

BOOK REVIEWS

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***Realizing Indonesia's Economic Potential*, edited by Luis E. Breuer, Jaime Guajardo and Tidiane Kinda.** Washington, DC: International Monetary Fund, 2019. Pp. 317.

It is always a difficult task to write a book on the Indonesian economy, given its sheer size and complexity. *Realizing Indonesia's Economic Potential* aims to tackle this challenge. It tries to provide a comprehensive macroeconomic analysis to capture the intricacy of Southeast Asia's largest economy.

Through its thirteen chapters, the book identifies the structural constraints preventing the country from growing faster and offers policy suggestions that could help the economy realize its hidden growth potential. Although many factors determine a country's overall growth rate, the authors try to narrow down the analyses to specific aspects that are of particular interest to the International Monetary Fund (IMF) – issues related to fiscal and monetary policy. In fact, all chapters, except the second, have been authored/co-authored by IMF staff members.

The book is comprised of five main parts. The first part includes two chapters that provide a broad overview of the entire edited volume, a brief discussion on important trends that could transform the economy, and a general assessment of how Indonesia has transformed since the Asian Financial Crisis (AFC) of 1997. The second part focuses on important structural reforms that could boost the nation's potential growth (Chapter 3), paying significant attention to the need to tackle issues pertaining to the prevalent infrastructure gap (Chapter 4). The third part covers public finance and looks at how fiscal policy could be used to support inclusive growth more effectively (Chapters 5 and 6). In the fourth part, the authors discuss cross-border trade and finance. The four constituent chapters highlight how domestic growth has been affected by spillovers from the global economy (Chapters 7 and 8), the need to diversify Indonesia's merchandise exports (Chapter 9), and the importance of improved management of the country's capital flows (Chapter 10). The final part evaluates the monetary and financial policy framework, specifically drawing the reader's attention to financial deepening and stability.

It is important to note that this is not the first review of the IMF publication. Stephen Grenville (2019) and Fredrik Sjöholm (2019) have drafted insightful commentaries on the book, and this review tries to complement their views.

The book is framed under a rather optimistic scenario for the global growth trajectory. Several chapters offer suggestions on how Indonesia could achieve a higher growth rate—close to the pre-AFC level of 7 per cent, instead of the current 5 per cent. For instance, in Chapter 3, Jongsoo Shin claims that a higher rate (1 percentage point greater than the baseline growth rate) can be achieved by structural reforms in infrastructure, regulations, and human capital (p. 49). Further, in Chapter 8, Mitali Das argues that increased exposure to economic and financial developments taking place in other parts of the world could open opportunities for Indonesia, which stands to benefit from the diffusion of technological advances and productivity-enhancing spillovers. This, together with structural supply-side policies, could help the country raise its growth potential (p. 181). Then, Heedon Kang, in Chapter 11, contends that financial

development (in the form of advancing financial deepening and inclusion) is also critical for boosting government efforts to develop infrastructure and human capital (p. 229). In general, most authors believe that Indonesia has been performing below its potential and a host of structural reforms are the need of the hour.

Some readers might question the assumptions behind the growth projections in the book. It seems that the authors believe that a 7 per cent growth rate (the target that President Joko “Jokowi” Widodo set during his first term) is achievable if the government is able to carry out the required structural reforms. While the book describes many conditions before Indonesia can achieve such a high expansion rate, it forgets to mention that, empirically, economic growth tends to be slower when a country reaches high-income status. On average, upper-middle-income countries with per capita income above US\$3,995 and below US\$12,375 usually grow by only 3 per cent annually. If we follow this international trend, Indonesia, whose per capita income currently stands at about US\$3,900 (the lower bound of the upper-middle-income threshold), is likely to experience slower growth momentum once its income level increases. As Chapter 8 highlights the country’s remarkably stable real output growth since the AFC (p. 172), it appears that the new normal for the domestic economy will be characterized by a lower average growth rate, and not a very high rate as projected in Chapter 3. Chapter 8 further shows that the growth trend will be mildly negative, and this is not limited to Indonesia alone (p. 177). Therefore, expecting the country to grow at an increasing rate (as indicated in Table 3.2, p. 62) is unrealistic. Given the existing capacity, sustaining growth at even 5 per cent looks challenging for Indonesia.

So, will Indonesia become an outlier? The book seems to suggest that this is possible if the appropriate structural reforms are undertaken. On this, readers might question what these reforms are, and at what pace should they be carried out—sequentially or simultaneously?

In this regard, my opinion is similar to that of Grenville (2019), who writes that the book provides very broad prescriptions on what the government should do (examples include improving infrastructure, investing in health and education, raising tax revenue, *inter alia*). These suggestions are overgeneralized to be useful. On a practical level, the book offers little information on how to implement the many structural reforms mentioned by the authors. For instance, they argue that the government should do more to raise its tax revenue by broadening the tax base (pp. 44 and 121), but fail to explain how to do so effectively, especially given the country’s huge informal sector. In another example, the authors opine that the state needs to continue investing in infrastructure, along with a gradual implementation plan supported by steady progress in structural reforms (p. 83). However, they do not tell readers what type of infrastructure should be prioritized or what kind of structural reforms are needed as prerequisites for effective infrastructure development. In Indonesia, there are many instances of “white elephant” infrastructure projects, which were mainly initiated to win political support from voters. Over time, these projects have neither boosted the economy nor benefited the local community.

Concerning this, the most critical topic not discussed in the book is the “human factor”, *i.e.*, the role of policymakers behind the reform agenda. There is a sense that the book deliberately avoids touching upon politics, which is critical to understanding the constraints on implementing major policy reforms, such as reducing fuel subsidies and raising taxes.

In Indonesia, economic thought generally switches between outward- and inward-looking policies. This is naturally driven by both external as well as internal factors, including the level of pragmatism and nationalism ingrained in the policymakers. As a result, the national policy swings from openness to protectionism and vice versa from one government to another. On average, the Indonesian economy remains half open or half closed but never fully open or fully closed. Despite this common knowledge, this book does not discuss how leaders’ personal opinions and external pressures affect their policy choices. For them, if the political cost of implementing reforms is too high, it is usually a better alternative to not take the risk. A clear example is the elimination of labour market rigidities (a case cited in the book),

which requires the government to revise the 2003 Labour Law. While this could bring significant benefits to the economy, the political cost will be huge for any incumbent government. That is why even the current administration has not been able to implement reforms in this sector.

Overall, the book does not delve into the cost of structural reforms before highlighting their sweeping benefits. Also, there is no mention of the human factor behind the policymaking process. On the topic of institutional reforms, the authors do not discuss whether anyone in the current administration is willing to drive such an agenda in the face of the obstacles brought about by vested interests. Without such considerations, hoping for growth acceleration is almost delusional.

Despite strong assumptions and generalized policy prescriptions, the book offers some useful frameworks to study the complexity of the Indonesian economy. While it does not fully capture the intricacies involved in understanding the political-economy dimension, it does provide important directions for further research on the feasibility of implementing structural reforms in the country, so that it can reach its optimal economic potential in the near future. Given the fast-changing nature of the global economic situation, researchers and policymakers keen on learning more about the Indonesian economy can use this book as a starting point.

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***An Evolving ASEAN: Vision and Reality*, edited by Jayant Menon and Cassey Lee. Manila: Asian Development Bank, 2019. Pp. 198.**

The edited volume *An Evolving ASEAN: Vision and Reality* provides interesting insights on the evolution of the region-making and region-building processes in Southeast Asia. Shedding light on ASEAN's community building exercise from the inside out, the authors take a deep dive into the motives, interests and reservations of the grouping's participant nations, the lessons they have learnt in the process, and their collective future direction. The book is particularly timely, as it helps readers understand ASEAN's policy response to mitigate the unprecedented challenges brought upon by the COVID-19 pandemic.

The book is a great starting point for researchers interested in ASEAN's socio-economic affairs. Presented in clear, simple language, it lays out even the most complex ideas in an easy-to-understand style, a feature that will be particularly useful for readers who are not familiar with the Association's organizational and operational structure. The volume is composed of seven chapters, plus an introduction by Narongchai Akrasanee, the former Minister for Energy and Minister for Commerce of Thailand. Through the elaborate narratives and detailed statistics, the authors not only examine ASEAN's evolution over the past five decades, but also foresee multiple futures for the regional organization. This past-
