMPUNG
AND THEN ON TO THE SURALAYA POWER PLANT ON THE WESTERN TIP OF
JAVA. THERE IT IS USED TO PRODUCE ELECTRIC POWER FOR JAKARTA'S
OFFICES, INDUSTRIES, AND HOMES.

ECONOMIC RESOURCES: PLANTATION PRODUCTS

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10 (U) CONSULATE MEDAN ESTIMATES THAT IN 1987, RUBBER AND
PALM OIL ALONE ACCOUNTED FOR ONE QUARTER OF INDONESIA'S USD 6.3
BILLION IN TOTAL NON-OIL EXPORTS. IN 1989, WITH THE GROWTH OF
NON-OIL/GAS EXPORTS TO USD 13.47 BILLION AND, DESPITE GROWING
SUPPLY, DECLINING RUBBER AND PALM OIL PRICES, THE SHARE OF
THESE TREE CROPS MAY HAVE FALLEN TO 10-15 PERCENT. IN 1989,
INDONESIA PRODUCED 1.263 MILLION METRIC TONS OF RUBBER, UP SLIGHTLY FROM 1988, BUT STILL SOME 200,000 METRIC TONS BEHIND MALAYSIA. SUMATRA PRODUCED WELL ABOVE ONE MILLION TONS THAT YEAR. ACCORDING TO THE ASIAN WALL STREET JOURNAL, INDONESIA ONLY PRODUCES TWO MILLION METRIC TONS OF PALM OIL (IN 1988 SUMATRA EXPORTED OVER 85 PERCENT OF INDONESIA'S CRUDE PALM OIL EXPORTS), BUT THE GOI HOPES, WHEN ALREADY PLANTED CROPS BEGIN TO PRODUCE, TO REACH FOUR MILLION METRIC TONS BY 1994 (MALAYSIA PRODUCES FIVE MILLION METRIC TONS).

11. (C) RELIABLE INFORMATION IS MEAGER ON TOTAL LAND ACREAGE DEVOTED TO RUBBER AND PALM OIL IN SUMATRA, OR ON HOW IT IS DIVIDED BETWEEN FOREIGN COMPANIES, GOVERNMENT PTP'S, PRIVATE INDONESIAN INVESTORS, AND SMALLHOLDERS. THE SCANT GOI STATISTICS AVAILABLE INDICATE THAT SMALLHOLDERS PREDOMINATE IN SOUTHERN SUMATRA, WHILE IN NORTH SUMATRA ACREAGE IS DIVIDED BETWEEN SMALLHOLDERS AND GOVERNMENT PTP'S; THE COMMON PERCEPTION IS THAT PRIVATE, JAKARTA-BASED ETHNIC-CHINESE CONTROL THREE QUARTERS OF THE PLANTATION LAND IN RIAU. HOWEVER, IT HAS PROVED PARTICULARLY DIFFICULT TO PENETRATE THE MURKY FINANCIAL WORLD OF PLANTATIONS AND ASSESS HOW MUCH THEY CONTRIBUTE TO BOTH THE CENTRAL GOVERNMENT AND PRIVATE JAKARTA-BASED COFFERS. CONVENTIONAL WISDOM IN SUMATRA HOLDS THAT THE SEMI-AUTONOMOUS STATE-OWNED PLANTATIONS PROVIDE FEW "PROFITS" TO JAKARTA. PLANTATIONS OWNED BY JAKARTA-BASED CONGLOMERATES, HOWEVER, ARE REPUTED TO CONTRIBUTE HANDSOMELY TO THEIR OWNERS' BALANCE SHEETS.

12. (U) SUMATRA ALSO PRODUCES A SUBSTANTIAL SHARE OF INDONESIA'S COFFEE, COCOA, AND TOBACCO. COFFEE EXPORTS FOR JAN-SEPT 1989 TOTALLED USD 409 MILLION, WHICH, ANNUALIZED, WOULD AMOUNT TO ABOUT USD 530 MILLION. IN 1988, SUMATRA ACCOUNTED FOR ABOUT 80 PERCENT OF INDONESIA'S COFFEE EXPORTS.

ECONOMIC RESOURCES: OTHER

13. (C) FOREST PRODUCTS: WITH THE EXPLOITATION OF THE FORESTS OF ACEH, RIAU, JAMBI, AND SOUTH SUMATRA, SUMATRA MAY PRODUCE ABOUT 40 PERCENT OF INDONESIA'S WOOD PRODUCTS. MAJOR PULP AND PAPER FACTORIES ARE THE P.T. KRAFT FACTORY (REPUTED EXTENSIVE FIRST FAMILY INVOLVEMENT) AT LHOKESEUMAWE, ACEH, P.T. INDORAYON (RAJA GARUDA MAS GROUP, ALSO REPUTED EXTENSIVE FIRST FAMILY INVOLVEMENT) IN NORTH SUMATRA, AND, IN RIAU, THE INDAH
KIAT FACTORY (TWO-THIRDS OWNED BY LIEM'S SINAR MAS), AS WELL AS A PLANNED USD 1.5 BILLION PULP AND PAPER FACTORY (RAJA GARUDA MAS) ON THE ROKAN RIVER. IN ADDITION THERE ARE INNUMERABLE PLYWOOD FACTORIES AND A SMALL RATTAN INDUSTRY. IN 1988, SUMATRA PRODUCED ABOUT ONE QUARTER OF INDONESIA'S TOTAL PLYWOOD EXPORTS.

WAYS AND MEANS
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14. (C) THE CENTRAL GOVERNMENT: INDONESIA'S CENTRAL GOVERNMENT COLLECTS OVER USD FOUR BILLION IN NET REVENUES FROM THE EXPLOITATION OF SUMATRA'S MINERAL WEALTH, PRINCIPALLY FROM OIL AND GAS. EXCEEDINGLY COMPLICATED WOULD BE ATTEMPTS TO CALCULATE NET CENTRAL GOVERNMENT REVENUES FROM SUMATRAN TREE CROP, AGRICULTURAL, AND TIMBER RESOURCES, AS WELL AS FROM CENTRAL GOVERNMENT INVESTMENTS IN SUCH INDUSTRIES AS FERTILIZER AND PULP AND PAPER PLANTS. ONE OF THE REASONS THAT CALCULATIONS OF NET PROFITS FROM GOVERNMENT INDUSTRIAL INVESTMENTS ARE SO DIFFICULT IS THAT BASIC INPUTS, SUCH AS CONFIDENTIAL
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NATURAL GAS AND FINANCIAL RESOURCES, ARE INVARIENTLY
SUBSIDIZED. OUR IMPRESSION FROM A VARIETY OF LOCAL PLANTATION
MANAGERS IS THAT THE SEMI-AUTONOMOUS STATE-OWNED PLANTATIONS
(PERSEROAN TERBATAS PERKEBUNAN OR PTP), WITH NET ASSETS OF USD
2 BILLION, CONTRIBUTE ONLY A SMALL SHARE OF THEIR POTENTIAL
PROFITS TO THE MINISTRY OF FINANCE. THIS IS PRIMARILY A RESULT
OF "SLIPPAGE", OR CORRUPTION, WHICH ENSURES THAT THESE
PLANTATIONS SELDOM HAVE SUBSTANTIAL BOOK PROFITS TO BE DIVIDED
WITH THE FINANCE MINISTRY OR TO BE PAID IN TAXES.

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15. (C) IN RETURN, THE CENTRAL GOVERNMENT TRANSFERS OPERATING
AND DEVELOPMENT FUNDS TO GOVERNMENT OFFICES IN THE PROVINCES.
HOWEVER, WHILE STATISTICS ARE UNAVAILABLE ON HOW CENTRAL
GOVERNMENT TAX REVENUES ARE BROKEN DOWN BY REGION, WE NOTE THAT
A CRUDE COMPILATION OF CENTRAL GOVERNMENT DEVELOPMENT FUNDS
ALLOCATED TO SUMATRAN PROVINCES SHOWED THAT IN NO CASE DID THEY
EXCEED THE NATIONAL PER CAPITA AVERAGE. WE THEREFORE ASSUME, SINCE
SUMATRA'S PER CAPITA INCOME IS ONLY SLIGHTLY BELOW THE AVERAGE
FOR JAVA, THAT INDONESIANS IN SUMATRA (EXCLUDING REVENUES FROM
THE EXPLOITATION OF MINERAL RESOURCES AND FROM
CENTRALLY-DIRECTED GOVERNMENT INVESTMENTS) CONTRIBUTE ABOUT THE
SAME AMOUNT IN TAXES AS THEY RECEIVE BACK IN GOVERNMENT
SERVICES.

16. (C) SIGNIFICANT FOR THE FUTURE WILL BE CURRENT
INVESTMENT. THE CENTRAL GOVERNMENT CONTROLS APPLICATIONS FOR
INVESTMENT LICENSES. WE CAN'T DEMONSTRATE THAT MINISTRIES IN
JAKARTA GUIDE INVESTORS, PARTICULARLY IN LABOR INTENSIVE
INDUSTRIES, TO LOCATE THEIR CAPITAL AND PLANT IN JAVA. IN
FACT, THERE IS REPORTEDLY GROWING INTEREST IN JAKARTA IN
INCREASING THE GEOGRAPHIC SPREAD OF INVESTMENT. ON THE OTHER
HAND, SUMATRA BUSINESS AND GOVERNMENT LEADERS BELIEVE THAT
CENTRAL GOVERNMENT MINISTRIES ENCOURAGE INVESTMENT IN AND
AROUND JAKARTA. WHATEVER THE REAL SITUATION, THE STATISTICS
COMPARING INVESTMENT IN JAVA AND SUMATRA ARE IMPRESSIVE.
DOMESTIC NON-OIL/GAS INVESTMENT FOR THE FIRST HALF OF THIS
INDONESIAN FISCAL YEAR (IN BILLIONS OF RUPIAH) WAS JAVA 11,171,
SUMATRA 1,883. FOREIGN INVESTMENT (IN MILLIONS OF USD) DURING
THE SAME TIME FRAME WAS EVEN MORE DRAMATIC, JAVA 2,334, SUMATRA
118.

17. (C) OVER TIME PERHAPS MORE IMPORTANT THAN PARTICULAR
THE ECONOMIC DECISION-MAKING PROCESS. THE EMBASSY INTENDS TO ADDRESS PRECISELY THIS QUESTION IN A REPORT ON "DECENTRALIZATION," BUT IN SUMMARY WE SHOULD NOTE THAT THE FLOW OF BUREAUCRATIC DECISIONS IN INDONESIA IS INEVITABLY DOWNHILL, NOT ONLY THROUGH THE REPRESENTATIVES OF EACH MINISTRY BUT THROUGH GOVERNMENT CONTROLLED COMPANIES. REPRESENTATIVE OFFICES OF EACH CENTRAL GOVERNMENT MINISTRY, IN CHARGE OF OVER EIGHTY PERCENT OF THE FUNDS THAT ARE USED FOR "DEVELOPMENT" IN THE INDIVIDUAL PROVINCES, ARE RESPONSIBLE TO THEIR PARENT MINISTRIES IN JAKARTA. IN ADDITION, CENTRAL GOVERNMENT COMPANIES (PERTAMINA, PERUMTEL, PTPS, FERTILIZER COMPANIES, AND SO FORTH) DOMINATE SUMATRA'S ECONOMY. HEADQUARTERED IN JAKARTA AND OFTEN CONFINED TO SMALL ENCLAVES IN THE PROVINCES WHERE THEY EXPLOIT NATURAL RESOURCES, THEY TOO REACH DECISIONS IN JAKARTA WITHOUT MUCH KNOWLEDGE OF OR REGARD FOR THEIR ROLE IN THE PROVINCES.

18. (C) THE ROLE OF THE ETHNIC CHINESE: THE SECOND LEG IN ENHANCING JAKARTA'S CONTROL OF SUMATRA'S ECONOMY HAS BEEN THE GROWING INFLUENCE OF JAKARTA-BASED ETHNIC CHINESE "CONGLOMERATES" ON "PRIVATE" BUSINESS IN SUMATRA. SUMATRA'S ETHNIC CHINESE, KNOWN AS TOTOKS ("PURE BLOOD"), HAVE RETAINED THEIR CULTURE AND REMAIN A COMMUNITY APART FROM OTHER INDONESIANS. UNLIKE CHINESE IN JAVA BUT SIMILAR TO THEIR COUSINS ACROSS THE STRAIT, THEY ARE RELATIVELY RECENT MIGRANTS TO SOUTHEAST ASIA. THIS ISLAND'S ESTIMATED 1.2 TO 1.5 MILLION ETHNIC CHINESE (INDONESIA PUBLISHES NO ETHNIC BREAKDOWN ON ITS POPULATION) HAVE TRADITIONALLY VIEWED SINGAPORE AS THEIR CULTURAL AND ECONOMIC CENTER. FROM 1965-85, SUMATRAN-BASED ETHNIC CHINESE APPEAR TO HAVE BEEN THE REGION'S MAIN BENEFICIARIES OF SUMATRA'S ECONOMIC RECOVERY AND GROWTH BECAUSE THEY HAD ALREADY ESTABLISHED POWERFUL BUSINESS STRUCTURES DRAWING ON SINGAPORE CAPITAL. SINCE STATE CORPORATIONS CONTROLLED KEY SECTORS OF SUMATRA'S ECONOMY, THE LOCAL CHINESE ENTERED INTO JOINT VENTURES WITH OR SUPPLIED THESE STATE COMPANIES. SUMATRAN CHINESE, DOMINANT IN THE CONSTRUCTION AND

REAL ESTATE INDUSTRIES, ALSO OWNED AND MANAGED MOST OF

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AMEMBASSY SINGAPORE
AMCONSUL SURABAYA

CONFIDENTIAL SECTION 05 OF 06 MEDAN 00228

E.O. 12356: DECL: OADR
TAGS: PGOV, PINS, ECON, ETRD, EINV, KPRP, ID
SUBJECT: SUMATRA'S TRADE AND INVESTMENT: JAKARTA INCORPORATES THE WORLD'S SIXTH LARGEST ISLAND

REFS: A) 89 MEDAN 00153, B) 89 MEDAN 00110

SUMATRA'S PALM OIL REFINING, CRUMB RUBBER PROCESSING, AND PLYWOOD FACTORIES.

19. (C) IN THE MID 1980S, HOWEVER, THE SOURCE OF ETHNIC-CHINESE CAPITAL SHIFTED FROM SINGAPORE TO JAKARTA. JAKARTA-BASED ETHNIC-CHINESE OWNED BUSINESSES, PARTICULARLY THOSE WITH STRONG TIES WITH THE FIRST FAMILY, BEGAN TO INVEST HEAVILY IN SUMATRA. SUMATRAN-BASED CHINESE BUSINESSMEN OFTEN PAINT A PICTURE OF RAPACIOUS "CONglomerATES" SWALLOWING-UP LOCAL BUSINESS. OTHER INTERLOCUTORS NOTE THAT JAKARTA CONFIDENTIAL

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BUSINESSMEN ESTABLISHED JOINT VENTURES WITH LOCALS, AND, OF EQUAL SIGNIFICANCE, THAT SUMATRAN-BASED BUSINESSES HAVE GONE NATIONAL, COVERING THEIR RISKS BY ALSO INVESTING IN JAKARTA. TRACING THE FLOW OF ETHNIC CHINESE CAPITAL IN INDONESIA IS, OF COURSE, ALL BUT IMPOSSIBLE, BUT NO MATTER HOW IT HAPPENED, CONTROL OF THIS CAPITAL SEEMS TO BE INCREASINGLY LOCATED IN JAKARTA.
20. (C) ACCORDING TO CONSULATE MEDAN REPORTING, BY 1984 THE TAKEOVER OF LOCAL CHINESE BUSINESS BY LIEM SIOE LIONG IN VITAL AREAS SUCH AS IMPORTING AND PALM OIL HAD "CAST A SHADOW" OVER THE ENTIRE NORTH SUMATRAN ECONOMY. AT THAT TIME, MEDAN'S BANKERS CLAIMED THAT LIEM WAS ATTEMPTING TO CONTROL ALL IMPORTS THROUGH THE PORT OF BELAWAN, FORCING LOCAL CUSTOMERS TO THE WALL. AWARDED CONTROL OF PALM OIL MARKETING, HE PROCEEDED TO "SWALLOW UP" PALM OIL PROCESSING PLANTS AND 50 PERCENT OF EK CHONG'S SINAR MAS COOKING OIL EMPIRE. (IN 1989 THE ASIAN WALL STREET JOURNAL ESTIMATED THAT LIEM CONTROLLED 65 PERCENT OF INDONESIA'S DOMESTIC COOKING OIL MARKET AND 40 PERCENT OF NATIONAL LICENSED REFINING CAPACITY). THE EMBASSY POINTS OUT, HOWEVER, THAT A JOINT VENTURE CALLED SINAR MAS INTIPERKASA IS 45 PERCENT OWNED BY LIEM, 45 PERCENT SINAR MAS (IE. EK CHONG AKA EKA TJIIPTA WIDJAYA), AND 10 PERCENT ONE OF THE PRESIDENT'S SONS. WHATEVER THE CASE, ALL PARTNERS ARE NOW JAKARTA BASED. JAKARTA-BASED COMPANIES, PRINCIPALLY OWNED BY LIEM SIOE LIONG, REPUTEDLY CONTROL ABOUT HALF OF THE PLANTATIONS IN RIAU. P.T. ASTRA, OWNED BY THE SOERYADYAJA FAMILY, ALSO MUSCLED INTO THE PLANTATION AND OTHER BUSINESSES IN RIAU AND NORTH SUMATRA. IN SHORT, MUCH OF MEDAN'S AND SUMATRA'S PREVIOUSLY "AUTONOMOUS" BUSINESS COMMUNITY, WITH TRADITIONAL TIES TO SINGAPORE, HAS BEEN PULLED INTO A JAKARTA-CENTERED NETWORK OF "CONGLOMERATES."

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SINGAPORE AND MALAYSIA

21. ALTHOUGH SINGAPORE HAS ENJOYED ONE OF THE FASTEST RATES OF ECONOMIC GROWTH IN THE WORLD AND ITS ECONOMIC ROLE IN INDONESIA HAS RECENTLY ACHIEVED NEW PROMINENCE WITH THE MEDIA ATTENTION GIVEN TO THE SPECIAL ECONOMIC ZONE ON BATAM ISLAND ACROSS FROM THE CITY STATE, SINGAPORE'S COMPARATIVE ECONOMIC ROLE AND CLOUT IN SUMATRA HAS DECLINED. BEFORE 1965, JAKARTA FOUND IT A CHALLENGE EVEN TO EXERT POLITICAL CONTROL IN SUMATRA, MUCH LESS TO STEADILY EXTRACT PROFITS FROM SUMATRA'S RESOURCES. INSTEAD, THE NEEDS OF SUMATRA'S STILL COMPARATIVELY WEALTHY, BUT RUN-DOWN ECONOMY, WERE MET LARGELY BY SINGAPORE. (THOUGH "KONFRONTASI" WITH MALAYSIA ALL BUT SEVERED THESE TIES FROM 1963 TO 1965). IT WAS SINGAPORE WHICH TRANSSHIPPED AND GUARANTEED THE QUALITY OF SUMATRA'S PLANTATION PRODUCTS; THAT REFINED AND MARKETED SUMATRAN OIL; THAT PROVIDED THE FEW CONSUMER GOODS REACHING THE SUMATRAN MARKET; AND, MOST OF ALL, THAT SAW SUMATRA'S CHINESE, AND THUS MUCH OF SUMATRA'S BUSINESS, THROUGH THE DAYS OF ECONOMIC ANARCHY.

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22. (C) SINGAPORE CONTINUES TO PLAY AN IMPORTANT ROLE IN SUMATRA'S ECONOMY, BUT ITS ROLE IS NOW MORE CLEARLY DEFINED GEOGRAPHICALLY AND IN TERMS OF ECONOMIC SECTORS. WE DO NOT KNOW EXACTLY WHY SINGAPORE'S ROLE HAS DECLINED, AND ATTRIBUTE IT TO A COMBINATION OF DECLINING SINGAPORE INTEREST, GROWING FINANCIAL CAPABILITIES IN JAKARTA, AND JAKARTA'S POLITICAL MUSCLE. ITS CLEAR, HOWEVER, THAT GEOGRAPHICALLY SINGAPORE MAINTAINS CLOSE LINKS TO THE ETHNIC CHINESE COMMUNITY IN MEDAN AND, IN NORTHERN SUMATRA AND PARTICULARLY RIAU, ALONG THE STRAITS OF MALACCA AND INTO THE SOUTH CHINA SEA. ITS OLD INFLUENCE IN SOUTHERN SUMATRA, PREVIOUSLY BASED ON PALEMBANG AND THE TIN ISLANDS, SEEMS TO HAVE FADED MOST RAPIDLY. IN TERMS OF ECONOMIC SECTORS, SINGAPORE HAS BEEN CUT OUT OF OWNERSHIP OF PLANTATIONS AND APPEARS TO PLAY FAR LESS OF A ROLE IN THE FINAL PROCESSING OF PLANTATION PRODUCTS OR THEIR MARKETING. ITS ROLE AS A PROVIDER OF BASIC CONSUMER GOODS HAS BEEN LARGE SUPPLANTED BY JAVA-PRODUCED INDONESIAN GOODS. ITS
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AGRE-00  FRB-03  RP-10  OES-09  USIE-00  JUSE-00  SP-01
DOEE-00  MMP-01  SNP-01  PRS-01  E-01  P-02  T-01
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FM AMCONSUL MEDAN
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INFO AMEMBASSY JAKARTA
AMEMBASSY KUALA LUMPUR
AMEMBASSY SINGAPORE
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ROLE AS A PROVIDER OF CAPITAL IS STILL IMPORTANT. MEDIUM AND A FEW LARGE CHINESE-OWNED ENTERPRISES STILL SECURE INVESTMENT FUNDS FROM ABROAD BY USING THEIR OWN FOREIGN BANK DEPOSITS AS COLLATERAL. FINALLY, WITH THE DEVELOPMENT OF BATAM'S SPECIAL ECONOMIC ZONE, AND THE PROSPECT OF THE SALE OF NATUNA GAS AND SUMATRAN WATER TO SINGAPORE, THE ISLAND STATE APPEARS TO BE INCLINED TO REEMPHASIZE ITS ROLE, ALBEIT MORE NARROWLY DEFINED, IN SUMATRA.

23. (C) DESPITE OLD ECONOMIC TIES BETWEEN NORTHERN SUMATRA CONFIDENTIAL
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AND PENANG, MALAYSIA (STILL SYMBOLIZED IN A PENANG-MEDAN SISTER CITY RELATIONSHIP), AND A SHARED INTEREST (AND RIVALRY) IN THE PRODUCTION OF PLANTATION PRODUCTS, CLOSE ECONOMIC TIES BETWEEN MALAYSIA AND SUMATRA HAVE GRADUALLY WITHERED. ACCORDING TO MALAYSIANS FEEL "UNCOMFORTABLE WITH THE LOCAL BUSINESS ENVIRONMENT" IN SUMATRA, THOUGH A GROWING NUMBER OF MALAYSIANS ARE SERVING AS MANAGERS OF SUMATRA'S PLANTATIONS. HOWEVER, FAMILY AND CULTURAL TIES, BOOSTED BY THE MORE THAN 100,000 MALAYSIAN TOURISTS EACH YEAR, REMAIN STRONG. TO SERVICE THIS FAMILY-ORIENTED TRAVEL, AIRLINES FLY THE MEDAN-PENANG-K.L. ROUTE AND WILL SOON INTRODUCE A PEKANBARU-KUALA LUMPUR-MALACCA SERVICE. MALAYSIAN STUDENTS ALSO STUDY AT MEDAN'S AND ACEH'S SECULAR OR ISLAMIC UNIVERSITIES. FINALLY, TWO HUNDRED THOUSAND INDONESIAN WORKERS (ILO ESTIMATE), MOST OF THEM JAVANESE TRANSMIGRANTS TO SUMATRA, WORK IN MALAYSIA. MALAYSIAN AUTHORITIES TEND TO WINK AT THE ILLEGAL EMIGRATION OF SUMATRA'S ETHNIC MALAYS.

COMMENT AND CONCLUSION
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24. (U) THIS REPORT OUTLINES JAKARTA'S DOMINATION OF A REGIONAL ECONOMY. IT IS DESIGNED TO BE THE BUILDING BLOCK FOR DETAILED ASSESSMENTS OF SUMATRA'S PROSPECTS IN TERMS OF FOREIGN INVESTMENT, THE ENVIRONMENT, AND INDONESIA'S POLITICAL STABILITY. THESE ISSUES WILL BE ADDRESSED SEPTEMBER.

25. (C) NONETHELESS, WE WOULD LIKE TO NOTE HERE THAT JAKARTA'S ECONOMIC DOMINATION HAS NOT REPEATED NOT ENGENDERED A POLITICALLY SIGNIFICANT, ISLAND-WIDE RESENTMENT. THERE APPEAR TO BE TWO REASONS FOR THIS REACTION. FIRST, COMPREHENSIVE INFORMATION ON SUMATRA'S CONTRIBUTION TO THE NATIONAL ECONOMY IS UNAVAILABLE TO THE PUBLIC, INCLUDING REGIONAL ELITES. CONFIDENTIAL
SECOND, SUMATRA IS INTERNALLY DIVIDED BY ETHNIC GROUP, SEVERAL
OF WHOM HAVE PROFITED FROM ENHANCED CENTRAL CONTROL. SUSTAINED
OPPOSITION TO JAKARTA IS THUS FOUND ONLY AMONGST THE ETHNIC
ACEHNES AND, TO A MUCH LESSER EXTENT, THE ETHNIC MALAYS, BOTH
OF WHOM COMBINE A) COMPARATIVELY LOW PER CAPITA INCOMES, B)
RESENTMENT OF INDONESIAN NATIONAL EXPLOITATION OF ACEHNES AND
EAST COAST MALAY BASED OIL AND NATURAL GAS, AND C) HISTORICAL
OPPOSITION TO OUTSIDE DOMINATION. ACEHNES AND MALAYS
CONSTITUTE LESS THAN ONE QUARTER OF THE ISLAND'S POPULATION.
THE CITY OF MEDAN, FOR ECONOMIC REASONS, APPEARS TO HARBOR SOME
RESENTMENT OF THE SOEHARRO GOVERNMENT, AND WEST SUMATRA (THE
MINANGKABAU) WOULD LIKE TO SEE A MORE ISLAMIC-ORIENTED CENTRAL
GOVERNMENT. OUTSIDE OF THESE FOUR AREAS, WE HAVE FOUND ONLY A
VERY LIGHT DUSTING OF POLITICAL OPPOSITION TO INDONESIA'S
JAVANESE-DOMINATED CENTRAL GOVERNMENT.

26. EMBASSIES JAKARTA, KUALA LUMPUR, AND SINGAPORE REVIEWED
AND CONTRIBUTED TO THIS REPORT.

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