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THE ECONOMIC STRUCTURE AND PROBLEMS
OF THE INDOONESIAN TEXTILE INDUSTRY
WITH
RECOMMENDATIONS FOR
POLICY AND IMPLEMENTATION

By

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Prepared Under

U.S. A.I.D./Djakarta
Personal Services Contract
No. AID-497-21
As Extended

February 16, 1968

BEST AVAILABLE COPY

LETTER OF TRANSMITTAL

Hong Kong
February 16, 1968

Mr. Stokes W. Tolbert, Director
U.S. A.I.D. Mission to Indonesia
American Embassy
Djakarta, Indonesia

And

Dr. Emil Salim, Deputy Director
BAPPENAS
Djakarta, Indonesia

In accordance with the provision of the proposed extension of my personal services contract No. AID-487-21, I provide herewith ten (10) copies of a report on The Economic Structure and Problems of the Indonesian Textile Industry with Recommendations for Policy and Implementation. In addition to the ten copies called for by the contract, I am providing five additional copies for possible use by the inter-governmental agencies such as International Monetary Fund and World Bank.

This is a companion report to one to be provided by the textile consulting firm of Kurt Salmon Associates.

It is a pleasure to acknowledge the cooperation of your agency, the Ministry of Textiles and Handicrafts, the various government and private textile enterprises visited, and the Indonesian Textile Manufacturers' Association. I particularly valued the opportunity to present a part of my findings and recommendations to the Country Meeting at the American Embassy and to the top policy meeting at BAPPENAS.

The report could not have been prepared without the encouragement and assistance of my wife, Alice P. Doyle, who traveled with me and typed the final draft of the report. Any errors of fact or interpretation are my responsibility.

Sincerely,

Leonard A. Doyle
Leonard A. Doyle

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SCOPE OF ASSIGNMENT

The work to be performed under this Personal Services Contract was proposed by the Contractor to the Foreign Investment and Industry Officer of the U.S. A.I.D. Mission to Indonesia. The subsequent expansion of the work to include the association of the consulting firm of Kurt Salmon Associates was also proposed by the Contractor. The further expansion of the work to include the P.L. 480 cotton agreement negotiations was requested by Mr. Stokes W. Tolbert, Director of the U.S. A.I.D. Mission to Indonesia.

Original Assignment

The original assignment is stated in Article I of Personal Services Contract No. AID-497-21 dated December 2, 1967 as follows:

ARTICLE I - SERVICES TO BE PERFORMED

A. Purpose and Objective

U.S. A.I.D./Jakarta desires the services of the Contractor to advise and assist the Cooperating Government, through its Ministry of Textiles and Handicrafts, and U.S. A.I.D./Jakarta in making an economic and management analysis of the present position and future problems and requirements of the Indonesian Textile Industry.

B. Duties, Report and Period of Services

1. Duties

Commencing December 2, 1967, the Contractor, who will have provided transportation at his own expense to Indonesia and who will provide transportation at his own expense from Indonesia at the conclusion of this contract, will enter into performance of the services required herein. In performing the above stated objective, the Contractor shall:

Scope of Work

In cooperation with the Ministry of Textiles and Handicrafts, the Contractor will make an economic and management analysis of the present position and future problems and requirements of the Indonesian textile industry. The industry has three parts: power sector, handloom sector, and batik sector. The major emphasis will be on the power machine sector, which is almost entirely located in Java, the heaviest concentration being in West Java, followed by Central Java and East Java.

- a. The main effort will be to determine the location and nature of the major bottlenecks to full capacity production. This will involve defining full capacity in terms of product mix or input, analyzing percentage and nature of capacity not presently usable because of mechanical breakdowns, securing general management estimates of requirements to restore full capacity, spare parts inventory and country source for full operation.

- b. Analysis of requirements for raw material and operating supplies.
- c. Analysis of financial requirements, divided into foreign exchange and local currency. Will expect to secure recent financial and cost statements. These will be in Indonesian, and the Contractor will translate into English and prepare summaries and analysis for A.J.D. and the Cooperating Government.
- d. Analysis of labor problems as they may affect rate of utilization, particularly second and third shift operation.
- e. Analysis of management resources. This will involve securing organization charts for present operation, any revisions required for expansion, and data on availability of additional personnel.
- f. Analysis of transport problems and warehouse problems.
- g. Analysis of marketing problems. This will be a critical feature of the work in terms of central government policy. The industry for at least ten years has operated in a seller's market and the bottlenecks have been raw material and spare parts. Now with the free economy and the appearance of larger amounts of foreign exchange than apparently were considered possible, the market is full of imported textiles in both yard goods and clothing form. An effort will be made to determine how "full" the market really is, the prices being charged and their relation to the domestic production costs; the kinds of imported cloth in relation to the domestic capacity, etc.

For the handicraft sectors the Contractor will do as much of the following as time and information permit:

- a. Handloom. Visit the major centers on Java and secure information about the mechanical condition of equipment, supply of weavers, and hence of yarn requirements. Data on recent production, financial problems, and present inventory position. Main thrust will be on marketing problems of major sections (geographical) with a view to developing alternatives for government policy concerning protection or subsidy.
- b. Batik. This industry is perhaps most important in Central Java, then in West Java and less so in East Java. There is a large cooperative in Central Java in Jogjakarta. This cooperative spins yarn and weaves the cambric from which batik is made. The spinning and weaving plant will be covered in the power machinery study, but its marketing problems depend on the batik industry. Will compare costs and prices of various grades of batik with import substitutes and secure estimates of percent distribution of output by machine and hand methods (both handicraft), and by price/quality classes, low, medium, high.

2. Report

- a. Contractor shall prepare and submit in writing (in the English language) a final report in six copies to U.S. A.I.D./Djakarta, and two copies will be sent for the attention of EA/IND/AID/W.
- b. The report and other data shall become the property of A.I.D. and are not to be published by the Contractor, either in whole or in part, or divulged to any person outside the Cooperating Government or A.I.D. without the written consent of A.I.D. The final report shall be submitted, if possible, before leaving the Cooperating Country, but in no event later than thirty (30) days after his departure therefrom.
- c. In the event of termination of this contract under the provisions of Article IV, Paragraph B, the Contractor shall, within thirty (30) days after such termination, prepare and submit a final report as specified above based on the data acquired and services performed as of the time of such termination.

3. Period of Service

The period of service of the Contractor hereunder, subject to the contingency of earlier termination of the contract as provided under Article IV, Paragraph B, shall be for a period not to exceed six (6) weeks. The exact days of service of the Contractor shall be agreed to in advance between the Contractor and the Private Investment and Industry Officer of U.S. A.I.D./Djakarta.

First Expansion of Assignment

At the end of the initial survey of the textile industry in West Java the writer and the Private Investment and Industry Officer of U.S. A.I.D./Djakarta agreed that U.S. A.I.D./Washington should contract with the textile consulting firm of Kurt Salmon and Associates of Atlanta, Georgia for the services of two textile consultants for a period of four weeks in Indonesia. The following is my understanding of the relation between the work of the KSA team and myself, based on a draft provided by the Private Investment and Industry Officer of U.S. A.I.D./Djakarta.

Scope of Technical Service (by Kurt Salmon Associates)

In association with Dr. Leonard A. Doyle and in cooperation with the Ministry of Textiles and Handicrafts the Contractor Representatives will make a technical analysis of the present position and future problems and requirements of the Indonesian textile industry. The industry has three parts: power machine sector, handloom sector, and batik sector. The major emphasis will be on the power machine sector, which is almost entirely located in Java, the heaviest concentration being in West Java, followed by Central Java and East Java.

1. The main effort will be to determine the location and nature of the major bottlenecks to full capacity production. This will involve defining full capacity in terms of product mix or input, analysing percentage and nature of capacity not presently usable because of mechanical breakdowns, securing general management estimates of requirements to restore full capacity, spare parts inventory and country source for full operation.
2. Analysis of requirements for raw material and operating supplies.
3. Analysis of labor problems as they may affect rate of utilization, particularly second and third shift operation.
4. Analysis of transport problems and warehouse problems.

In conduct of this survey, the contractor representatives will, in association with Dr. Doyle:

1. Inspect selected spinning mills and advise concerning best quality mix yarn if P. L. 480 cotton is used and possibilities of mixing staple fiber to improve quality. Present output is nearly all 20s.
2. Advise on steps needed to get remaining 12,500 spindles in operation in a new 30,000 spindle plant of English origin.
3. Advise on possible quality mix of best existing large weaving mills of approximately 200 looms.
4. Advise on problems of consolidating small weaving plants of 50-100 looms into larger units.
5. Advise on technical problems of finishing equipment required in relation to findings regarding 1 to 4.

The contractors representatives will be accompanied by Dr. Doyle and representative of Ministry of Textiles and Handicrafts who will interpret when necessary.

The textile industry has over 90% of its plants in Java, of which approximately 50% are in West Java centered in the Bandung region, 30% in Central Java in three main centers, 20% in East Java in and around Surabaya. The contractor representatives will spend one week with Dr. Doyle in each of these geographic areas of Java. After the first survey, the contractors representatives probably will want to separate and work on most important problems which were disclosed by first survey.

A trip to be made to Sumatra to review the problems there, as time permits.

Second Expansion of Assignment

Subsequent to the decision to secure the services of Kurt Salmon and Associates, the writer was asked by Mr. Stokes Tolbert, Director of U.S. A.I.D. Mission to Indonesia, to sit in on the first negotiating session for the 1958 P.L. 480 cotton agreement. This was followed by work with Mr. Carl Winberg, Acting Agricultural Attache, U.S. Embassy, Djakarta, with respect to determining the approximate amount of cotton which the spinning

mills in Indonesia might use in 1968, and for suggestions concerning procedures under the agreement which would enable the cotton to make the maximum contribution to the 1968 stabilization efforts of the Government of Indonesia.

The writer and Mr. Tolbert agreed orally that the additional work would require an extension of the contract. The pressure of time and the course of economic and political events in Indonesia were such that a specific amendment to the contract was not discussed until just prior to the departure of the writer from Indonesia on February 2. On February 2 the writer initialed a proposed draft amendment containing, among others, the following provisions concerning the time and scope of work:

NOW, THEREFORE, the parties mutually agree that said contract shall be and it hereby is amended as follows:

1. Basic Contract, Article I

B.3.

PERIOD OF SERVICE as amended, is effective as of December 2, 1967 and shall continue through 31 January 1968, to provide for time to prepare a balanced, comprehensive report with findings, conclusions and recommendations which will be of maximum utility to A.I.D. and the Government of Indonesia. This extension will permit Contractor to attend meetings, conferences, seminars and hold discussions with responsible Government of Indonesia Ministries, trade associations, and visit textile and handicraft facilities incident to making an overall survey to determine the location and nature of the major bottlenecks to full capacity production. The extension will also permit Contractor to attend negotiating sessions between the Government of Indonesia and A.I.D. concerning Public Law 480 agreements as the basis for making specific recommendations to A.I.D. on how P.L. 480 products, particularly cotton can most effectively be used in rehabilitating or expanding the textile industry and to make recommendations with respect to what terms and conditions should be included in P.L. 480 Agreements to provide A.I.D. with sufficient continuing information to ensure effective utilization of P.L. 480 commodities.

2. Article I, B.2.

REPORT is hereby amended as follows:

(a) After arrival of Contractor in Cooperating Country, it was mutually agreed that Contractor would submit three (3) Interim Reports on results of his investigations of various aspects of the textile and related handicraft industries. These reports were required for use by USAID for use in negotiations with Cooperating Country representatives concerning possible imports of Public Law 480 commodities from the United States. The interim reports were also required for day-to-day use by USAID in planning of proposed courses of action with respect to the textile industry in cooperating country. Timing with respect to submission of the interim reports as well as format to be used by Contractor in their preparation will be as mutually agreed to

between Contractor and USAID.

(b) Contractor shall prepare and submit in writing (in the English language) a final report in ten (10) copies to USAID/Djakarta. The Report should reflect the findings, conclusions and specific recommendations of Contractor with respect to each of the items under Article I.B.

Duties, Report and Period of Service in Basic Contract for each of the named industries and handicrafts. The recommendations should be set forth in a manner which will reflect relative priorities for various actions which must be taken to improve the industries being reported on.

I T I N E R A R I E S, M E E T I N G S, A N D C O N -
F E R E N C E S

The investigation included the following:

1. Two series of textile plant visits. The first was made prior to the arrival of the KSA team, and required approximately ten days in Djakarta, Bandung and the vicinity of Bandung, and Den Pasar, Bali. The itinerary for this trip comprises Appendix A-1. The second was made in company with the KSA team and covered Djakarta, Bandung and the area around Bandung, Central Java, and East Java. The first few days were spent with both members of the KSA team, and after that the work was divided so that the KSA men concentrated on technical plant problems and I conferred with general management and secured cost and financial data. Most of the evenings on the field trips were spent with government officials and private industry executives in discussions ranging over a wide variety of economic, political, financial and management problems of the textile industry. The itinerary of the second field trip comprises Appendix A-2 of this report.
2. Conferences with representatives of the Ministry of Textiles and Handicrafts of the Government of Indonesia, including the Minister, Ir. Sunusi; the Director General, Ir. Safioen; Drs. I. Sumedi Wignjosumarto, Director of Production; several section heads of the Directorate General; and the Chief Inspectors of Industry of the provinces of West Java, Central Java, East Java, and Bali.
3. Conferences with officials of the Institute of Textile Technology at Bandung, including the Director, Major General Surjosurjarso; Wibowo Moerdoko, Director of Research and Development; and R. Soemarlan, Director of Administration.
4. Conferences with representatives of the Textile Manufacturers' Association, including K. Kridoharsojo, Chairman; J. G. Tambunan, First Vice-Chairman; and Mr. Engkun Widjaja, member and owner of the private spinning-weaving enterprise, P.T. Wisma Oesaha in Bandung. I also met with representatives of the Textile Manufacturers' Association and representatives of the Ministry of Textiles at a meeting in Djakarta chaired by Ir. Safioen.
5. Secured documents and financial statements (mostly in Indonesian) from the Ministry of Textiles, the Textile Manufacturers' Association, Institute of Textile Technology, and

- virtually all central government, provincial government and government/private enterprises visited. The documents secured and analyzed fill a very large briefcase.
6. Conferred with Dr. Widjojo Nitisastro, Chairman of the National Development Planning Body; Dr. Emil Salim, Deputy Chairman of the National Development Planning Body for Industry and Infrastructure; Dr. Mohammed Sudli, Chairman of the Foreign Investment Team.
 7. Attended the first negotiating meeting for the 1968 P.L. 480 cotton agreement and subsequently conferred several times with Mr. Carl Winberg, temporary Agricultural Department representative in Djakarta, and in company with Mr. Winberg met with representatives of the Ministry of Textiles and Handicrafts to develop data on 1968 cotton requirements and 1967 cotton usage and imports.
 8. In company with Messrs. G. L. Turbyfill and Al Batts of Kurt Salmon and Associates I discussed our chief findings and recommendations at a 2½-hour Country Meeting at the American Embassy in Djakarta on Wednesday, January 31, 1968, and at a 4-hour meeting in the conference room of the National Development Planning Body in Djakarta on Thursday, February 1, 1968. The latter meeting was attended by about twenty officials of the Government of Indonesia, representatives of the World Bank and International Monetary Fund, and advisors to the Government of Indonesia from the Netherlands group of Professor Tinbergen and the Harvard Development Advisory Service.
 9. I conferred constantly with the KSA representatives on the field trips, in Djakarta, and in Hong Kong where we reached a final decision on the general coverage of our reports. I had copies made of documents jointly required and translated the Indonesian where necessary.
 10. I met twice with General Mashudi, Governor of West Java where over half of the textile industry of Indonesia is located. I first met Governor Mashudi in 1959, and renewed my acquaintance in 1960. This time I paid a courtesy call the first day I was in Bandung and had dinner with him and his family the night before leaving Bandung on my first trip.

STRUCTURE, LOCATION AND OWNER-
SHIP PATTERN OF THE INDONESIAN
TEXTILE INDUSTRY

Introduction

The textile industry in Indonesia is divided into two groups: machine and handicraft. The handicraft group consists of handloom weaving and batik making. The handlooms use both domestic and imported yarn. The bulk of the yarn used is cotton, but rayon and silk are used also, as is silver and gold thread. The batik industry dyes cotton cambric cloth by covering parts of the cloth with wax to secure two or more colors by hand dipping. The unique feature of batik is that the pattern is the same on both sides of the cloth. Batik cloth is used for several purposes, but the largest amount is for the traditional long skirt of Indonesian women and, in certain areas, for men. The woman's skirt is called "kain pandjang" or long cloth. It is usually one meter wide and $2\frac{1}{2}$ meters long and is wrapped around the body. The batik industry is protected by the prohibition of imports of machine printed batik patterns. There are at least three main kinds of handloomed cloth, worn chiefly by men: a vertical stripe called "lurik" which is made into a long jacket and worn chiefly by Javanese men; a plaid pattern called "sarung plengkat"; and a multi-colored floral or geometric design. The sarung for men made on handlooms is about 24 inches wide, and two of these are sewn together lengthwise and the ends joined to form a circle a little over two meters in circumference. A piece long enough for a sarung is the basis for payment to the weaver.

Plaid sarung material is made both on handlooms and machine looms, and the domestic industry is protected by total prohibition of imports of the traditional patterns. Each region in which sarungs are worn appears to have certain color combinations or designs which are popular. The machine products usually are trademarked and designated according to quality, of which there are three grades. In general, the quality grades depend on the size of yarn, but the difference between second and third grade appears to be chiefly in the quality of the weaving and finishing and not in the yarn. It appears that the larger and better-managed handloom establishments also use trademarks or "tjaps".

The Mechanical Loom Sector

The machine sector of the textile industry consists of four major processes: spinning, weaving, finishing, and knitting. Finishing includes bleaching, dyeing, hand screen printing, automatic machine screen printing, and roller printing. It is rare for a single enterprise to have an integrated operation. Most of the weaving units are small by conventional industry standards. Most of the spinning mills are new, modern and consist of 30,000 spindles. One mill, Tjilatjap in Central Java, consists of two units of 30,000 spindles each, the first starting production in 1956 and the second in 1964 (I am not certain of the dates). There are five cotton spinning mills which also do weaving, and one small rayon mill which spins and weaves.

The weaving plants are mostly private enterprises, but the largest ones are under some form of government ownership/management. One large and modern integrated spinning/weaving/bleaching plant is owned by the Batik Producers' Cooperative, and one of the new 30,000 spindle spinning mills is privately owned and has weaving facilities which, as I understand it, take a relatively small proportion of the yarn. Most of the weaving enterprises, whether large or small, use looms that are quite old, some going back to the nineteen-thirties. If a weaving mill does its own finishing, it is usually only bleaching and dyeing. The yarn for plaid sarungs and floral or geometric patterns is dyed before weaving (for both hand-looms and machine looms); other fabrics are dyed after weaving or sold to the final consumer as greygoods. Some of the small weavers sell greygoods to the few finishing mills, practically all of which are small and relatively inefficient. Prior to independence, there were no separate finishing mills. The lead in establishing finishing facilities was taken by the Central Government in, I understand, 1954. It built five finishing plants called "induks." This word may be translated roughly as "mother hen" because they were to be an example for others to follow. The induks now, to the best of my knowledge, are owned and operated by the provincial governments. None of the induks, to my knowledge, does either automatic screen printing or roller printing, but some do hand screen printing, chiefly camouflage cloth and insignia for the military.

I understand there are now at least three roller printing operations, and at least one of these also has an automatic screen printing machine. A few plants have automatic screen

printing equipment but not roller printing. In order to do either automatic screen printing or roller printing it is almost universal practice to use imported cloth. The best domestic cloth appears to be too poor in quality and must be secured from too many mills to produce the quality of printed cloth required to compete with imported prints. The KSA report will deal with the technical problems of this operation. We encountered only one roller printing operation in Java which is integrated with a weaving plant, and it apparently prints little or none of its own cloth.

The machine knitting industry consists almost entirely of small units with single-stitch machines which use chiefly domestic cotton yarn of 20S count to produce singlets and T-shirts, often of a somewhat drab appearance. The knitwear is quite serviceable, but with the recent large imports from Japan and Hong Kong the domestic product apparently is not selling well in large urban areas. One firm in Djakarta has tricot equipment and is a very well-managed concern. A major fabric in the Indonesian market is a tricot used in making the traditional woman's blouse called a "kebaja". This blouse is worn with the long batik skirt or sarung. For reasons unknown to me, the combination of a handicraft batik and an imported blouse material is traditional among upper-class women, particularly in Java. A kebaja may also be made from printed material, again usually imported. Virtually all the knitting mills have a garment department in which the knitted material is cut and sewn into undershirts and T-shirts or sportshirts. Some of the better-managed enterprises also produce other ready-to-wear garments from knitted scrap or new material. It is my impression that at present there is substantial unused machine capacity and reasonably skilled operators for ready-to-wear garments, both at the knitting factories and in small garment factories. A few of the knitting units are combined with weaving, but most are separate establishments.

As the foregoing description suggests, the Indonesian textile industry is a mixture of modern large-scale plants and small-scale plants, and the dominant pattern is not one of the integration of two or more processes. Let us now reduce the qualitative data to quantitative form before proceeding further.

Quantitative Picture of the Indonesian Textile Industry
The statistics now available concerning the number, size and location of the textile enterprises in Indonesia are based on the licensing system. It is now realized in Indonesia that

these statistics do not provide the best possible data and a new approach is being used.

For reasons associated with colonial policy, The Dutch looked on Indonesia as a profitable market for the textile industry centered in the Twente region of the Netherlands. It was not until the great depression of the nineteen-thirties that an effort was made to expand and to improve the handloom industry of Indonesia and to develop a machine textile industry. The device for developing or reviving the handloom industry was the establishment of a textile institute in Bandung, West Java. Perhaps the most important contribution of the institute was to develop an improved handloom which could be made for very little money and entirely from domestic material. This loom is still in use throughout Indonesia. It is very simple and efficient, and a new one today is reported to cost between Rp. 500 and Rp. 1,000. The handloom industry currently is so depressed, particularly in West Java, that a second-hand loom in working order can be bought for Rp. 100 or less. The machine industry was for the Dutch primarily and not for the Indonesians. As was the case in other large-scale manufacturing, the Chinese in the Netherlands Indies also got into textile manufacturing.

For reasons not particularly relevant to the present, the Netherlands Indies Government controlled the development of the textile industry (and others) by a licensing system. Under this system an enterprise could not operate until it secured a license for each critical unit of equipment. This system was taken over intact by the Indonesian Government after independence. Where the Dutch used the system to promote their conception of orderly industrial development, the Indonesians used the licensing system to promote their conception of orderly industrial development. For the Indonesian government the objective has been to limit, as far as possible, new textile enterprises to Indonesian nationals. This led to one of the major features of the industry, Indonesian "fronts" for Chinese capital. It is probably fair to say that getting a license was a combination of political affiliation and political entrepreneurship. The license on occasion had great economic value. In technical economic terms, it was worth the discounted present value of anticipated profits.

It is my understanding that the license must remain in the name of the person or enterprise to whom it was first issued. This produces the curious result that the license holder can

sell the physical equipment but not the license, and that an actual enterprise may use equipment originally licensed by two or more persons or firms. All present official statistics on the capacity of the textile industry are in terms of licensed units. There may actually be fewer enterprises in existence than the number of licenses, and the number of units of equipment may be less than the total number licensed. In effect, the licensed capacity is a perpetually expanding number with no provision for scrapping or obsolescence, and does not recognize the actual number of enterprises or their managerial structure. The licensing system was the basis for the allocation of raw material under the guided economy of the Sukarno regime, and is now in large part the basis for estimating yarn requirements for weaving and knitting.

Table 1 shows the licensed spinning equipment in Indonesia at the end of 1966 by area and type of ownership. The upper half of Table 1 was prepared from data supplied by the Directorate General of the Textile Ministry, the lower half was computed by the writer. Table 2 was prepared from data supplied by the Directorate General and the lower half was computed by the writer. All of the enterprises of Table 2 are considered by the Directorate General to be private enterprises. This means not owned by the Central Government. As will be pointed out later, the provincial governments own and operate several large mills and some small mills, and the large batik cooperative owns one large integrated spinning/weaving/bleaching mill and, apparently, two small weaving mills.

The important facts to note from Tables 1 and 2 appear to me to be the following:

1. The spinning sector consists chiefly of large units and the other machine sectors of small units.
2. The textile industry is concentrated almost entirely on the island of Java.
3. The proportion of spinning capacity in any one province is different from the proportion of weaving or knitting capacity in the same province.

Tables 1 and 2 do not bring out an important feature of the industry, the relation between the domestic capacity to produce yarn and the domestic capacity to process yarn. I shall deal with this imbalance in detail in a subsequent section, but for the present I shall simply assert that the spinning capacity at the end of 1967 was substantially less than the capacity to process yarn at the end of 1967.

Table 1 does not provide a completely satisfactory picture of the spinning capacity at the end of 1967, both because new mills came into production and because the ownership structure is not made clear. Table 3 shows the spinning capacity at the end of 1967, and also indicates the spinning mills under construction but not operating. In addition, Table 3 brings out a very important factor for future policy considerations, the number of spindles not available for use in spinning mills now operating. Column 2 of Table 3 is based on figures supplied by the Directorate General of the Textile Industry and appears to be inaccurate. Column 3 of Table 3 shows the number of spindles operating according to my field study, but I did not visit all the spinning mills and I know that my data are inaccurate. The KSA report will provide more complete and accurate data on this important question and will contain specific recommendations for dealing with the problem of getting the spinning mills up to designed capacity.

In a subsequent section I shall deal with the economic and financial issues of the presently non-operating spinning capacity. For the moment, however, the important point is to explain the general reasons for the fact that every spinning mill appears to have designed capacity in excess of operating capacity. The existing spinning mills may be grouped according to whether they were ordered prior to about 1961 or after 1961. For those acquired prior to 1961, the problem is to get back into operation capacity which at one time was in operation but became idle because of the shortage of foreign exchange for replacement parts in recent years. For the spinning mills ordered after 1961, the problem is to complete the plants. Apparently all the machinery and equipment for the post-1961 mills was shipped by the manufacturers as soon as possible after the terms of sale were completed. As a result the equipment arrived in Indonesia long before the buildings to house it were ready. Some of the equipment was delivered to the plant site and some remained for a time in the harbor area. In the time between arrival and installation some equipment was damaged or stolen. I do not have complete information concerning the arrangements with the manufacturers concerning supplying technicians to supervise the installation of the equipment, supervising the start-up, or training a cadre of Indonesian technicians and managers. If such arrangements were included in the original contract, they apparently were not carried out because of the various "confrontations" of the "guided economy" period.

As a result, virtually none of the post-1961 spinning mills ordered by the government had the benefit of foreign technicians to supervise installation and start-up, and few, if any, sent Indonesian technicians or managers to the country of origin of the equipment for training.

If one removes the three Central Government mills (the first nine make up the post-1961 mills) shown as non-operating, i.e. Bekasi, Bandung and Palembang, the designed spindle capacity of the operating mills is 150,000 in relation to present effective capacity of 128,000 spindles, there is about 20% of assigned capacity to be completed. I believe the KSA report will indicate a somewhat larger figure, perhaps the equivalent of one new mill of 30,000 spindles. Clearly the present mills should be brought up to designed spindle capacity before any new mill is included in the prospective five-year development plan.

It appears from Table 3 that at least 10% of the pre-1961 mill capacity is now inoperative because of spare parts problems. Virtually all of the equipment required for both groups of mills will require foreign exchange. In a subsequent section I shall discuss the decision model which I believe to be appropriate for top government policy on this issue, and the KSA report will discuss the technical aspects of the problem.

A final feature of Table 3 to which attention is directed is the large component of spinning capacity now in the hands of the provincial governments, approximately 29% of the designed capacity. These mills present a special problem in what I call the leakage of funds from P.L. 480 cotton. The same is true of the private mills. The "leakage problem" is discussed on pages

It should be noted here that if the effective capacity of the Indonesian spinning mills is substantially less than the probable minimum yarn requirements of the domestic weaving and knitting mills, as it definitely is, there should be no question about adopting a policy of not importing yarn until it is clear that the full effective capacity of the Indonesian spinning mills is being utilized. This is because there is virtually no foreign exchange required for the spinning mills for current operations. As the KSA report will show in some detail, the amount of foreign exchange required to increase current effective capacity to designed capacity may exceed the foreign exchange required for equivalent yarn imports--depending on the time horizon involved for the allocation of foreign

Table 1.

Licensed Spinning Facilities in Indonesia

31 December 1966

	S P I N N I N G		
	Government Mills		
	No. of Enterprises	No. of Spindles	Spindles per Enterprise
JAVA:			
West Java Area			
Djakarta Raya	1	30,000	30,000
Rest of West Java	3	68,000	22,667
Total - West Java	4	98,000	24,500
Central Java Area			
Special Area Jogjakarta	-	-	-
Rest of Central Java	4	155,000	38,750
Total - Central Java	4	155,000	38,750
East Java Area	2	45,000	22,500
Total - Island of Java	10	298,000	29,800
SUMATRA:			
North Sumatra			
West Sumatra			
South Sumatra			
Total - Island of Sumatra			
SUMBAWA (South)			
BALI	1	15,000	15,000
TOTAL } ALL INDONESIA	11	313,000	28,454

PERCENTAGE OF LICENSED MACHINES
BY GEOGRAPHICAL AREA

JAVA:	
West Java Area	31.3 %
Central Java Area	49.5 %
East Java Area	14.4 %
Total - Island of Java	95.2 %
SUMATRA:	
North Sumatra	-
West Sumatra	-
South Sumatra	-
Total - Island of Sumatra	-
SULAWESI (South)	
BALI	4.8 %
TOTAL - ALL INDONESIA	100.0 %

Source: Directorate General of Textile Industry

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M I L L S

Private Mills			T o t a l		
No. of Enterprises	No. of Spindles	Spindles per Enterprise	No. of Enterprises	No. of Spindles	Spindles per Enterprise
1	10,600	10,600	1	30,000	30,000
1	10,600	10,600	4	78,600	19,900
			5	108,600	21,720
1	30,000	30,000	1	30,000	30,000
1	30,000	30,000	4	155,000	38,750
			5	185,000	37,000
1	30,000	30,000	3	75,000	25,000
3	70,600	23,333	13	368,600	28,350
1	30,000	30,000	1	30,000	30,000
1	30,000	30,000	1	30,000	30,000
4	100,600	25,125	15	413,600	27,600

10.5%	26.3%
29.8%	44.8%
29.8%	18.1%
70.2%	89.1%
29.8%	7.3%
-	-
-	-
29.8%	7.3%
-	-
-	3.6%
100.0%	100.0%

Table 2.

Licensed Textile Manufacturing Facilities in Indonesia

31 December 1966

	<u>WEAVING MILLS</u>			<u>F I F I</u>
	<u>No. of Enterprises</u>	<u>No. of Looms</u>	<u>Looms per Enterprise</u>	<u>No. of Enterprises</u>
JAVA				
West Java Area				
Djakarta Raya	35	1,863	53	1
Rest of West Java	<u>495</u>	<u>16,456</u>	<u>33</u>	<u>42</u>
Total-West Java	<u>530</u>	<u>18,319</u>	<u>35</u>	<u>43</u>
Central Java Area				
Special Area Jogjakarta	9	342	34	-
Rest of Central Java	<u>72</u>	<u>2,993</u>	<u>41</u>	<u>1</u>
Total-Central Java	<u>81</u>	<u>3,335</u>	<u>41</u>	<u>1</u>
East Java Area	<u>47</u>	<u>2,456</u>	<u>52</u>	<u>14</u>
Total-Island of Java	<u>658</u>	<u>24,110</u>	<u>36+</u>	<u>58</u>
SUMATRA:				
North Sumatra	23	596	26	3
West Sumatra	5	327	65	
South Sumatra	<u>2</u>	<u>134</u>	<u>67</u>	
Total-Island of Sumatra	<u>30</u>	<u>1,057</u>	<u>35</u>	<u>3</u>
SULAWESI (South)	<u>3</u>	<u>67</u>	<u>22</u>	<u>-</u>
BALI	<u>2</u>	<u>21</u>	<u>10</u>	
TOTAL - ALL INDONESIA	<u>693</u>	<u>25,255</u>	<u>36+</u>	<u>61</u>
PERCENTAGE OF LICENSED MACHINES BY GEOGRAPHICAL AREA				
JAVA:				
West Java Area		72.5%		
Central Java Area		13.2		
East Java Area		9.7		
Total - island of Java		<u>95.5</u>		
SUMATRA:				
North Sumatra		2.4		
West Sumatra		1.3		
South Sumatra		.5		
Total - Island of Sumatra		<u>4.2</u>		
SULAWESI (South)		.3		
BALI		.1		
TOTAL - ALL INDONESIA		<u>100.0</u>		

Source: Directorate General of Textile Industry

Table 3
Spinning Mills in Indonesia
December 31, 1957

	No. of Spindles		No. Shifts	% of Spindle Capacity	
	Designed	Per Ministry Doyle/KSA		Designed	Operating
<u>Central Government:</u>					
Operated by P.N. Sandang					
Senajan - Djakarta	30,000	27,000	27,000	3	
Bekasi - Djakarta	30,000	-	-		
Tjipadung - Bandung	30,132	27,000	17,500	3	
Bandjaran - Bandung	30,000	-	-		
Setjang - Magelang	30,132	27,000	23,000	?	
Grati - Pasuruan	30,132	27,000	28,000		
Lawang - Malang	15,200	13,000	12,000	3	
Tohpati - Den Pasar	15,200	7,000	10,000	2	
Palembang - Palembang	30,000	-	-		
SUBTOTAL - 9 mills	240,796	128,000		50.8	39.
<u>Central Government/Private:</u>					
Nebritay - Pasuruan	22,376	20,000	16,226	4.6	7.
SUBTOTAL - Cen. Gov. - 10	263,172	148,000		55.4	46.
<u>Provincial Governments:</u>					
West Java					
Inteks - Bandung	8,000	7,000			
Central Java					
Texin - Tegal	37,072	30,000			
Tjilatjap - Tjilatjap	60,000	54,000			
Djantra - Semarang	31,528	20,000			
SUBTOTAL - C. Java - 3	128,600	104,000			
SUBTOTAL - Prov. Gov. - 4	136,600	111,000		28.8	34.
SUBTOTAL - All Gov. - 14	399,772	259,000		84.2	80.
<u>Private Enterprises:</u>					
Cooperative (BATIC)					
G.K.B.I. - Medari - 1	34,000	30,000	29,000	7.2	9.
Private					
Pardede - Medan	30,000	27,000			
Wisma Usaha - Bandung	10,600	8,000			
SUBTOTAL - Private - 2	40,600	35,000		8.6	11.
SUBTOTAL - Priv. & Coop. - 3	74,600	65,000		15.8	20.
TOTAL - All cotton & staple Fiber - 17	474,372	324,000		100.0	100.

exchange. (See pages 70-72)

Another set of data concerning the spinning mills is important. This is the cost of the imported components of the mills. Table 4 is derived from several sources. Data for the Central Government mills were supplied at my request by the Directorate General of Textiles, data for the provincial government mill (two units) at Tjilatjap were supplied by the President Director, and data for the integrated spinning/weaving/bleaching mill of the batik cooperative in Medari in Central Java were supplied by the Chief Accounting and Finance Officer. The mills are listed in Table 4 according to the country from which the machinery and equipment were imported. I had no way of checking the accuracy or completeness of the figures supplied, but I have no reason to question the data. The data of Table 4 suggest the following tentative conclusions:

1. Japanese spinning equipment appears to cost substantially less per unit of spindle capacity than European equipment.
2. There appears to have been substantial price increases for Japanese equipment between 1953 and 1964.
3. Based on the G.K.B.I. (batik cooperative) experience, the incremental cost of enough looms and more than enough bleaching capacity to handle all the spinning capacity is quite low.

The data of Table 4, however, do not take into account differences in the count of yarn for which the mill was designed or the existence of equipment for doubling and twisting yarn. It is my understanding that the English and Italian mills and the G.K.B.I. mill were designed to produce yarn of higher count than the other mills. The other mills, as I understand it, were designed primarily for yarn of 20S count. The difference between yarn count and doubling is very important. These are technical matters and will be explained and discussed in the KSA report.

A final consideration in the spinning industry is the ownership/management structure of the Central Government mills. During the "guided economy" regime the task of building the mills, installing the machinery and equipment and starting up the mills apparently was assigned to an organization called "Komando Operasi Proyek-Projek Sandang." I regret that time did not permit me to determine just how this organization was related to the other agencies concerned with textiles. Apparently it was a combination of military and civilian personnel,

Table 4

Reported Foreign Exchange Cost #
of Indonesian Spinning Mills
Which Were Acquired 1950-1967 ##

	<u>C & F</u> <u>U.S.\$</u>	<u>Spindles</u>	<u>Year of</u> <u>Contract</u>	<u>Year Produc-</u> <u>tion Started</u>
JAPANESE				
Tjilatjap - Unit 1 w/o air cond., f.o.b. Japan	1,342,134	30,000	1953	1956
Tjilatjap - Unit 2 w/o air cond.	2,743,339	30,000		1963 ?
GKBI - C & F - All	2,987,037			
Less - Weaving	573,773			
- Finishing	282,828			
Subtotal	856,611			
Weaving only	2,130,426	34,000		1961 ?
Senajan	3,630,313	30,000	1961	Dec., 1965
Lawang	1,901,862	15,200	1961	Mar., 1966
Tohpati	1,901,862	15,200	1961	Apr., 1966
ENGLISH				
Setjang	4,934,327	30,132	1961	Feb., 1966
Seati	4,934,327	30,132	1961	Oct., 1965
Tjipadung	4,934,327	30,132	1961	Dec., 1965
ITALIAN				
Sekasi	6,277,108	30,000	1963	Late 1968
INA - JAPAN				
Bandjaran				
China	2,560,826		1964) Oct., 1967
Japan	1,397,506			
Total	3,978,332	30,000	1964	
EAST GERMANY				
Palembang (incomplete?)	412,954	30,000		Late 1969

In equivalent U.S. dollars.

Does not include Pardede Mill at Medan.

and drew heavily on the Institute of Textile Technology in Bandung and the Association of Textile Experts. (Indonesia has a title of Textile Engineer taken over from the Dutch and based on work abroad in textile engineering or the Sardjana [master's] degree from Bandung.) It is my understanding that the Komando organization recently was dissolved and replaced by a state corporation called P.N. Sandang. The letters P.N. stand for Perusahaan Negara or State Corporation, and Sandang is a word used to designate clothing. I believe that P.N. Sandang is not directly under the Minister of Textiles and Handicrafts, but I am not certain. My impression is that the corporation is rather autonomous in determining its operating and pricing policy. The problems involved in having an autonomous organization operating about 50% of the textile capacity in Indonesia will be discussed at some length in connection with recommendations for a Textile Development Authority and the handling of P.L. 480 cotton.

Let us return now to the data of Table 2 concerning the Indonesian yarn-using facilities. For practical purposes, this means the weaving and knitting enterprises, including handlooms. It was pointed out at the beginning of this section that Table 2 is derived from the license records. It is my understanding that the use of licensed capacity in the textile industry has been the subject of controversy for several years. The Ministry of Textiles and Handicrafts has recognized the weaknesses of the licensed units data and for some time has been attempting to substitute data concerning actual enterprises and actual units of equipment in existence. The time and circumstances available in Djakarta at the end of this study did not permit the careful check of the data that I wanted to make. As a result, I can only provide data which illustrates the problem, but cannot do more.

Table 5 was prepared in Hong Kong from detailed listing of enterprises and yarn requirements prepared by the Directorate General dated February 9, 1966. To the best of my knowledge, this tabulation was intended to provide the basis for estimating yarn requirements for the calendar year 1966, and probably was based on the expectation that yarn would be allocated in 1966 as it had been in 1965.

The basic tabulation used to prepare Table 5 gave the name and address of each enterprise and listed the number of looms under each of some twenty classes (golongan). I believe the classes were based on the width of loom and possibly on the speed, and from this information the amount of yarn required was computed

Table 5

Number of Weaving Enterprises and Number of Looms
Province of West Java (excluding Djakarta)
 (Tabulation of February 9, 1966)

<u>No. of Looms/ Enterprises</u>	<u>Enterprises</u>		<u>Looms</u>		<u>Looms per Enterprise</u>
	<u>No.</u>	<u>% of Total</u>	<u>No.</u>	<u>% of Total</u>	
1 - 10	96		693		
11 - 20	74		1112		
21 - 30	53		1316		
31 - 40	25		854		
41 - 50	23		1062		
Subtotal 1-50	271	81.8	5037	38.5	18
51 - 60	11		613		
61 - 70	9		582		
71 - 80	9		679		
81 - 90	2		171		
91 - 100	3		292		
Subtotal 51-100	34	10.3	2337	17.9	68
Subtotal 1-100	305	92.1	7374	56.4	24
101-125	8		878		
126-150	2		273		
151-175	3		473		
176-200	4		773		
201-225	4		845		
Subtotal 101- 225	21	6.3	3212	24.6	153
Subtotal 1-225	326	98.4	10586	81.0	32
over 225					
239	1		239		
339	1		339		
350	1		350		
397	1		397		
1157	1		1157		
Subtotal 251- 1250	5	1.5	2482	18.9	496
Total 1 - 1157	331	100.0#	13068	100.0#	39

May not add to total because of rounding.

(whether for one or two shift operation I am not certain, but I expect for one shift). I went through the tabulation and added the number of looms and then prepared the loom size tabulation shown in the stub of Table 5. I did this only for the province of West Java, excluding the area of Djakarta Raya. It will be noted from Table 2 that the area of West Java had over 72% of the number of licensed looms in Indonesia, and that Djakarta Raya had 1,863 looms and the rest of the province had 16,456 looms. The figure of 16,456 looms in Table 2 thus compares with the figure of 13,068 in Table 5, and the number of weaving enterprises in Table 2 of 495 compares with 331 in Table 5.

I shall assume that the data of Table 5 provide a rough approximation of the number of actual enterprises and looms at the end of 1965. Given the circumstances of 1966 and 1967, it is probably reasonable to assume that few if any new enterprises were established in those years. Table 5 places in rather dramatic focus the problems of the weaving industry of Indonesia. The problems center around the fact that the vast majority of the enterprises have less than 100 looms. The KSA report will deal at some length with the technical features of small size for weaving establishments, particularly with respect to cost and quality of the output.

If 92% of the weaving enterprises have 100 looms or less, and account for 56% of the total number of looms, one perhaps might conclude that this part of the weaving industry is not much more than an extension of the handloom industry. Certainly this argument might be made for enterprises with fifty looms or less. As I believe the KSA report will indicate, a weaving enterprise with fifty looms or less either will not have a preparation department at all, or will have a poor one. Small enterprises also will have little opportunity to control the quality or source of yarn. The KSA report also will deal with the problem of weaving enterprise size in relation to sizing equipment. If an enterprise does not have sizing equipment or does not have the warp (beam) prepared by an enterprise with sizing equipment, it must use doubled yarn for the warp. The yarn most commonly used for the warp is 42/2. Very little of this is produced in Indonesia, hence it must be imported. Small weaving enterprises rarely have any kind of finishing equipment, hence the output of such enterprises must be sold to a finishing mill for bleaching and/or dyeing or hand screen printing. As Table 2 indicates, the existing finishing capacity in Indonesia is small, and as the KSA report will show,

it is rather inefficient and the quality of work is somewhat substandard.

Based on the data of Table 5, one may conclude that only twenty-six weaving establishments out of a total of 331 are large enough to have a preparation department which includes sizing equipment, and to have finishing facilities. Our small sample suggests that not all the weaving establishments with over 100 looms have sizing and finishing equipment, and the sample indicates that those that do have very serious quality problems in using the equipment. Again, this will be dealt with in the KSA report.

Table 5 does not bring out the ownership of the weaving enterprises or the variation in product mix. The two largest weaving enterprises in fact have about 10% of the loom capacity. The largest one is P.T. Pabrik Tenun Garut "Ampera I" in the town of Garut about thirty miles from Bandung. This is a former Dutch enterprise now owned and operated by the province of West Java. The second largest mill is P.T. Bandung located in the city of Bandung. This formerly was owned by a Dutchman of Indonesian nationality but was sold to the Union of State Railway Employees in 1960.

We visited both the mill in Garut and P.T. Bandung, as well as two other large weaving mills in Bandung, and I visited at least two others in 1959 and 1960. The most significant thing about the large weaving establishments visited was the large percentage of output represented by checked sarung material. Going back to the Dutch era, imports of traditional patterns of checked sarung material have been totally prohibited. This import prohibition policy was established to protect the handloom industry. In fact it appears to protect the large mechanical weaving enterprises far more than it protects the handloom enterprises. Thus one encounters the curious situation that the large weaving establishments able to produce checked sarungs have complete protection for this part of their output. This protection, it should be noted, does not protect against substitute products, but checked sarungs are "traditional" in Indonesia and substitution of "modern dress" appears to have been slow. One may speculate also that the gradual substitution of modern dress for checked sarungs is likely to affect the small handloom producers more than the large mechanical weaving establishments. This is because the large enterprises can (and do, as far as our limited sample provided information) produce a better quality of product, can use brands or "tjaps," are more efficient in marketing, and under the rationing system for yarn of the "guided economy" very

likely secured more yarn and more foreign exchange for good dyestuffs.

Before leaving the mechanical loom sector, another feature of large enterprises in relation to small enterprises should be noted. This is that most of the large firms visited appeared to be working two and three shifts whereas the small weaving enterprises were usually working only one shift, and then not using more than 50-60% of the looms reported to be in working condition.

The Handloom Sector

Let us now turn to the handloom industry. At a very early stage in the study I found that I would be unable to secure adequate data on this sector without a far greater expenditure of time and effort than was available. The qualitative information was that the handloom sector is very sick indeed, and that it is worse in West Java than in Central or East Java. The relative health of the handloom industry in Central and East Java was attributed to the fact that in these regions the type of cloth produced is less vulnerable to competition from imports or import substitutes and the domestic mechanical weavers than is the type of cloth produced in West Java. The handloom weavers of West Java were reported to produce chiefly checked sarungs and low-grade cambric for the batik industry, chiefly in Djakarta. In Central Java it was reported that the chief product was the striped "lurik cloth" favored by Javanese, and cambric for batiks. In East Java and Bali the handlooms were reported to produce multi-color sarungs of floral or geometric patterns difficult or impossible to produce with mechanical looms.

In general our extremely limited visits to handloom establishments confirmed the preceding description. But our visits also caused us to have serious reservations as to when, if ever, the handloom industry ever was "healthy." The little information I secured leads me to the conclusion that the use of the number of licensed handlooms in Indonesia as a measure either of capacity or unemployment is not warranted. I do not believe that any reliable data exist concerning the actual output of the handloom sector or the number of looms that have worked in any one year, or the portion of the year they worked. 1965 was reported to be the big year for textile production in Indonesia, but inquiries at the handloom sectors and of officials in the provincial inspectorate of industry indicate that actual production by handlooms in 1965 was rather low. The few establishments we visited were relatively large (some with 50-200

looms) and the owners appeared intelligent and competent. In general, the owners in Central and East Java appeared better businessmen than those in Badjalaraja in West Java---but the sample was too small and the method of selection such that one should not generalize.

When I stated in interviews with provincial and central government officials that I thought the number of licensed handlooms greatly exceeded the number in existence, and that the number in existence was not the number in working condition, and that the number in working condition had not in fact worked for many years, they agreed with me. They stated that they were attempting to get more realistic data by means of a "retribution tax." This is a small tax (as I recall, about Rp. 25 per loom) imposed by the provincial government. The general idea is that a license holder will not pay tax on more looms than he has, and probably not on more looms than he expects to use. My own guess is that taxes will not be collected on more than half of the number of looms reported as licensed--284,430 according to an English language statement dated December 1, 1966 issued by the Department of Textile Industry and People's Handicraft.

What is the explanation for the continued use of licensed unit data in the face of widespread knowledge that it does not adequately describe the actual conditions either in the handloom sector or the mechanical loom sector of the Indonesian textile industry? In part it may be bureaucratic inertia and the enormous task of securing actual data, and in part the yarn allocation system of the "guided economy" period. The yarn allocation system must be understood in order to grasp the magnitude of the problem of devising a sound policy for the future development of the textile industry.

The Allocation System of the Guided Economy

The allocation system is generally believed to have contributed to the manipulation and corruption of government/industry, and perhaps no place more than in textiles. The system is particularly vulnerable when the various production processes are out of balance. It would not be a bad system if the producing units were reasonably balanced, and if the available domestic production capacity were approximately equal to the effective market demand. Here again one encounters an almost diabolical situation, that of hyper-inflation. I last studied the problems of Indonesian manufacturing during the second half of the year 1960. In my book Inter-economy Comparisons: A Case Study (University of California Press, Berkeley, 1965) the table re-

produced here appears. In rough terms, one can say that the money supply in the three years 1957-1959 increased at a compound rate of 50% per year, using December, 1956 as the base. The rate increased each year. In 1959 the currency and bank deposits, for practical purposes, were devalued by 90%. In December, 1965 the currency was devalued de facto by 99% by the substitution of one new rupiah for 1,000 old rupiahs.

Table 6

Money Supply of Indonesia 1956-1959
(Billions of Rupiahs)

End of Month	<u>M o n e y S u p p l y</u>			Per cent of December, 1956
	Currency	Bank Deposits	Total	
1956				
December.....	9.4	4.0	13.4	100
1957				
March.....	9.3	4.0	13.3	100
June.....	10.9	4.3	15.2	117
September.....	12.5	4.3	16.8	129
December.....	14.1	4.8	18.9	145
1958				
March.....	14.0	5.6	19.6	151
June.....	15.4	6.2	21.6	166
September.....	16.5	7.5	24.0	185
December.....	19.9	9.5	29.4	226
1959				
March.....	20.1	9.9	20.0	230
June.....	22.8	9.5	32.3	250
September.....	20.2#	4.1#	24.3#	187
December.....	26.4	8.5	34.9	269

After 90% devaluation.

Source: Leonard A. Doyle, Inter-economy Comparisons: A Case Study. Berkeley: University of California Press, 1965, page 120.

Hyper-inflation of the magnitude experienced by Indonesia during the "guided economy" period produced a seller's market in virtually all commodities, and particularly for a necessity such as textiles. Although attempts were made to control prices, the control procedures could not be effective and black markets developed. The black market in effect was the real device for allocating output in the textile industry. To the extent that the intended mix of textile products was inconsistent with the effective demand mix as reflected by the black market, production was diverted from the intended raw material product use to one more in line with real market demand.

According to my present information, the most serious extra-legal diversion of raw material was from the handloom sector to the power loom sector. This occurred chiefly with yarn, but there are reports of raw cotton being diverted from domestic spinning mills to Taiwan. Allocation of raw material was based on licensed capacity, and the allocation went to the license holder. Yarn allocation to the major uses, handlooms, mechanical looms, and knitting, is reported to have been rather arbitrary, although the wisdom of Solomon would hardly have been equal to the task of establishing a "rational" basis. In effect the market had to decide in the absence of effective compulsion. We see two possibilities: one, that the end use was wrong, and two, that the allocation within each product group was on the basis of political favoritism. In the latter case this meant that some producers got more yarn in relation to licensed capacity than did other producers. The second situation was not serious in terms of end-product output as long as the supply of yarn did not exceed total production capacity. The first case, planning the wrong end-product use, was serious, as the following explanation shows.

Allocating yarn to handlooms on the basis of the number of licensed looms would result in actual use by the owners if they had the capital and market knowledge to use the yarn in their looms. Allocation of yarn to handlooms as an industry would result in actual use by handlooms only if the effective rate of return on capital was about the same for handloom production as for mechanical looms or knitting. Neither assumption was in accord with the facts.

The manipulation and corruption of the "guided economy" period in textiles is rather widely believed to be based on the fact that the licenses were held largely by Indonesians without adequate capital or market knowledge or managerial know-how, and the capital, market savvy, and managerial skill were possessed by the Chinese. The Chinese capitalist in effect advanced the money to the Indonesian license holder, and he "bought" the yarn. If the return in handloom production was as attractive as in the power loom or knitting sector, the Chinese capitalist would either finance the handloom production of the Indonesian handloom license holder, or use it for his own handlooms. It is not illegal to own unlicensed equipment, hence the owner needs only yarn. He could get it from other people with licenses. The "split" between the actual license holder and the capitalist depended on the bargaining power of the two. My information suggests this was seldom 50-50, but more nearly

10-25% for the license holder and 75-90% for the capitalist. The percentage of yarn diverted from handlooms to mechanical looms and knitting probably varied from year to year and from region to region. The latter occurred because it was illegal to transport the finished textiles from one province to another. My information suggests finished products actually did cross provincial boundary lines, and that illegal exports occurred.

Following the assumption of power by General Soeharto, the allocation system was phased out and abolished entirely in January, 1967. The freeing of the economy and the revision of the B.E. system to provide foreign exchange for textile imports resulted in a large movement of finished textiles, yarn and ready-to-wear clothing into Indonesia between December, 1966 and March, 1967. Since March, 1967 the rate of imports, I believe, has slowed, and most are reported by trade sources to be financed under the Japanese credit arrangement. The large volume of imports combined with the tight money policy of the government have created something of a crisis in the domestic textile industry. To understand the nature and policy problems of the Indonesian textile industry as it enters 1968, a few comments about the role of the Chinese appear necessary.

The Position and Role of the Chinese in the Indonesian Textile Industry

One does not get very far in a discussion of textiles in Indonesia before the role of the Chinese is introduced. It is reported that these comprise three rather distinct groups:

1. Those whose families have been in Indonesia a long time, who became Indonesian citizens rather soon after the opportunity became available, and who own and operate textile enterprises and regard textile manufacturing as their main business;
2. Those also of Indonesian nationality who are "capitalists" who provide working capital (and on occasion fixed capital) to Indonesian owners of textile enterprises. These capitalists are considered by some to shift their capital from domestic financing to importing whenever the latter is more profitable;
3. Those who either are not citizens or who are thought to have their primary loyalty to political and/or financial interests outside of Indonesia. The composition of the third group is reported to shift with political changes vis-a-vis Red China, Taiwan, Hong Kong, and Singapore. The latter group also is thought by some

to be the major importers of textiles on credit, and it has been suggested that a bit of smuggling is done on occasion. The third group is also on occasion charged with manipulating the Indonesian textile market primarily for political ends.

The Chinese capitalists are regarded as the main group involved in the diversion of yarn during the allocation period from the handloom and small mechanical loom license holders to the larger mechanical loom enterprises which they controlled or perhaps owned through Indonesian "fronts." To the extent that the regular commercial banks are unable or unwilling to make working capital loans to the small weavers and knitters, they are virtually forced to rely on the Chinese capitalists. The capitalists in turn are a "destabilizing" force in the textile industry if they shift their activities from financing domestic production to financing imports. They may further aggravate the situation if they use imported textiles secured on credit as a means of securing cash for lending.

My scanty information suggests that the Chinese capitalists are a major factor in the West Java textile industry, particularly in the Madjalaja area. Madjalaja is a major trouble spot---a sort of feast-or-famine area. It was reported to me that at the height of the 1965 "boom" there were forty "capitalists" in Madjalaja owning Mercedes-Benz cars. When I was there in December it was reported that the number of Mercedes cars was down to ten. Curiously enough, this also represented the proportion of December output in relation to the 1965 rate of output! It should be noted, however, that not all the Mercedes were reported to be owned by Chinese.

Having given a qualitative and quantitative picture of the Indonesian textile industry, let us now examine the statistics for the period 1960-67 as they were presented to me shortly after I arrived in Indonesia in late November, 1967.

Statistics of the Industry, 1960-67

Some time after I arrived in Indonesia the office of the Director General of Textiles and Handicrafts supplied me with three documents which were being used in Government of Indonesia analysis and planning for 1968 and 1969. U.S. A.I.D. supplied me with copies of the two reports prepared by Mr. Henry Bressette, the first dated October, 1966 and the second dated May, 1967. Table 9 was in Indonesian, and I have prepared a rough translation. The three Ministry documents comprise Tables 7 through 9 of this report. The documents are

labeled as follows:

- Table 7 Information About Indonesia's Textile Problem
- Table 8 Estimated Textile Stocks for Year 1967
- Table 9 Memorandum Concerning Raw Cotton Imported Under P.L. 450 (prepared by Drs. I. Sumedi Wignjosumarto, Director of Production, and addressed to Drs. Captain Adisumarto, Staff Technician in the Ministry of Finance).

It is important that the reader study the three documents with some care before proceeding with my comments.

Particular attention is directed to the following:

1. Table 7 is dated November 27, 1967. This appears to be an updating for interdepartmental use, because I received at my first meeting a copy containing the same data dated December 1, 1966. It is likely that this document was used in Mr. Bresette's second report of October, 1966.
2. The domestic yarn production estimate in Table 8 of 100,050 bales should be compared with the December, 1966 estimate in Table 7 of 160,000 bales.
3. Item iii, 1967 production of cotton fabrics, of Table 7 shows an original estimate of 380 million meters, and in parenthesis is a note that realization will be 230 million meters. This was the estimate at the time of my first meeting with Ministry officials. Note that the latest estimate for 1967 is 225 million (Item 3 of Table 8).
4. Planning for textiles tends to be in terms of meters of cloth per capita. For 1967-68 it appears that a total population of 110-112 million is being used. It may be important to note that about 50% of Indonesia's population is under 25 years of age. This population is likely to wear western clothes and not traditional sarongs and batiks. For practical purposes, the revised estimate at the time of my arrival of total supply of 450 (revised domestic production of 230,000,000 meters and imports of 220,000,000 meters) million meters represents about four meters per capita for 1967. In my experience various target figures have been used, ranging from nine or ten meters per capita down to five or six. Item 3 of Table 7 shows 1961 as the year of largest total supply in the period 1960-67, and 1965 was the best year for domestic production of yard goods.

1967 will be the best year for yarn production. It is important to note that the high yardage production of 1965 seems a bit inconsistent with the combined supply of domestic and imported yarn, even allowing for a large carry-over from 1964 and low inventories at the end of 1965.

5. In early December the Government of Indonesia officials were pushing for immediate negotiations for P.L. 480 cotton for 1968 because of the inventory position of raw cotton at the end of October. Item 3 of Table 9 states that there was estimated to be enough raw cotton at the spinning mill gudangs to last until April, and enough in other gudangs for another month. In Item 4 of Table 9 they assumed that it would take six months from the signing of the agreement to the receipt of cotton.

Table 7

Information About Indonesia's Textile Problem

1. Domestic Production

i. Production of cotton yarn in:

1960	42,000	bales of 400 lbs.	(128,000 spindles)
1961	40,000	" " " "	(128,000 spindles)
1962	52,000	" " " "	(162,000 spindles)
1963	42,250	" " " "	(228,000 spindles)
1964	29,500	" " " "	(238,000 spindles)
1965	77,569	" " " "	(338,000 spindles)
1966	116,003	" " " "	(388,000 spindles)
1967	160,000	" " " "	(418,000 spindles)
1968	180,000	" " " "	(500,000 spindles)

ii. Total spinning capacity per year - 3 shift = 41,000 ton of yarn

Number of spindles now = 415,076 spindles

Potential capacity per spindle per year - 3 shift = 100 kg. yarn

Real capacity per spindle per year - 3 shift = 80 kg. yarn

iii. Production of cotton fabrics inc. gray goods in:

1960	282,000,000	meter
1961	374,000,000	"
1962	307,130,000	"
1963	268,267,500	"
1964	192,242,500	"
1965	456,003,800	"
1966	191,289,000	"
1967	380,000,000	" (realization will be) (230,000,000 meter)

iv. Total weaving potential capacity:

Power looms: per year 1 shift = 230,000,000 meter

Hand looms: per year 1 shift = 360,000,000 meter

(efficiency 60%)

Number of looms:

Power looms: ± 29,000

Hand looms: 284,430

v. Requirement of raw materials:

a. For spinning industry in	1965	15,500 ton cotton
	1966	12,000 ton cotton
	1967	34,000 ton cotton

b. For weaving industry in	1965	365,000 bales cotton yarn
	1966	154,000 bales cotton yarn
	1967	520,000 bales cotton yarn

Table 7 (Continued)

vi. The needs for spare-parts:

- a. In spinning industry - US\$ 1,500,000
- b. In weaving industry - US\$ 2,500,000

2. Employment and Skills

i. Present employment in:

- a. Spinning industry - 3 shift = 22,000 workers
- b. Power loom industry - 2 shift = 83,000 workers
- Hand loom industry 60% of 1 shift = 426,000 workers
(part are part-timers)
- Batik industry - 1 shift = 300,000 workers
(part are part-timers)

Output per worker per year:

a. In spinning industry:

1964 output per worker per year ± 500 kg. cotton yarn
1965 " " " " " ±1,200 kg. cotton yarn

b. In weaving industry:

1964 output per worker per year, 384 mtr gray cotton
1965 " " " " " 912 mtr gray cotton

ii. Present average and minimum wages both in spinning and weaving industry:

- a. Daily worker Rp. 22.50 and Rp. 30 per day
- b. Monthly " Rp. 950. and Rp. 1,500 per month
- c. Work order Rp. 35 and Rp. 60 per day

These wages include 8 kg. of rice per worker and 3 - 5 kg. rice for his wife and each of his children per month.

iii. The skilled labor for the textile industry is relatively enough.

3. Consumption

Total textile available (gray and finish goods)

	Domestic Production	Imported	Total
1960	282,000,000 meter	122,400,000 meter	394,200,000 mtr
1961	374,000,000 "	237,000,000 "	611,000,000
1962	307,130,000 "	91,000,000 "	398,130,000
1963	268,257,500 "	124,000,000 "	392,257,500
1964	192,242,500 "	106,800,000 "	299,042,500
1965	456,033,800 "	104,000,000 "	560,033,800
1966	194,289,000 "	44,000,000 "	238,289,000
1967	380,000,000 "	170,000,000 "	550,000,000

Table 7 (Continued)

4. Imports

	Raw Cotton	Cotton Yarn	Gray & Finished Goods
1960	9,300 ton	300,000 bales	122,400,000 meters
1961	8,100 "	126,000 "	237,000,000 "
1962	8,000 "	80,000 "	91,000,000 "
1963	13,900 "	169,000 "	124,000,000 "
1964	10,000 "	120,000 "	106,800,000 "
1965	12,000 "	93,710 "	104,000,000 "
1966	17,000 "	40,354 "	44,000,000 "
1967	34,300 "	53,000 "	220,000,000 "

Raw cotton is imported from:

- United States of America
- People's Republic of China
- Pakistan
- India

Cotton yarn is imported from:

- Japan
- Yugoslavia
- Hong Kong
- People's Republic of China
- Italy
- Pakistan
- India

Gray and finished goods are imported from:

- Japan
- Yugoslavia
- Hong Kong
- People's Republic of China
- Pakistan
- India

Djakarta, November 27, 1967

DEPARTMENT OF TEXTILE INDUSTRY
AND PEOPLE'S HANDICRAFT

Table 8

Estimated Textile Production and Inventories
Calendar Year 1967

<u>Item No.</u>	<u>Explanation</u>	<u>First nine months</u>	<u>Calendar year</u>
1.	Cotton yarn produced in Indonesia		
	a. First quarter	18,600 bales	18,600 bales
	b. Second quarter	21,275 "	21,275 "
	c. Third quarter	27,175 "	27,175 "
	d. Estimate for 4th		
	e. Subtotal 1.	67,050 bales	100,050 bales
2.	Imports of Cotton Yarn		
	a. Sop Gap Yen Credit#	27,392 bales	27,392 bales
	b. Taiwan (Berdikari)	38,478 "	38,478 "
	c. General imports:		
	70% x P.I.		
	@ 2.9 million (\$200/Bale)		
	" \$2 million	10,000 "	10,000 "
	d. Estimated general imports for 4th qtr.		4,000 "
	Subtotal 2.	75,870 bales	79,870 bales
	Subtotal of 1 & 2	142,920 bales	180,000 bales
	Convert Bales of Yarn to Meters of Cloth:		
	1 bale = 1,250 mtr.	179,000,000 meters	225,000,000 mtr.
3.	Imports of Yard Goods		
	a. 70% of P.I. entering first three quarters		
	" \$U.S. 74,248,322.80 =		
	\$U.S. 51 million		
	at ave. price \$0.32/M	151,000,000 meters	151,000,000 mtr.
	b. Estimate for fourth quarter		50,000,000 mtr.
	c. Estimated stock at Jan. 1, 1967 (Berdikari)	19,000,000 "	19,000,000 "
	d. Subtotal 3.	170,000,000 meters	220,000,000 mtr.
	Total of Items 2a & 3.	& 349,000,000 meters	445,000,000 mtr.

Probably should read "Step Gap Yen Credit"

& Estimated that 50% of the total stock is at the beginning of Lebaran

Table 9

Memorandum Concerning Raw Cotton Imported Under P.L. 480

The following is a rough English translation of a memorandum in Indonesian dated December 1, 1967. The memorandum is addressed to:

Drs. Kaptin Adisumarto
Staf Ahli SPRT Menteri Keuangan

From: Drs. J. Sumedi Wignjosumarto
Direktur Produksi, Direktorat Djendral
Perindustrian Tekstil

Concerning: Kapas kasar (raw cotton) ex P.L. 480

In response to our discussion at the meeting in your office on 29 November 1967, concerning the problem of raw cotton imports under P.L. 480 and in answer to questions raised by the American government in Djakarta in its letter dated 24 November 1967, the information is as follows:

1. Inventory of raw cotton in the warehouses of the spinning mills at the end of October, 1967 was 62,182 Bales (500 lbs.)

Inventory of raw cotton in other warehouses at end of October, 1967 was	11,125 Bales
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Total	<u>73,307 Bales</u>
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2. Inventory of cotton yarn at the spinning mills at end of October, 1967 was 11,825 Bales (400 lbs.)
3. Average monthly consumption of raw cotton at the spinning mills for October, 1967 is estimated at 9,000 bales. At this rate the available stock above will be consumed by the end of June, 1968. There are several spinning mills whose stock of raw cotton will be exhausted by the end of April, 1968.
4. Reserve stocks of cotton required:
 - 4.1 It is an operating principle of the Indonesian spinning mills that a reserve stock equal to 3 month's production requirements should be maintained. As a result, the cotton agreement must be signed at least 6 months before stock will arrive in Indonesia.
 - 4.2 It can be seen that it is probable that we will have only 5 month's reserve stock of cotton when the agreement is signed.
5. Requirements of raw cotton, cotton yarn, and ready yard goods, in connection with P.L. 480 for the years 1968 and 1969 are estimated as follows:

<u>Type of Product</u>	<u>1968</u>	<u>1969</u>
a. Raw cotton	150,000 Bales	180,000 Bales
b. Cotton yarn	175,000 Bales	200,000 Bales
c. Yard goods	None	None

Table 9 (Continued)

1 Bale raw cotton = 500 lbs.
1 Bale cotton yarn = 400 lbs.

6. It is hoped that cotton yarn and yard goods will be received by other means in the years 1968 and 1969 (private importers) as follows:

<u>Type of Product</u>	<u>1968</u>	<u>1969</u>
a. Cotton yarn	20,000 Bales	30,000 Bales
b. Yard goods	200 mill. meters	200 mill. meters.

7. Requirements for yarn of all kinds in the years 1968 and 1969 are estimated as follows:

1968	:	350,000	-	400,000 Bales
1969	:	400,000	-	450,000 Bales

Note: The estimate of yarn requirements above is based on the assumption of a general improvement in the economy, in the demand for domestically produced textiles.

8. Conditions of sale of raw cotton, cotton yarn, and yard goods proposed herein are as follows:

a. Raw Cotton	:	For Government mills	-	delayed payment/consignment
		For private mills	-	cash and carry
b. Cotton Yarn	:	Domestic production	-	cash and carry
		Imports	-	will enter under B.E./B.E. Credit
c. Yard Goods	:	Domestic production	-	cash and carry
		Imports	-	will enter under B.E./B.E. Credit

(A courtesy ending)

DIREKTORAT DJENDRAL PERINDUSTRIAN TEKSTIL
DIREKTUR PRODUKSI

Signed

(Drs. I. Sumedi Wignjosumarto)

Copies:

1. Diridjenteks
2. Dirum P.N. Sandang
3. Dinas Pengadaan
4. A r s i p

Note: Translated by Dr. Leonard A. Doyle but not checked with Indonesian officials for accuracy.

Revision of the 1967 statistics and 1968
Estimates During the Study Period

On December 22, 1967 the Directorate General of the Textile Industry issued a new set of estimates for 1967 and of requirements for 1968. These estimates are included in this report as Appendix Tables B-1 through B-7. I have taken the liberty on Table B-1 of putting in parentheses the ownership of the spinning mills.

The most important revision in the data for 1967 was the change in the estimate of finished textile imports from 220 million meters to 511 million meters. The lower figure was based on an estimating technique employed for several years which used what is called "Intent to Import" data of the Central Bank, Bank Indonesia. In effect these figures, stated in U.S. dollars, are for imports to be paid for in cash. This was the only way of importing textiles for most of the guided economy period. Early in 1967 textile imports were permitted on credit under what is called the B.M. Credit System. It was apparent that a large dollar volume of textiles were imported on credit in the first half of 1967. As a result, the import estimates based on Customs receipts greatly exceeded those based on "Intent to Import" data. The revision to 511 million meters was based on Customs receipts data. The figure I heard fairly often was that credit imports were about U.S.\$ 60,000,000. This, of course, does not include illegal imports. I believe this was a fairly significant amount.

A second significant revision was in the estimate of domestic yarn production in 1967. Table 7 shows 160,000 bales of 400 pounds, whereas Table 8 (prepared later in December) shows 100,050 bales. If the data of Table 7 really were prepared around the end of 1966, as I understand was the case, the yarn production estimate of Table 8 should be considered as the official one at the end of 1967. It should be noted, however, that the December estimates of domestic spinning mill cotton consumption are not quite consistent with the December estimates of domestic yarn production. Using the standard waste percentage of 15% for cotton converted to yarn, my arithmetic indicates that 103,759 bales of 500 pounds of raw cotton should produce 110,245 bales of yarn of 400 pounds per bale. This, however, is not a serious discrepancy.

The reader will recall that one of the important tasks of the KSA team was to provide an independent estimate of raw cotton requirements for 1968. The team visited every large spinning

mill and their estimate will be shown in detail in their report. It is my recollection that it will be around 125,000 bales or less. This compares with 180,000 bales in Table 7 and the latest estimate of 161,436 bales in Appendix Table B-1. There is no great harm in overestimating cotton requirements if there is no constraint on the foreign exchange involved. Since there is a very serious constraint for 1968, it is desirable to estimate requirements as carefully as possible.

A third significant revision in the data for 1967 was with respect to the quantity of yarn imported. The last page of Table 7 shows 53,000 bales; Table 8 shows 79,870 bales, and Appendix Table B-5 uses 53,000 bales. It is my impression that the figure of 79,870 bales is more in accord with the facts than the figure of 53,000 bales. Time did not permit a reconciliation of the two estimates.

Although it does not involve a revision of the data, a word of caution is in order about the method of converting domestic production and imports of finished textiles to the common denominator of linear meters of textiles. Items 2 and 3 of Table 8 show the arithmetic employed. This is an extremely crude method because it does not allow for differences in quality or even in width. To convert the dollar value of several different kinds of yard goods and many different sizes and kinds of ready-made clothing into meters hardly provides a useful or significant measure of consumer supply. Thus in one year only cheap printed cloth might be imported, and in the next year only expensive yard goods and finished garments. If the dollar value in each year was the same, would the yardage be the same? It is my impression that the textiles imported in 1967 were of higher quality and consisted more of ready-to-wear items than was the case in earlier years. If this was so then the amount measured in meters probably was not as much greater in relation to 1966 as the official estimates show.

The imports of textiles in 1967, legal and illegal, appear to have brought about a serious situation for both the domestic weaving and the domestic knitting industry in the last half of the year, and particularly in the last quarter. When I visited the small weaving and knitting plants in December and January almost all were working only one shift and with only part, often less than one-half, of the looms or knitting machines said to be in operating condition. During the month of January in particular there was the curious paradox of a sharp increase in the price of yarn and reported distress and shutdowns

in weaving and knitting. We must now look at some of the features of the textile market in Indonesia, with particular attention to December, 1967 and January, 1968.

THE I N D O N E S I A N T E X T I L E M A R K E T
S T R U C T U R E A N D P R I C I N G
P R A C T I C E S

The Cotton Market and Pricing Practices

For practical purposes the entire supply of raw cotton in Indonesia is in the hands of the central government. I shall confine my discussion to the current situation in which the entire supply of imported cotton is secured from the United States under the provisions of P.L. 480. It is my understanding that in both 1966 and 1967 the entire purchase of P.L. 480 cotton in each year was shipped at one time. Our field study indicated that the staple lengths requested by the individual mills were not always ordered, and that what was ordered by the officials in Djakarta was not always what was purchased by the Indonesian government representatives in the United States. The terms of sale in the 1966 and 1967 agreements provided for inspection of the cotton after arrival in Indonesia and for the arbitration of claims that the quality received was not the quality paid for. The KSA report will deal with the technical problems of testing staple length in Indonesia and make recommendations for a new contract procedure for 1968 and subsequent years.

Evidence obtained at the spinning mills indicated that the staple lengths actually received often were significantly different from those required by the type of equipment at the mills and the count of yarn scheduled for production by the separate mills. An example was the situation in the provincial government mills in Central Java. The three mills, Djantra, Texin at Tegal, and Tjilatjap had to engage in a rather elaborate exchange of cotton at the end of 1967 and early in 1968 to secure the staple lengths best suited to the mills, and also to transfer a surplus from Djantra to Tegal and Tjilatjap.

I did not visit the large private spinning mill of Pardede in Kodan, and do not know the details of its controversy with the government concerning the terms of sale of raw cotton from P.L. 480 purchases. One of the KSA men did visit Pardede, and the KSA report will deal with the alleged discrimination with respect to the private mills.

It appears that the central government mills and the provincial government mills secure their cotton "on consignment." This means that they do not pay for the cotton used until they collect from their customers. In effect, the central government sells cotton to government mills on credit. Now comes the strange part. The terms of sale in rupiahs per pound of a given quality of raw cotton are the same as the terms of sale by the U.S. Government to the Government of Indonesia. At first glance this seems reasonable. It would be in a stable price situation, but that has not been the situation in Indonesia in 1966 and 1967. As was pointed out earlier, Indonesia does not produce all the yarn it uses and must import yarn. In 1966 and 1967 most of the yarn appears to have been secured under what is termed a "third country processing agreement" in connection with the P.L. 480 agreement. In effect the United States Government sells to the Indonesian Government enough raw cotton for both its own spinning industry and all or most of its imported yarn. The yarn not produced in Indonesia is processed in a "third country." In effect, Indonesia gets the cotton component of the yarn under the same liberal terms that it gets for cotton processed in Indonesia, but must pay the processing costs in foreign exchange or make some credit arrangement with the processing country. I am not informed about the 1966 agreement, but it is my understanding that in 1967 Indonesia secured about 27,392 bales of yarn from Japan under what is called the "stop gap yen credit agreement" and about 38,478 bales of yarn from Taiwan. As I understand it, both these amounts were from P.L. 480 cotton--certainly the Taiwan yarn was. In addition, the Directorate General of Textile Industry estimated that about 14,000 bales of yarn were imported by private traders.

It is my understanding that the "third country" yarn was imported by one or more of the State Trading Companies of the Central Government. The unexpected nature of my work in Djakarta after returning from the field study with the KSA team prevented me from looking into the government yarn import arrangements. For this reason what follows may be inaccurate. As I understand the situation, however, the State Trading Companies, particularly P.N. Berdikari, pays the Ministry of Finance/Bank Indonesia the contract price with the third country processor plus the raw cotton component in rupiahs at the rate of exchange prevailing at the time of the cotton purchase. It also is my understanding that the State Trading Company or companies price the imported yarn to the domestic processors at a rupiah price equivalent to that charged by the private importers. This in turn

is based on the current B.B. rate plus some adjustment for anticipated changes.

If the B.B. rate changes because of inflation, i.e. it takes more rupians to buy a dollar of foreign exchange, the State importer secures what I will call an "inflation profit." By the same reasoning, if the central and provincial government spinning mills price yarn at or slightly below the current price of imported yarn, they also will secure an "inflation profit."

Indonesia experienced hyper-inflation in the latter part of the guided economy period, and prior to that the money supply increased at about a compound rate of 50% a year. The new regime is desperately striving to balance the central government budget and halt the inflation spiral. The existing arrangement for the pricing of cotton to the spinning mills appears to create inflationary prices for yarn because of the existence of a small amount of private yarn imports. The implication of this for future policy will be discussed in the section on Policy Recommendations.

The Yarn Market and Pricing Practices

The way in which the current market price of both domestic and imported yarn tends to be determined by the current landed cost of privately imported yarn was explained above. Here I shall deal with the terms of sale of government yarn. As I understand it, both the State importing companies and the government spinning mills sell yarn on a "cash and carry" basis. There may be some credit to certain customers, but it is my impression that through 1967 at least there was little yarn sold on credit. Although I did not have an opportunity to meet with officials of P.N. Berdakari, the chief importer of "third country" yarn, some of my other sources of information led me to believe that the State importing firms, at least in prior years, were slow to pay the Ministry of Finance/Central Bank for the yarn. To the extent that an importer or a government mill is slow to pay the Ministry of Finance/Central Bank, to that extent the central government current budget position is impaired.

As will be shown in more detail under the section on Accounting Practices, Costs and Margins, yarn is by far the largest single element of cost for a weaving mill and a knitting mill. When these enterprises (predominantly small private firms) must pay cash for yarn and meet the current conversion costs in cash, they will suffer a serious deterioration in "real

working capital" if the price of their finished product does not move up with the price of yarn. If the price of the finished product increases faster than the price of yarn, they will realize an increase in "real working capital." In the hyper-inflation of the last years of the guided economy, the latter almost certainly was the case. This was helped by the yarn allocation policy which, as I understand it, provided yarn at original cost and not at replacement value. This explains why a license was so valuable, and why there may have been a lot of manipulation and some corruption in the allocation of yarn.

In 1967 the weavers and knitters, to use a hackneyed expression, found the shoe on the other foot. In 1967 the plentiful supply of imported textiles of good quality and relatively low prices put a fixed or slowly-rising ceiling on selling price, and certainly reduced the quantity they could dispose of at the prices determined by imported goods. They were thus "squeezed" between the relative fixed selling prices and the rising cost of yarn determined by the B.E. exchange rate, the long-overdue increases in the prices of electricity from the central government power agency, PLN, and the price of diesel fuel from the state petroleum distributing agencies. Added to this was the sharp increase in the cost of rice. As I shall show in the section on Accounting Practices, Costs and Margins, rice for the workers is one of the largest elements in the cost of production for every government weaving mill and many private mills. Even when a private mill does not distribute rice directly to its workers and managers, it is under almost irresistible pressure to raise money wages when the price of rice advances sharply--or suffer deterioration in worker morale and quality of production. The result in 1967 was a severe reduction in the "real working capital" of the weaving and spinning firms.

The Finished Textile Market and Pricing Practices

There appear to be two "layers" of wholesalers between the small textile producer and the retailer. The largest weaving mills may have their own sales department, but apparently even there they must sell some of their output to a wholesaler. The few conversations I had with private industry executives indicated that both wholesalers and retailers attempt to secure a margin of at least 10% on selling price, and if possible on cost. Since the cost pyramids from yarn through the wholesaler, a retail margin of 10%, while very low by the standards of

western economies, is a large margin in Indonesia when related to the wage and salary level. The result is that retailing units are usually small, and in the small towns and villages are very small indeed. In Bali, for example, I bought a handloomed Balinese sarung at a small retail stall in one of the pasars in Den Pasar, the largest town. I paid Rp. 250 for it. With a 10% markup the retailer realized as much from that one sale as the weaver received in wages for one day!

Within a day or two after we arrived in Djakarta my wife accompanied a friend to the new market called Pasar Senen. This is a multi-story building of re-enforced concrete in which there are over 100 small shops or stalls, of which the largest percentage sell textiles. The Indonesian woman with my wife was enthusiastic about the abundance of imported items, the good quality, and the low prices. A few days later my wife and I systematically sampled the textile stalls at the same market with the view of comparing the prices and quality of domestically produced textiles with the prices and quality of imported textiles. We found in every stall visited that the display area for domestic textiles occupied a very small percentage of the total area, and was unfavorably located. The Indonesian textiles were of extremely poor quality and obviously were not selling. Conversations with the clerks confirmed this.

When I was in Bandung my wife and I found the same situation. When I traveled with the KSA team we conducted more extensive investigations in Bandung and other cities and the KSA men bought samples of the various Indonesian textile products. They will cover their impressions in some detail in their report. Here it must suffice to say that we appear to be in agreement that the Indonesian yard goods we saw in the market and at many of the mills, large and small, were of extremely low quality in every respect. The KSA men said that in the U.S. market such cloth would be regarded as "waste" or "rags" and would sell for about the cost of the yarn. I would estimate that in the middle and upper-class market areas in the large and medium-sized towns the Indonesian stock of yard goods was less than 5% of the total stock, and the turnover a small fraction of that of the imported goods.

The implications of the large stock of imported textiles of good quality and relatively low price in relation to the small stock of domestic textiles and their inferior quality will be dealt with under the general subject of Policy Recommendations under the heading Can the Domestic Weaving and Knitting Industry

be Protected by High Import Duties?

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I have neglected the batik industry up to now. This is because it represents a combination of spinning, weaving, and finishing as well as a somewhat unique marketing situation. For those not familiar with the process of making batik cloth, it may suffice to say that the dyeing process is without doubt the most labor-intensive and dye-expensive in the world. On simple economic grounds and by western industry measures, the Indonesian batik process is an anachronism. But Indonesia is not a western country. Batiks are a "traditional" item of considerable importance in the Indonesian culture. By definition "economic development" implies substantial changes in traditional values and traditional ways of doing things. Also by definition an important barrier to economic development is a deeply-rooted and pervasive resistance to change in traditional values and ways of doing things.

As with several other parts of my study, the events of the last week or ten days in Djakarta completely eliminated the time I expected to spend with the G.K.B.I. (Indonesian Batik Producers' Cooperative) executives at the head office in Djakarta. Not having the benefit of their views and their statistics, I can say much less about the batik industry than it deserves. The following generalizations are based in part on our experience in buying batiks in 1956-57, and in part with visits to batik production units then and in 1959 and 1960 in relation to our visit to the cooperative in Pekalongan, Central Java in January, 1968.

In general, my impression is that the quality of workmanship of batiks we saw this time was substantially below that of those we saw and purchased in 1956-57. This is true of the cloth itself and of the batik dyeing. The few Indonesian friends with whom we discussed batik quality supported this general impression. I attribute the decline in quality of dyeing to the demoralization of the long period of inflation. Batik making is a small-unit handicraft industry, and the employers seldom provide rice or other essential commodities, and seldom provide housing. Money wages apparently have always been low, particularly for the women who make up the majority of the work force.

At the big G.K.B.I. integrated spinning/weaving/bleaching mill at Medari we were told that the output of the mill at full capacity met only about 10% of the cambric requirements of the batik industry. Ten per cent seems low to me, however. G.K.B.I.

operates 500 modern looms three shifts a day. Since I do not know the annual yardage of batik production, I cannot check the 10% estimate. The provincial government integrated spinning/weaving mill, Texin at Tegal, Central Java is reported to have produced primarily dyed black jean cloth for sale to the tanis (farmers) under the former Dutch owners. It now produces mainly cambric for the batik industry. It does not bleach its cambric and apparently it is not bleached before dyeing, and goes into the lower quality batiks. The best batiks are made with imported cambric. The Netherlands formerly supplied all the cambric for high-quality batiks, but we were informed that now most of the cambric comes from Japan. The quality of the Netherlands' cambric is considered superior to that of Japanese cambric for the batik process, but the Japanese have a price advantage.

Although the batik industry is considered to be "depressed," it was also thought to be "depressed" in 1956-57. In general, I believe it will be a declining industry in the future, but that the decline will be relatively slow and gradual if the long-standing policy of completely prohibiting imports of printed cotton with traditional batik patterns is continued. If this is so, the gradual decline will not pose a serious threat to the Indonesian weaving industry. The quality of batik dyeing may improve if the economy of Indonesia is stabilized and the purchasing power of money wages stops declining. If this desired result comes about, it may be possible to raise real money wages and improve the generally bad working conditions of the batik workers. If inflation continues at something like past rates, I see little hope for bettering the real income and working conditions of the batik industry. Poor quality may do more to hasten its decline than high prices. Another long-term factor working against batik is the large number of young people. I anticipate they will break more with "tradition" and wear western clothes, especially if output continues to lag behind population growth.

Imported Textiles in the Indonesian Market

Data on textile imports are shown in Appendix Table B-7. Japan usually is the chief supplier of textiles to the Indonesian market, but other countries appear to contribute large amounts when political conditions favor them. The chief exporters of textiles as "political exporters" have been the People's Republic of China, Russia, and Hong Kong. The recent movement of capital from Hong Kong to Taiwan and Singapore is reported to have made Taiwan and Singapore significant factors

in the 1967 import picture: Taiwan for yarn and some yard goods, Singapore for yard goods and ready-made clothing.

Given a continuation of the Soeharto government, one may assume that the major suppliers will be Japan and Hong Kong, with Taiwan and Singapore also sharing. Each of these countries will be "political exporters," but in somewhat different ways. It is likely that Japanese textile exports to Indonesia will be financed largely through some form of government credit, particularly in 1968 and 1969. Exports from Hong Kong, Taiwan and Singapore probably will be on a private financing basis, and may well depend on how they came out with their B.E. Credit exports in 1967.

Two major factors now appear important for textile import policy in 1968: (1) the size of the stock of imported textiles already in Indonesia after the Lebaran period of early January, 1968; and (2) the tariff/credit policy of the Government of Indonesia in 1968. With respect to the first, the Directorate General of the Textile Industry estimated the stock of yard goods at the end of 1967 at 107 million meters (Appendix Table B-6). This is about one-seventh of the estimated consumption in 1967. Given the method of converting domestic yarn consumption to meters and of converting U.S. dollar F.O.B. imports to meters, one should use the estimates with extreme caution. With respect to tariff/credit policy, one may assume that the B.E. Credit System will be modified or eliminated after the late-1967 early January-1968 run on foreign exchange. It is my personal view that the sharp increase in the B.E. rates, particularly B.E. Umum (the "freest market rate") was the result of efforts by the textile importers to "cover" the reported credit imports of about U.S. \$60 million. It is my understanding that late December or early January was the last period for paying for the imports. It may be argued, however, that some of the importers did not in fact "cover" their commitments. This is true if such importers were Chinese who were in some way also associated with the exporters in Hong Kong, Taiwan, and Singapore. Such "family" relationships probably meant that the Indonesian importer would not buy foreign exchange if the price in rupiahs was considered excessive. They could postpone payment until 1968, relying on some combination of stabilization or even decline in the B.E. Umum rate and an increase in the price of textiles in terms of rupiahs in Indonesia.

Lacking definite information about either the extent of textile stocks in Indonesia after Lebaran or the amount of credit still outstanding, it will be difficult for the Government of Indon-

esia to forecast the effect of changes in either import duties or the B.E. Credit System. I shall discuss the possible alternatives in the section on Policy Problems and Recommendations. Since Japan is expected to be one of the largest contributors to the foreign exchange credit pool of U.S. \$325 million being requested by the Government of Indonesia for 1968, it is to be expected that it will have a strong interest in the textile import plans of Indonesia for 1968.

"Lebaran" as a Factor in the Indonesian Textile Market

The industrialized countries are almost all in the temperate climate zones and so have distinct "seasons." This makes for seasonal variation in the textile markets, and this in Christian countries is re-inforced by Christmas shopping and Easter shopping. Indonesia is in the tropics and so does not have great temperature variations to affect the textile market. It is, however, a Moslem country, in the sense that about 90% of the population belong to the Moslem religion. In Indonesia the end of the fasting month is a holiday period called "Lebaran." It is traditional for the Moslem population to buy new clothes for Lebaran, to visit relatives and friends, and to have family feasts or celebrations. As a result of the traditions associated with Lebaran, the purchase of textiles for "final consumption" is done primarily in the few weeks preceding Lebaran. I do not know the percentage of annual sales concentrated in this period, but I believe it is more than 50%, and may be as high as 75%. It is asserted that most of the textile retailers are Chinese, and that they take advantage of the Lebaran season and increase the prices of textiles and food. I have heard rather frequently that the price increases may be from 50 to 100%.

Lebaran came shortly after the New Year for 1968, and there were sharp increases recorded in the prices of textiles and food, particularly rice. To what extent the price increases, particularly for rice, reflected standard Lebaran practice, to what extent they reflected a real shortage of rice, particularly in Djakarta, and to what extent they were inspired by political/economic considerations probably will never be known. What is important, however, is the fact that for perhaps the first three-quarters of 1968 effective demand for textiles in Indonesia is likely to be low. This, combined with the possibly large stock of imported textiles, is likely to bring about a continuation of the present depression for Indonesian textile

production. At the same time, it should provide a breathing spell for the Government of Indonesia to revise its textile policies.

A C C O U N T I N G P R A C T I C E S , C O S T S ,
M A R G I N S , A N D T A X E S I N T H E
I N D O N E S I A N T E X T I L E I N D U S T R Y .

Accounting Practices

Financial and cost accounting practices in Indonesia are derived from Dutch accounting, with some time lag. This is generally true for all but the foreign British and American firms. Dutch accounting and financial reporting in many respects is superior to British and American practice. In general, it is more detailed, and makes a distinction between "fiscal" and "financial" profit. Fiscal profit is the profit on which income taxes are computed, and financial profit is what the management/owners consider to have been realized. This distinction, of course, is made in British and American accounting, but not so explicitly in the Income Statement as in Dutch (and German) accounting. In general, fiscal profit is computed by using certain "actual expenditures" in the tax year for which "reserve accounts" are employed for financial accounting. Thus the expense for estimated bad debts, repair of fixed assets, management and employee bonuses, etc. used in computing financial profit would be credited to the appropriate reserve account. For tax purposes the entries would be reversed and the actual payments during the tax period are the expenses deductible for determining taxable income.

In making industry studies in Indonesia in 1959 and 1960 I followed the practice of requesting cost and financial statements from private enterprises, but not demanding such information. When I was doing work for the Government of Indonesia, as I did in 1960, I often was able to obtain extensive cost and financial data from the government enterprises. In 1959 and 1960 I never received either a cost statement or a financial statement from a private national enterprise, but I did from many private foreign enterprises.

In the present study of the Indonesian Textile Industry I followed my 1959-60 practice of requesting but not demanding cost and financial statements from the private national enterprises

we visited. The fact that the study was a joint Indonesian-U.S. Government project had the happy result that the representatives of the Directorate General of the Textile Industry who traveled with me alone and later with the KSA team requested cost and financial statements from nearly all the Central Government and Provincial Government enterprises visited. The government enterprises were most cooperative and helpful in providing cost and financial statements and in discussing their cost and financial problems. It is a pleasure to acknowledge their help. As in 1960, however, my hints concerning cost and financial data from private national firms produced no current statements. Many of the executives, however, spoke freely and frankly about their practices and problems; and so contributed substantially to our understanding, if not to our collection of documents.

In few industrial countries is cost accounting standardized, but it often is fairly standardized within a particular industry. In Indonesia I found no standardization at all in the textile industry, even among firms under the same ownership/control agency. Because of the lack of uniform costing methods, the task of reducing cost and profit data to even reasonably comparative form was time-consuming and frustrating. I believe, however, that I was successful in reconciling the data so as to bring out the general results and the policy implications. I obtained both cost and financial statements only from some of the government spinning mills and the three integrated spinning/weaving mills in Java. One of the integrated mills is the batik producers' cooperative mill in Medari, Central Java. For this mill I secured cost statements but not financial statements.

Profits in Spinning and Spinning/
Weaving Enterprises in 1966

Four government enterprises provided financial data for the year 1966. Two of the enterprises are spinning mills owned by the Provincial Government of Central Java, Tjilatjap and Djantra. Tjilatjap is the largest spinning mill in Indonesia, and Djantra is an old mill with a very bad location. Two of the enterprises are integrated spinning/weaving mills, Toxin at Tegal, Central Java, and Nebritex at Pasuruan, East Java. In Indonesia all government enterprises are set up as separate corporations and subject to the same income tax regulations as private firms. The data for 1966 are shown in Table 6.

Table 10

Income Statements for Four Indonesian Textile Enterprises

Year 1966

<u>Type and Name of Enterprise</u>	<u>Sales</u>	<u>(New Rupiahs)</u>		
		<u>Taxable Income</u>	<u>Income Tax</u>	<u>Profit after Income Tax</u>
<u>Spinning Mills:</u>				
Tjilatjap	98,688,475	30,112,712	17,992,628	12,120,084
Djantra (Sales estimated)	31,000,000	6,193,034	3,640,822	3,552,212
<u>Spinning/Weaving Mills:</u>				
Texin (Sales estimated)	60,000,000	34,539,250	20,628,550	13,910,700
Nebritex	51,793,714	33,381,512	19,933,907	13,447,605

The year 1966 was a relatively poor year for spinning enterprises because of the shortage of cotton during the first part of the year. Of the four mills listed in Table 6, only one had a profit estimate for 1967 at the time of my visit. This was Djantra, the least efficient of the four. It estimated its financial profit for 1967 as Rp. 5,123,464 compared with a financial profit of Rp. 6,193,034 in 1966. It is my impression that the other three mills will do much better in 1967 than in 1966.

In general, the integrated spinning/weaving enterprises secured more profit in relation to sales income than did the spinning mills. This suggests that the effect of taking cotton into cost at the rupiah price in effect at the time of the P.L. 480 contract and selling the yarn or cloth on the basis of the current B.B. rate for imported yarn or cloth produces very substantial "inflation profits." Although the Indonesian income tax rate is high for profits in excess of Rp. 1,000,000 (60%), there is still a "leakage" of at least 40% in favor of the government corporations and against the Ministry of Finance. The leakage is in fact more than 40% because the provincial government mills pay a sales commission to the provincial government "holding corporation" of 4% of sales, and apparently the central government mills pay at least 2%.

Sales, Costs, and Profits of
Three Spinning Mills--1967

At two of the government spinning mills I was able to secure income statements for the month of October, 1967, and for a third for the third quarter. I attempted to convert the data to comparative form by: (1) valuing the actual output for the period at the current prices for yarn, and (2) by using the monthly average figures for the mill reporting for the third quarter (Djantra). The results are shown in Table 11. In preparing Table 11 I show the "cash costs" of production under two groups, cotton, and conversion costs. The government enterprises in Indonesia use a category of "indirect cost" called "Beban Sosial." This consists chiefly of payments in kind, chiefly rice, but also food and drink at the plant, medical care, pension provisions, the Lebaran bonus, including clothing, etc. Depreciation is shown separately to bring out the effect of the age of the mill (Djantra is, for practical purposes, fully depreciated, half of Tjilatjap is fully-depreciated, and Lawang is a new plant). The data at the bottom of Table 11 express revenue and cotton in terms of a bale of cotton used, and show the percentage of rice in the total rupiah value of social cost. It will be noted that the central government mill at Lawang had much lower "social cost" in proportion to total cash conversion cost than did the two provincial government mills. I did not visit Lawang, so cannot explain the difference.

Cost and Output Comparisons for
Three Integrated Mills

Tables 12 and 13 were prepared to illustrate the differing accounting problems and effects when integrated mills have differing degrees of "balance of facilities" and of "product mix." An integrated mill is said to be "out of balance" if it is able to produce more product in one process than it uses in a subsequent process. The product mix differs if the final products of the mills are not the same. The three mills compared in Tables 12 and 13 are the batik cooperative mill, G.K.B.I. at Medari, the joint Central Government/British mill Nebritex at Pasuruan, and the provincial government of Central Java mill Texin at Tegal. The G.K.B.I. mill is the best balanced of the three, in the sense that it was designed so that it has just enough looms to handle the average output of the spinning mill, but the bleaching plant was designed to not only bleach all the output of the looms but the additional output of two

Table 11

<u>Profit Statement for Three Spinning Mills</u> <u>Using Current Sales Value of Production</u> (000 New Rupiahs)			
	<u>Tjilatjap</u> <u>October,</u> <u>1967</u>	<u>Djantra</u> <u>Third</u> <u>Quarter</u>	<u>Lawang</u> <u>October,</u> <u>1967</u>
Revenue			
Sales value of yarn prod.	58,166	9,189	11,862
Sales of waste prod.	410	130	118
Other	- -	230	- -
Total	<u>58,576</u>	<u>9,749</u>	<u>11,970</u>
Cash Costs of Prod.			
Cotton	<u>40,483</u>	<u>5,705</u>	<u>6,028</u>
Conversion cost:			
Social costs, chiefly paid in kind	4,664	1,541	182
Other	<u>7,351</u>	<u>1,321</u>	<u>1,645</u>
Total Cash Conversion Cost	<u>12,018</u>	<u>2,862</u>	<u>1,827</u>
Total Cash Cost	<u>52,501</u>	<u>8,567</u>	<u>7,855</u>
Cash Margin	6,075	1,182	4,115
Depreciation	<u>422</u>	<u>9</u>	<u>1,037</u>
Operating Profit before management fee and taxes	<u>5,653</u>	<u>1,171</u>	<u>3,078</u>
Approximate no. of bales of cotton used	1,980	450	413
Average revenue per bale of cotton used	29,583	21,665	29,000
Average cost per bale of cotton used	20,450	12,650	14,600
Rice as a % of social cost	60%	50%	43%

Table 12

Physical Production Data for Three Integrated Spinning/Weaving/Finishing Mills - October or November, 1967

	GKBI	Nebritex	Texin
	<u>Oct., 1967</u>	Four weeks ending <u>4/11/67</u>	<u>Nov., 1967</u>
<u>Physical Production Data:</u>			
Cotton used in spinning in kg.	<u>101,788</u>	<u>167,053</u>	<u>155,515</u>
Yarn produced in spinning in kg.	88,511	152,800	135,231
Yarn transferred to weaving dept. in kg.	<u>60,538</u>	<u>52,084</u>	<u>135,231</u>
Surplus yarn produced over weaving use in kg.	<u>27,973</u>	<u>100,726</u>	<u>- - -</u>
Cloth woven:			
in meters			793,128
in yards	537,438	408,829	
Cloth finished:			
Bleached - yds.	<u>395,551</u>	- - - -	
Cloth dyed as black jeans - meters		<u>- - - -</u>	<u>298,790</u>
Cloth produced and to be sold as gray goods:			
in meters			494,338
in yards	- - -	408,829	
Apparent increase in inventory of unbleached cloth - in yards	<u>141,887</u>		

Table 13

Process Cost/Flow Sheets (In New Rupiahs)
For Three Integrated Indonesian Textile Mills
October or November, 1967

Item No.	Explanation	G. K. B. I. (Month of Oct., 1967)		
		Spinning	Weaving	Bleaching
1	Output in Units	<u>88,511kg.</u> Rp.	<u>537,438yd.</u> Rp.	<u>395,551yd.</u> Rp.
2	Raw Cotton Cost	<u>4,578,139</u>		
3	Cost Transferred from Prior Process		<u>5,656,990</u>	<u>6,902,374</u>
	Conversion Cost in this Process:			
4	Social Cost, Chiefly in kind	1,323,930	1,618,839	347,320
5	Other Cash Costs	2,007,500	2,025,150	644,211
6	Depreciation	<u>149,300</u>	<u>77,316</u>	<u>39,991</u>
7	Total Conversion Cost	<u>3,480,730</u>	<u>3,721,313</u>	<u>1,021,522</u>
8	Conversion Cost Plus Material Cost	8,058,869	9,378,303	7,933,896
	Cost Transferred to:			
9	Next Process	<u>5,656,990</u>	<u>6,902,373</u>	
10	Finished Goods			<u>7,933,896</u>
11	Change in Inventory	<u>2,401,879</u>	<u>2,473,929</u>	

Unit Costs:

Cost per kg. of Yarn Produced:

Raw Cotton	51.73
Conversion Cost	<u>39.32</u>
Total	<u>91.05</u>

Cost per Yard or Meter of Cloth Produced:

Yarn	10.52
Weaving	<u>6.92</u>
Total	<u>17.44</u>

Cost per Yard or Meter of Bleaching or Dyeing

Cloth Bleaching/Dyeing	17.45
Total	<u>2.60</u>
	<u>20.05</u>

N E B R I T E X
(4 week end 4/11/67)

<u>Spinning</u>	<u>Weaving</u>
<u>152,800kg.</u>	<u>408,829yd.</u>
Rp.	Rp.

6,039,470

3,667,521

776,159

1,315,330

3,440,340

1,825,413

22,663

10,000

4,439,162

3,150,823

10,478,632

6,818,343

3,667,521

6,818,343

6,811,111

39.52
29.05
68.57

8.97
7.71
16.68

T E X I N
(Month of Nov., 1967)

<u>Spinning</u>	<u>Weaving</u>	<u>Dyeing</u>
<u>135,231kg.</u>	<u>739,128M</u>	<u>119,394M</u>
Rp.	Rp.	Rp.

7,825,758

12,131,001 2,761,801

769,697

569,933

N.A. #

1,716,553

6,317,769

N.A.

N.A.

N.A.

N.A.

2,486,250

6,887,702

1,255,688

10,312,008

19,618,703

4,017,189

12,131,001

2,761,801

4,017,189

(1,818,993) 16,256,102

57.87
17.65
75.52

15.29
8.68
23.97

18.49
8.41
26.90

other small weaving mills of the batik cooperative. It also has the least complicated product mix in that it produces for practical purposes just one width of cambric, for which it spins one count of yarn for the warp and another for the weft. The Nebritex mill is the most unbalanced of the three, having much more spinning capacity than it has weaving capacity. It differs from the other two mills in having no finishing facilities for either bleaching or dyeing. The mill at Texin was originally designed by the Dutch to produce a cheap cloth called "black yeans" for the farmers. This product is dyed but not bleached. The mill now produces chiefly cambric for the batik industry. Both Texin and Nebritex have old looms, and they are a mixture of single width and double width looms. Texin produced six different kinds of cloth in November, requiring three different counts of yarn. Only one kind of cloth, 5% of the output, was dyed. In the four-week period ended November 4, 1967 the mill at Pasuruan produced three different counts of yarn in two different forms, cones and hanks, and produced four different grades of cloth, none of the same width, and two kinds were each produced in two different widths. Two of the mills, G.K.B.I. and Nebritex, measure cloth in yards, and Texin measures it in meters.

Given the enormous variation in integration and product mix, any comparison between costs or output for the three mills is bound to be unsatisfactory. The comparison provided by Table 13 over-simplifies by using a common denominator of kilograms of weight for yarn and total yards or meters of cloth for weaving and finishing. Given the problems of reducing output to a common denominator in each process, the unit cost data provided at the bottom of Table 13 indicate the importance of the cost of cotton, and general variations in efficiency of similar processes in terms of the conversion cost per unit. Although each spinning mill produced a different mix of yarn, Nebritex and Texin produced chiefly 20S count and G.K.B.I. 5/9 of 30S and 4/9 of 36S yarn.

For those readers not familiar with process manufacturing and process costing, it is conventional to have the cost statement provide separate data for each process employed. This usually is done by providing a separate column for each process, and to arrange them in the order in which the material moves, i.e. the first process in the first column on the left and the final process in the last column on the right. In Table 13

two of the plants have three separate processes and one has two. The first line of figures under the column heading shows the units of output during the period for that process. The second line shows the cost of raw material transferred into the process during the month. For easier understanding I have put the raw cotton cost of the spinning department on the second line and the third line shows the cost transferred into weaving and finishing during the period. Thus if less yarn is transferred to weaving than is produced in the spinning department, the amount of yarn cost transferred to weaving for item 3 will be less than the total cost of yarn produced as shown by item 8. In effect, the amount of item 9 for spinning is the amount for item 3 for weaving; and the amount of item 9 for weaving is, in turn, the amount of item 3 for finishing. For a particular mill, in effect, there should be as many different sets of two or three columns as there are separate products produced in each process. Every plant involved has some variation of this general system.

A final word is in order about the theory of inventory movement employed in constructing Table 13. The inventory theory is called last-in-first-out or LIFO. All three plants appeared to use this method, and it is appropriate for their situation. I shall have more to say about an extension of the LIFO theory in the policy recommendations concerning possible changes in the income tax regulations.

Income Tax Rates and Regulations
in Indonesia

Indonesia uses a graduated income tax structure for corporations, but the rate structure appears to have been designed for a time when the price level was much lower than it has been for many years. The structure is reported to be as follows, based on income subject to corporate income tax (company tax):

Taxable Income Bracket	Tax Rate
1 to 10,000	20%
10,000 to 40,000	30%
40,000 to 100,000	40%
100,000 to 200,000	45%
200,000 to 500,000	50%
500,000 to 1,000,000	55%
Over 1,000,000	60%

In sum, for firms with taxable income in excess of Rp. 1,000,000, the first million is taxed at 50.5% and the rest at 60%. In terms of attracting foreign investment to the textile industry, the Indonesian corporation tax rate is very high, and the exist-

ing accounting regulations do not recognize the factor of inflation with respect to the valuation of inventories or of depreciable assets for the purpose of computing depreciation for tax purposes.

Formula for Sharing After-Tax Profit
for Province of Central Java Enterprises

The textile mills under the ownership of the Provincial Government of Central Java reported the following formula for the distribution of annual profit after income tax:

20% to the General Reserve of the Enterprise

12% to the Employees of the Enterprise

55% to the Provincial Government for its
General Fund

3% to the Provincial Government for Pay-
ment of the Dutch Government Claim for
Taken-over Assets

5% for Social Education use, Presumably by
the Enterprise

5% for Production Bonuses in the Enterprise

Time did not permit detailed enquiries concerning the basis for the formula, nor did I have time to find out what formulas are used by other provincial governments or by P.N. Sandang for the central government spinning mills.

In evaluating the above formula, one should keep in mind that a sales commission of about 4% of gross sales is paid to the provincial government agency which, in effect, serves as a holding company/sales agency for the textile mills.

RECOMMENDATIONS FOR
POLICY AND IMPLEMENTATION

Introduction

In developing recommendations for policy and its implementation I have assumed that there are two time periods involved, 1968 and the five-year plan period 1969-1973, and that the orderly development of the Indonesian Textile Industry is a common concern of all the countries participating in the proposed U.S. \$325 million aid program for 1968, and that the nations involved will continue to support Indonesia in developing and implementing the five-year development plan. Based on the foregoing, I shall divide the policy recommendations into the following three groups:

1. Those which appear to involve all the aid-giving countries as a group acting in concert with the Government of Indonesia.
2. Those which appear to involve only the relations between the Government of Indonesia and the U.S. Government with respect to the P.L. 480 cotton and rice agreements.
3. Those which appear to be strictly internal problems of the Government of Indonesia with respect to the textile industry.

This separation of policy issues into three groups does not imply that there is no overlap among the three. I shall attempt to make the overlapping issues as clear as possible.

1. Policy Recommendations Involving the
Government of Indonesia and the Aid-
Giving Countries

In this area I assume that the chief inter-government agencies having an interest in the textile industry are the International Monetary Fund and the World Bank. As I see it, these agencies require current and reliable statistics for the textile industry, particularly with respect to imports, domestic production, and prices. At the present time responsibility for providing statistics appears to be primarily with the Directorate General of the Textile Industry, with subsidiary roles for Bank Indonesia, Customs, and the Central Bureau of Statistics. The Directorate General does not appear to me to have a clearly defined set of responsibilities. Its present organization appears to be based primarily on the policies of the "guided economy" period, particularly those associated with the allocation of cotton and yarn, and the encouragement of the handicraft sector and the smaller units of the mechanical sector. The lines of authority of the Directorate General are not clear with respect to P.N. Sandang (the State corporation oper-

ating the central government spinning mills), P.N. Berdikari (the State trading corporation responsible for importing third-country processed yarn and selling it), the various provincial governments operating large textile mills, the Batik Producers' Cooperative operating the G.N.B.I. mill, and the joint Central Government/British mill at Pasuruan. As the section on Market Structure and Pricing Practices shows, there may be considerable "leakage" of rupiahs in favor of the government and private spinning mills and P.N. Berdikari. This affects the government budget and hence the stabilization program.

The fact that most of the new spinning mills were purchased from countries in the aid-giving group, and that at least three of the large mills are included in the Dutch claims, appears to me to give the aid-giving countries (hereafter called Consortium Group) an important financial interest in the contribution of the Indonesian Textile Industry to the foreign exchange position. If policy for the future expansion of the textile industry involves foreign investment, either in the form of mixed foreign/Indonesian firms or all-foreign firms, reliable and current statistics and clear and definite policy will be necessary.

To handle the various problems associated with the joint interests of the Government of Indonesia and the Consortium Group, I recommend the establishment of a Textile Development Authority. This should be a very small agency in terms of number of personnel. It should be concerned with major policy and administrative problems and with securing and publishing current and reliable statistics on the key indicators of the textile industry. I believe that the Textile Development Authority should have several foreign advisors, and that these advisors should be provided by some inter-government agency or Foundation. The foreign advisors should not be associated with any one of the foreign governments in the Consortium Group, and it seems to me that there would be great merit in recruiting the staff members in several countries having major textile industries or textile machinery industries. In addition to foreign advisors for the Textile Development Authority, there should be a small number of foreign advisors assigned to the Institute of Textile Technology at Bandung. It is important that the Institute work closely with the Textile Development Authority.

Number and Qualifications of Foreign Advisors

I suggest a minimum of five advisors for the Textile Development Authority and two for the Institute of Textile Technology.

Of the five assigned to the Textile Development Authority, two should work in Djakarta and one each in Bandung, West Java; Semarang, Central Java; and Surabaya, East Java (including Bali). One of the advisors in Djakarta should be concerned with general management problems and the other with economic and statistical problems. Each of the three advisors assigned to the provinces should be combined management/plant technicians with qualifications similar to those of the two KSA men associated with me in this study. One of the advisors at the Institute of Textile Technology should be concerned with the technical education functions of the Institute, and one concerned with the research and development functions.

The precise responsibilities of the Textile Development Authority will depend on the nature of the agreement between the Government of Indonesia and the U.S. Government with respect to P.L. 480 cotton and third-country processing agreements, and on the general Government of Indonesia policies for the future course of the development of the industry. I shall offer a series of recommendations concerning these matters and then return to the responsibilities of the Textile Development Authority in implementing these recommendations.

2. Recommendations Concerning the 1968 and Subsequent P.L. 480 Cotton and Rice Agreements

As I understand the situation, the general policy of the U.S. Government with respect to P.L. 480 sales is that they represent "standard commercial transaction." This is an understandable policy in terms of the past sensitivity of developing countries to "invasions of sovereignty" by foreign aid-giving nations. It is my strong personal view that the U.S. Government has actually hindered the economic development of Indonesia by not concerning itself with what happens to the surplus commodities after they reach Indonesia. It is my view also that past agreements have not protected the U.S. Government from the effects of devaluation in Indonesia, and that the current policy of treating sales to Indonesia as "sales for convertible foreign exchange under liberal credit terms" tends to disguise the real situation. This means that if Indonesia does not stabilize its economy and develop a substantial surplus of exports over current imports, it will be unable to pay either the low interest or the principal for P.L. 480 commodities. By the same reasoning, if Indonesia does not stabilize its economy and develop a substantial export surplus, it will be unable to complete payments on the existing long-term debts which it is attempting to re-schedule. Since these long-term

debts presumably include the unpaid balances of the Central Government spinning mills and the unpaid claims of the Dutch for taken-over textile enterprises, the Consortium Group has a strong interest in effective internal use of P.L. 480 commodities.

Given the present conception that P.L. 480 commodity sales obligates the Government of Indonesia to pay interest and principal based on the U.S. dollar value of the commodities at the time of purchase, the requirement that the Government of Indonesia deposit in a special account in Bank Indonesia the rupiah value of the purchase (plus relevant transportation costs) at the official rate of exchange at the date of purchase is reasonable. But it is reasonable only if inflation is assumed to be stopped or reduced to something like the real growth rate of the Indonesian economy. Is it sound policy to assume the achievement of something which all past experience suggests is impossible or at best extremely difficult to achieve? The question answers itself.

If the conditions under which the Government of Indonesia puts surplus commodities into the market virtually assures the continuation of inflationary and destabilizing pressures, would it not be sensible for both governments to cooperate to minimize such pressures?

In the section on Marketing Structure and Pricing Practices I explained how continued inflation produces "leakage" in the rupiahs actually received by the Ministry of Finance from the sale of cotton and third-country processed yarn. I implied but did not state explicitly that there may also be a "leakage" of current foreign exchange if the State trading company which contracts for third-country yarn processing does not make the best deal possible. Given these possibilities, I believe the P.L. 480 cotton agreement should go beyond the "standard commercial sale" philosophy and be concerned with maximizing the rupiah receipts of the Ministry of Finance from the use of the cotton and yarn, and with minimizing the possibility of excessive foreign exchange costs for third-country processing. I believe that an effective mechanism for achieving these objectives would be a Joint Review Board. In formulating this proposal I suggest the use of foreign consultants. If the recommendation for a Textile Development Authority is implemented, the foreign advisers could probably handle the work involved. If the proposal for a Textile Development Authority is not implemented, then the foreign consultants might be required only on an intermittent basis.

A Joint Review Board for the P.L. 480
Cotton Agreement

I believe the following provisions should be included in some way in the 1968 cotton agreement:

P R E A M B L E

The Government of Indonesia, as a part of its general program to stabilize its economy and to stimulate private enterprise and investment, and in particular to increase the production of cotton textiles and to improve employment and living conditions of workers in the textile industry, enters into this agreement with the United States Agency for International Development for the purchase of cotton. On its part the United States Agency for International Development, in furtherance of the objectives of the Government of Indonesia, will supply the quantity of cotton specified under the terms specified.

Here should be the conventional clauses concerning P.L. 480 cotton.

.. - ..

It is further mutually agreed that to implement the objectives set forth in the Preamble, a Joint Review Board is established with the following members and responsibilities:

A. Membership

For the Indonesian Government:

Chairman - General Achmad, Badan Urusan Logistik

Members - Representatives of:

Ministry of Finance

Bank Indonesia

Personal Staff of Acting President

For the United States Government:

Chairman - Mr. Stokes Tolbert, Director, U.S.A.I.D.
Mission to Indonesia

Members - Representatives of Program, Food for
Peace, Economics Section

B. Meetings

The Joint Review Board will meet at least quarterly, and more often if necessary. Regular meetings will be scheduled on or about the tenth day of May, August, November and February to review the progress towards the objectives of this agreement during the calendar quarters ended, respectively, March 31, June 30, September 30 and December 31.

C. Meetings and Agenda

The meetings of the Joint Review Board will be chaired by the Chairman of the Government of Indonesia representatives. The Chairman will appoint a recording secretary. In addition to

the regular quarterly meetings, special meetings may be requested by either party on ten days notice for a mutually convenient time and place.

The regular quarterly review meetings of the Joint Review Board will include consideration of the specific items listed below under Responsibilities and Related Procedures. It is understood, however, that the primary responsibility of the Board is to determine and attempt to deal with any difficulties in carrying out the broad objectives set forth in the Preamble to this agreement.

D. Responsibilities and Related Procedures

The following objectives and implementing procedures will be the responsibilities of the Board and the named cooperating agencies:

1.) The Program to Stabilize the Economy

It is the intention of both parties to this agreement to make available to the Ministry of Finance of the Government of Indonesia as soon as possible the proceeds from the regular commercial sale of the raw cotton and yarn acquired under the provisions of this agreement.

It is understood that the economic objectives of Indonesia may best be realized by the sale of cotton or yarn at rupiah prices slightly below the equivalent landed cost to private importers of such material. Price schedules, credit terms, and other related terms of sale will be developed by the Textile Development Authority (or if one is not established, by the Director General of the Ministry of Textiles and Handicrafts) for review and approval by the Joint Review Board. It is specifically agreed that the U. S. representatives on the Board may participate in the discussion of the terms of sale but will not be entitled to vote on this item. The vote will be the prerogative and responsibility of the representatives of the Government of Indonesia. The representatives of the Government of Indonesia may amend the proposals of the Director General of the Ministry of Textiles and Handicrafts.

The Joint Review Board is charged with the responsibility to determine that the conditions of sale and access to stocks of raw cotton are not less favorable for private spinning mills than for government spinning mills, and that conditions of sale and access to stocks of cotton yarn are not less favorable for private weaving and knitting enterprises than for government enterprises. To assure equal treatment, representatives of private and government enterprises may petition for hearings by the Board.

A special account will be established in Bank Indonesia and its branches in which the proceeds of the sale of cotton to private spinning mills and of yarn to private and government processors will be deposited in accordance with the conditions of sale adopted by the Board.

2.) The Program to Stimulate Private Enterprise and Investment and to Increase the Production of Cotton Textiles and to Improve Employment and Living Conditions in the Textile Industry

Recognizing that the Joint Review Board will require a substantial amount of financial and statistical data for the effective discharge of its responsibilities, it is decided that the necessary steps will be taken to provide the following information which is to be sent to each Joint Board Member with the call to the regular quarterly meeting:

- a) The Textile Development Authority (or the Director General of Textiles and Handicrafts) will maintain or secure such records of raw cotton inventories and consumption as necessary to provide a report for the quarter under review and a forecast for the coming quarter of cotton stocks, receipts, and consumption at each spinning mill and for the free stocks maintained outside mill gudangs.
- b) The Textile Development Authority (or the Director General of Textiles and Handicrafts) will maintain or secure such records of yarn production, shipments, and inventory by yarn count for each spinning mill as will enable the Joint Review Board to appraise the adequacy of supply and the progress towards an orderly market in yarn and towards the full employment of domestic weaving and knitting facilities.
- c) The Agency or Agencies delegated responsibility by the Government of Indonesia for contracting for yarn processing, receiving, warehousing, and distributing such yarn will provide quarterly reports to the Textile Development Authority (or to the Director General of the Ministry of Textiles and Handicrafts) for consolidation with the yarn statistics of the domestic spinning mills for the quarterly report to the Joint Review Board.
- d) The Agency or Agencies delegated responsibility by the Government of Indonesia for contracting for yarn processing or textile processing of cotton provided under this agreement will provide the joint chairman of the Review Board with copies of all notices of tender and of all processing agreements signed.

In accordance with the provisions of Section 1 above, the Agency or Agencies delegated the responsibility for procuring and distributing yarn or finished textiles from cotton secured under this agreement will not have authority to make direct payments to processors or to deposit proceeds of the sale of such yarn or textiles in its own account. All such payments and deposits will be through the special account established in the Bank Indonesia and in accordance with procedures developed by Bank Indonesia, the Ministry of Finance, and the contracting agency or agencies. Copies of these procedures will be filed with the Joint Review Board.

3.) Employment of Consultants

In implementing the objectives of this agreement, the Joint Review Board may employ such consultants and authorize such studies of the Textile Industry as it determines to be necessary for the orderly development of the

industry and for the Board's understanding of the problems of the industry. The costs of such consultants and studies will be borne by the parties to this agreement as mutually determined.

Explanation of the Key Features of the
Review Board Proposal

The Joint Review Board proposal was developed after I attended the first negotiating meeting for the 1968 cotton agreement and was presented to Mr. Stokes W. Tolbert, Director of the U.S. A.T.D. Mission to Indonesia in a memorandum dated December 24, 1967. The extensive financial data subsequently secured in Central Java in January re-inforced early December findings in Djakarta and Bandung concerning possible "leakage" in the handling of cotton and yarn imports and sales. The plugging of these leaks should be a high priority of the Central Government top economic policy group. The Review Board is intended as a mechanism to provide for the quick and accurate reporting of key statistics and consideration of their implications by both governments.

The proposal, in my view, does not constitute an improper invasion of sovereignty of the Government of Indonesia, for it does not give the U.S. Government representatives on the Board a vote on any policy issues. I believe the U.S. Government representatives should have an opportunity to be consulted about policies affecting P.L. 480 cotton and yarn, and the Review Board procedure seems a workable device for this. It certainly is desirable that consultation occur in advance of policy decisions and not long after they are made.

The requirement of better statistics on key components of the textile market is based on the 1967 experience with textile imports, particularly those on credit. It seems clear that the imports were much larger than the top economic policy group intended or even knew about, and that this seriously affected the B.E. Unum "run-up" at the end of December and early January. Better knowledge of the inventory position of cotton, yarn, and imported textiles obviously is required for critical policy decisions. These not only involve the Indonesian Government and the U.S. Government, but the Consortium Group countries, International Monetary Fund and the World Bank.

The Government Textile Enterprises
and the Rice Problem

During the short period I was in Indonesia the rice problem appeared to be the most critical political and economic issue. Both private and government enterprises in Indonesia have a "paternalistic" employment policy somewhat more extensive than

is found in other developing countries. The extent of paternalism was extended and expanded during the hyper-inflation of the "guided economy" period. Since the textile industry is the largest domestic manufacturing industry in Indonesia in terms of both number of employees and value of product, and since the various government mills completely dominate the spinning industry and account for a very large fraction of the weaving industry employment, the practice of providing free or subsidized rice to all employees of government textile mills contributes substantially to the inelastic demand for rice. Just how serious this is is indicated by the rice allowance of one of the provincial government mills:

<u>Rice Allowment per Month</u>	
Each worker	20kg.
Spouse (limit of one)	8kg.
Each child under 21 and not employed	8kg.
Limit per family	68kg.

Many plants have no limit on the number of children for which rice is provided. It was reported that many families "adopt" young children just to get the rice. In general, every government textile plant we visited had from 1,000 to 1,500 employees. Some 15 spinning mills and five or six large weaving mills account for a large work force---say at least 20,000. If they distribute just 50 kg. of rice a month they require 1,000,000 kg. or 1,000 metric tons a month. The fact that the government textile plants distribute rice certainly puts pressure on nearby private enterprises to do the same, although our small sample suggests that they have resisted the pressure.

In Table 11 I showed that rice alone comprised from 43 to 63% of the "social cost," and that this item alone was over 50% of total conversion cost for one mill and 40% for another. Certainly the distribution of rice to government employees discriminates against private enterprises, and it puts a very high floor under the quantity of rice "required" by Indonesia. What is perhaps more serious for the future, rice distribution appears to discourage family size limitation. I suspect that a sample census will show that Indonesia now has a net population increase of nearly 3% a year. Government policy which, in effect, asks foreign friends to provide a fixed quantity of rice per family for a rapidly increasing population is out of touch with reality and must be changed. Making rice (and textiles and sugar and soap and kerosene) commodities which all consumers must buy will go a long way toward reducing Indonesia's present almost total dependency on foreign assistance

for virtually all of its development capital requirements and a very large fraction of its current consumption requirements for rice and textiles.

The importance of rice and of family planning is a major reason for my strong recommendation that a Textile Development Authority be established to formulate and implement basic economic policy in the textile industry. Family planning could be expanded substantially in Indonesia by making use of the present free medical services of the government mill polyclinics and hospitals. Some idea of the urgency of this is provided by the Government cement plant at Gresik, which reported to me an average of 27 babies a month in the plant hospital for the past two years for a work force of 1,500. I see no reason to believe that this experience was not repeated in the government textile mills.

Indonesia must and will plan for the five years after the expected stabilization of the economy in 1968. Rice and textiles are perhaps the two most critical commodities in the present and for the immediate future, and good statistics and sound policy based on facts and reality are urgently required. To have a cotton agreement which ignores what happens to the rupiahs generated by the sale of the cotton is unwise policy. It appears equally unwise to supply rice without looking at the way the rice is used, particularly if the use guarantees that the crisis the next year will be as great or greater than the current crisis.

Cotton Required in 1968 for Indonesian Spinning Mills

Although the determination of the amount of cotton likely to be required by the spinning mills in Indonesia in 1968 was a part of my original assignment, this task was transferred to the KSA team. By the time of the first negotiating session in late December I estimated the 1968 requirement as not much more than 125,000 bales. The reader is referred to the KSA report for a more precise estimate, broken down by individual mills. The KSA report will also deal with the important question of cotton quality inspection and with the problems of getting the proper staple lengths to each mill in order to enable it to produce the count of yarn planned for the mill in relation to its equipment.

Obstacles to the Full Utilization of Production Capacity of the Indonesian Spinning Mills

This is in part a technical problem to be covered in the KSA report, and in a part a financial/economic problem. With respect to the latter, we were unable to obtain the data required for a specific answer, but I can outline the nature of the information required and the decision model to be employed. At only one plant were we able to get a reasonably complete list of parts required to replace those lost, stolen, or damaged during construction. This list did not have prices attached. In recommending three provincial advisors for the Textile Development Authority we have in mind that one of the first tasks for each advisor will be to develop a complete parts list for each spinning mill and secure prices and delivery dates. With this information a priority schedule for completing the Central Government spinning mills can be developed. The priority schedule must take into account the count of yarn each mill can and should produce.

In general, the decision model on which the KSA team and I agree is that no new spinning mills should be planned until the existing mills are completed to designed capacity and are being operated as efficiently as possible. We are convinced that the foreign exchange required to complete the mills will be much less than that required to secure equivalent production capacity with new mills. The KSA report will indicate the equivalent number of new 30,000 mills involved in completing the existing mills. The KSA report will also make recommendations with respect to transferring certain major pieces of equipment from some of the existing mills to other

mills which require such equipment. Such surplus equipment arises when a mill is to be used for yarn of a higher count than that originally contemplated in designing the mill. Higher count yarn means that the spindles run slower and process less cotton, hence equipment prior to the spindles may have more capacity than is needed.

In developing priorities in 1968 and probably in 1969, the decision model should include a "time horizon" or "minimum pay-out period in years or months" for the foreign exchange component of the spare parts. If the time horizon is short, as it is likely to be in 1968, the foreign exchange required for third-country processing may be much less than the foreign exchange required to secure the production capacity for the equivalent amount of yarn. Assuming P.L. 480 cotton for both domestic yarn and third-country processing, the foreign exchange for cotton will be the same whether the cotton is processed in Indonesia or in a third country.

The development of data for proper decisions on when to order spare parts will be a time-consuming operation. It is also so important that the results probably will pay for the foreign advisors required. It must be emphasized that all the spare parts required to bring the spinning mills to designed capacity will require foreign exchange. The parts cannot be made in Indonesia. As I shall point out in discussions of the spare parts problem for weaving, Indonesian or mill machine shops can handle most of the repair and renovation work for the weaving plants.

Yarn Requirements in 1968 to Supplement Domestic Production

Time in Indonesia did not permit us to estimate either the stock of yarn at the end of 1967 or the probable consumption. We did find one or two instances of speculative hoarding of yarn by provincial government spinning mills, but all of the central government spinning mills seemed to be selling their yarn as fast as they produced it.

Appendix Table B-5 shows the estimates of the Directorate General of the Textile Industry concerning yarn for 1967 and 1968. In general, I am inclined to believe that the stock of yarn at the end of 1967 was quite a bit more than 4,000 bales. The estimate of domestic production in 1967 does not appear out of line with our findings, but the estimate of 165,000 bales of domestic production in 1968 appears to be on the high side. The KSA report probably will deal with this question. The

estimate of domestic consumption for 1968 is 360,000 bales in relation to estimated consumption of 176,000 in 1967. This appears to be the basis for the first request of 150,000 bales of cotton for domestic processing and a like amount for third-country processing. The Directorate General qualified its yarn consumption estimate for 1968 by stating that it is based on the assumption of stabilizing the economy and a much higher level of consumer purchasing power than in prior years.

I am inclined to believe that successful stabilization in 1968 will mean continued deflationary pressures and not a sharp increase in purchasing power. As I shall explain in more detail later, I believe the stock of imported textiles at the end of 1968 was larger than that estimated by the Directorate General, and that the domestic weaving and knitting mills will continue to experience marketing difficulties in 1968 similar to those experienced in the last half of 1967.

In light of the foregoing, I urge extreme caution in making a firm commitment for P.L. 480 cotton for third-country processing at the same time that the agreement is made for cotton for the domestic spinning mills. It should not be necessary to make commitment for third-country processing until after the final decision by the Consortium Group on the total amount of credits to be made available in 1968. If an early decision must be made, I would suggest not less than 50,000 bales of cotton, and certainly not more than 100,000. There is less danger in under-buying yarn than in under-buying raw cotton.

3. Internal Policy with Respect to Protecting the Domestic Weaving and Knitting Industry

The domestic weavers and knitters, individually and through the Indonesian Textile Manufacturers' Association, appear to be urging a high protective tariff as a solution to the present depressed condition of the domestic manufacturing industry. I have great reservations about this proposal.

Can the Domestic Weaving and Knitting Industry be Protected by High Import Duties?

For 1968 at least, I believe the answer is No! To protect domestic producers with a high schedule of import duties obviously requires at least two conditions: (1) that the imports are not already in the country, and (2) that the quality of the domestic product is approximately the same as that of the imported products. A third requirement may be added--that

the import regulations clearly specify that the import duties apply to the specific products to be protected.

In terms of long-run equity, the small private weavers in particular have a strong case for protection. This is that the present policy of completely prohibiting the importation of batik design prints and checked and floral design sarung material tends to protect only the large government weaving mills and a few of the large private weaving mills with an established position in the sarung market. If there is a substantial case in equity for extending similar protection to the producers of greygoods and knitwear, it runs against the facts at the beginning of 1968. There is a very substantial volume of imported textiles in inventory, and even if the domestic weaving and knitting industry operated at capacity (one shift for handlooms and two shifts for mechanical looms and knitting enterprises), the output would be about one-half of the domestic textile requirements.

Two things appear essential to protect the domestic weavers and knitters: (1) to determine precisely the products they can and should produce, and (2) determine the cost of production of such goods of satisfactory quality. The KSA report will deal at some length with the quality of domestic weaving. I shall only assert that it is very low indeed. Being of such low quality, it can only be protected by very high import duties or total prohibition of imports. The latter is sensible if, and only if, the weaving industry can be rationalized so that it concentrates on a few products for which it can satisfy the entire domestic demand. The quality of current production is much lower than it needs to be in terms of the quality of yarn and the condition of the equipment. The KSA report will deal with this problem. The quality improvement problem for both yarn and manufactured goods was an important consideration in my recommendation for three foreign consultants in the three provinces of Java. Six would be better, for this would permit one in each province to work on spinning and the other to work with the private mills on weaving, finishing and knitting.

In October the Indonesian Textile Manufacturers' Association presented to the Ministry of Textiles a set of cost computations designed to show why the domestic sales tax on the weaving industry and the knitting industry should be eliminated. This action was taken by the Ministry. The computations also

were designed to show that even after the elimination of the manufacturer's sales tax the weavers suffered a cost disadvantage compared to the landed cost plus import duty of competitive imported products. I believe that the cost data are substantially inaccurate and greatly overstate the actual cost experience for every component. I stated this to representatives of the Association and I believe they agreed with me. One of them offered to provide more accurate cost data, but the press of events and time at the end of my stay prevented me from securing the data.

Given more time, one could develop better cost data, but this is not the most important consideration. The important consideration is quality. Closely related to this is the fragmentation of the private weaving and knitting industry shown by Tables 2 and 5. In order to deal with the problems of small size and poor quality, a long-term policy of consolidating small inefficient units into larger and more efficient units must be developed. Let us look now at some of the ways in which such a policy might be implemented.

Helping the Small Weaving and Knitting Enterprises to Help Themselves

The first and perhaps most important suggestion I have for dealing with this question is with respect to working capital. The combination of a ceiling on selling prices set by existing imports and rising costs of yarn and labor has substantially reduced the "real working capital" of the private mills. The most obvious way to ease the working capital situation is for the entire supply of yarn from the domestic government spinning mills and the State trading companies to be sold on credit at a low interest rate. The Government of Indonesia is getting cotton from the United States at 2% interest and the government spinning mills do not pay any interest, to my knowledge, and pay for cotton only as used. Why not extend the same credit terms to the private weavers and knitters?

The second suggestion is to change the accounting regulations for all manufacturing enterprises so as to permit the valuation of inventories at replacement cost and not treat the revaluation as taxable income. Related to this is the suggestion that all manufacturing enterprises be allowed to revalue their depreciable assets to something like one-half replacement cost in foreign exchange. Depreciation for tax purposes should then be based on the official B.E. rate for imported machinery and any upward revaluation should, like the revalu-

ation of inventories, not be treated as taxable income.

A third suggestion is to schedule all government purchases of cloth for the military and civil services so that it is allotted to the private mills on an equitable basis. This would provide a definite and scheduled volume of output for the private mills most in need of help, and at the same time provide pressure to improve quality. Quality tests should be made by the Institute of Textile Technology.

A fourth suggestion is to provide tax and other incentives for several small inefficient enterprises to combine into a larger and more efficient enterprise. Related to this should be a planning program for more sizing equipment and more and better finishing equipment. The technical aspects of this probably will be covered in the KSA report.

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A Final Word Concerning a Textile Development Authority

It is obvious by now that the three areas of policy and policy implementation overlap. There should be a single coordinating agency for developing policy for the Indonesian Textile Industry, particularly for the five-year plan, budgeting foreign exchange, and developing import policy. I believe a small group of highly-qualified experts can best do this job, including developing good and current statistics.

In recommending a Textile Development Authority in the first part of the Policy section I suggested that the foreign advisors should not be provided by a single foreign government. I now want to suggest that these might well be paid directly by the Government of Indonesia. Seven or even ten good foreign advisors would almost certainly save the Government of Indonesia far more in foreign exchange than they would cost. In addition to the money aspect, they would, in all probability, greatly improve the present low morale of all the enterprises with which they work. This would be particularly important for the key enterprise, the Institute of Textile Technology at Bandung.

Appendix Table A-1

Itinerary of Field Work
November 29 -- December 31, 1957

Wed. Nov. 29	Visited private weaving and knitting factory P.T. Oriental and central government spinning mill Senajan in Djakarta.
Thurs. Nov. 30	Visited large private knitting and garment factory P.T. Radjut Persodjo in Djakarta.
Fri. Dec. 1	Visited retail textile stalls at Pasar Senen in Djakarta.
Mon. Dec. 4	Courtesy call on Mr. Sanusi, Minister of Textiles and Handicrafts in Djakarta.
Tues. Dec. 5	By car of Directorate General of the Textile Industry to Bandung, West Java - accompanied by Drs. Gultom of the Industry Promotion Section of the Directorate General of the Textile Industry. Courtesy call on General Mashudi, Governor of the Province of West Java.
Wed. Dec. 6	Visited the Institute of Textile Technology in Bandung to discuss their needs for foreign technical advisory assistance and imported equipment and to obtain views on problems of industry in the Bandung area.
Thurs. Dec. 7	Visited central government spinning mill Tjipadung near Bandung. Visited provincial government weaving mill P.T. Pabrik Tenun Garut "Ampera I" at Garut, West Java.
Fri. Dec. 8	Visited weaving and knitting factory P. T. Bandung owned by Foundation of State Railway Employees. Visited private staple fibre spinning/weaving enterprise P.T. Wisma Cesaia.
Sat. Dec. 9	Visited private printing and finishing enterprise P.T. Sumber Gandang. Visited private handloom and mechanical loom weaving enterprise P.P. Tjinangga.
Mon. Dec. 10	Trip to Madjalaja near Bandung Visited provincial government warp preparation, finishing and hand screen printing "induk". Visited a small and new weaving plant. Visited a small handloom enterprise.
Tues. Dec. 11	Visited a machine shop owned by Foundation of State Railway Employees and used to produce spare parts for looms. Dinner with family of Governor Mashudi.
Wed. Dec. 12	Returned to Djakarta in car of Inspectorate of Industry of Province of West Java.
Thurs. Dec. 28	Visited central government spinning mill in Den Pasar, Bali.
Fri. Dec. 29	Visited Daerah government weaving mill P.T. Balitex. Visited handloom enterprise in Den Pasar.
Sat. Dec. 30	Visit handloom enterprise in Den Pasar using primitive harness looms.

Appendix Table A-2

Itinerary of Field Work with KSA TeamJanuary 8 -- January 23, 1968

- Mon. Jan. 8 Visited central government spinning mill Senajan in Djakarta
- Tues. Jan. 9 Visited private knitting and garment factory P.T. Radjut Persodjo in Djakarta.
- Wed. Jan. 10 By hired car to Bandung, West Java.
Visited Institute of Textile Technology at Bandung
- Thurs. Jan. 11 Visited central government spinning mills Tjipadang and Bendjara at Bandung.
Visited provincial government weaving mill P.T. Fabrik Tenan Garut "Ampora I" at Garut.
- Fri. Jan. 12 Visited weaving and knitting factory P.T. Bandung owned by Foundation of State Railroad Employees.
Visited private spinning/weaving enterprise of member of Textile Manufacturers' Association, P.T. Wisma Oesaha.
- Sat. Jan. 13 Trip to Madjalaja, near Bandung.
Visited provincial government warp preparation, finishing and hand screen printing "induk".
Visited a small private weaving mill
Visited a handloom enterprise
Visited largest mechanical loom enterprise operating on "toll basis" for a Chinese capitalist.
- Sun. Jan. 14 By car to Tegal, Central Java.
Spent evening with executives of provincial government spinning/weaving/dyeing enterprise Texin.
- Mond. Jan. 15 Visited plant of Texin and obtained cost data while KSA team studied technical operations.
By car to Tjilatjap, Central Java.
- Tues. Jan. 16 Visited provincial government spinning mill (largest in Indonesia) at Tjilatjap. Obtained cost and financial data and met with Director.
By car to Djogjakarta.
- Wed. Jan. 17 Visited integrated spinning/weaving/bleaching mill of C.K.B.I. (batik cooperative) at Madari near Djogjakarta. Obtained cost data while one KSA man made technical inspection of this plant and the other visited the central government spinning mill Setjang at Magelang.
- Thurs. Jan. 18 By car to Solo to visit provincial government finishing "induk", Infitex.
By car to Salatiga to visit a private weaving and roller printing enterprise.
- Fri. Jan. 19 By car to Semarang
Visited provincial government spinning mill Djantra in Semarang. Obtained cost and financial data while KSA team made technical inspection of mill.

Appendix Table A-2 (Continued)

- Sat. Jan. 20 By car to Pekalongan, Central Java
 Courtesy call on Bupati and Walai Kota
 Visited batik dyeing enterprise of local
 batik cooperative.
 Visited handloom and small mechanical loom enter-
 prise.
 Returned to Semarang by car.
- Sun. Jan. 21 By car to Tretes, East Java.
 Spent evening in conference with representative
 of provincial Inspectorate of Industry and two
 representatives of Directorate General of the
 Textile Industry.
- Mon. Jan. 22 Visited joint central government/British
 integrated spinning/weaving mill Hebritex at
 Pasuruan and left USA team to continue work
 in East Java and Bali.
 Visited Surabaya office of Hebritex to obtain
 cost and financial data.
 Visited central government cement plant at
 Gresik to arrange visit to a handloom enterprise
 in Gresik.
 Visited handloom enterprise in village of Gresik.
- Tues. Jan. 23 Returned to Djakarta by plane.

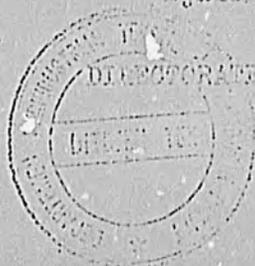
Appendix Table B-1

INDONESIA : Consumption of Raw Cotton by mills, estimated 1967
and Forecast 1968
(In terms of 500 lb's bales)

Name of Cotton Mill		Estimated 1967	Forecast 1968
1.	Pardede (private)	3,915	13,800
2.	Siantar (private)	310	500
3.	Palembang (central govt.)	-	3,300
4.	Sonajan (central govt.)	13,819	14,873
5.	Tjipadung (central govt.)	2,859	10,254
6.	Bandjaran (central govt.)	-	7,452
7.	Tebitiks (provincial govt.)	1,338	2,385
8.	Wisma Gecaba (private)	2,862	2,750
9.	Mekasi (central govt.)	-	2,190
10.	G.K.B.I. (private-cooperative)	5,856	12,162
11.	Torain (provincial govt.)	9,616	9,214
12.	Djantoe (provincial govt.)	6,256	6,256
13.	Seljong (central govt.)	5,240	3,927
14.	Tjilidjaj (provincial govt.)	25,972	27,020
15.	Grati (central govt.)	9,722	12,640
16.	Lawang (central govt.)	4,825	7,073
17.	Kebriken (central govt./British)	9,194	16,261
18.	Tekpati (central govt.)	2,272	3,775
19.	Kasa Husada (not known)	400	400
20.	Darbelat Indonesia (not known)	400	400
Total		193,759	161,436

* Present ownership

Djakarta, December 22, 1967



DIREKTORAT JENDERAL INDUSTRI TEKSTIL

DEPARTEMEN PERDAGANGAN

Appendix Table B-2

INDONESIA : Imports of Raw Cotton by Country of Origin
1963 - 1967 and forecast 1968
(In terms of 500 lb.'s bales)

Country of Origin	1963	1964	1965	1966	1967	Forecast 1968
1. U.S.A.	31.037	19.364	28.050	30.496	158.408	150.000
2. People's Rep. of China	-	-	14.045	-	-	-
3. Pakistan	-	-	14.929	4.686	-	-
4. Other Countries	16	-	-	-	-	-
T o t a l	31.055	19.364	57.024	35.182	158.408	150.000

Djakarta, December 22, 1967



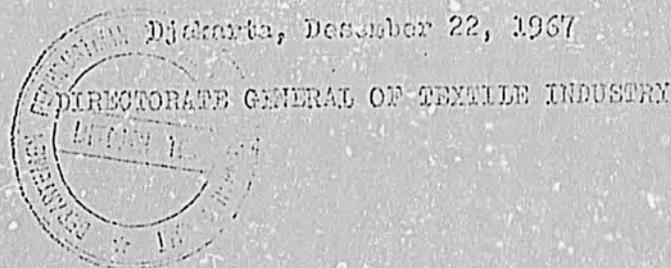
DIRECTORATE GENERAL OF TEXTILE INDUSTRY

Appendix Table B-3

INDONESIA : Supply and Distribution of Raw Cotton, estimated
C.Y. 1967 and forecast C.Y. 1968.

	Estimated 1967	Forecast 1968
	000 bales +)	000 bales +)
<u>Supply :</u>		
Beginning Stocks, Jan. 1 ^{st.}	59	59
Domestic Production	4	4
Imports	158	150
Total Supply	162	213
<u>Distribution :</u>		
Consumption	103	161
Export	-	-
Ending Stocks, Dec. 31 ^{st.}	59	52
Total Distribution	162	213

+) 500 lb. bales.



Appendix Table B-4

INDONESIA : Imports of Cotton Yarn (Including Staple fibres) by Country of Origin, 1963 - 1967 and forecast 1968, in terms of 400 lb. S bales.

Country of Origin	1963	1964	1965	1966	1967	Fore cast 1968
1. Hongkong	14,806	8,768	12,895	8,047		
2. Japan	13,635	177,826	4,538	136,487	14,000	
3. Peoples Rep. of China	88,226	135,052	17,431	139,585		
4. U.S.A.	204		771			
5. Mexico	7,970	567				
6. India	748	551				
7. U.S.S.R.	61					
8. Bulgaria	39					
9. Singapore	6					
10. Yugoslavia		22,583	13,239	4,829		
11. Czechoslovakia		699	1,821			
12. Pakistan			28,166	15,054		
13. Italy	61			7,987		
14. Philippines				1,309		
15. Manchuria			517			
16. Ghana		28				
17. France			83			
18. Swiss				33		
19. West Germany			6	34		
20. Belgium	6					
21. N. Korea			83			
22. Taiwan					38,478	
23. Country of Origin Unknown						265,000
	1125,762	145,578	1230,854	113,365	52,478	265,000

4) Imports from Hongkong and Japan



Djakarta, December 22, 1967

DIRECTORATE GENERAL OF TEXTILE INDUSTRY

Appendix Table B-5

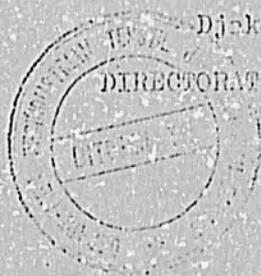
INDONESIA : Supply and Distribution of Cotton Yarn (Including Staple Fibers) Estimated C.Y. 1967 and Forecast C.Y. 1968.

	! Estimated C.Y. 1967	! Forecast C.Y. 1968
	! 000 bales +)	! 000 bales +)
<u>Supply :</u>	!	!
Beginning Stocks Jan. 1 st.	! 27	! 4
Domestic Production	! 100	! 165
Imports	! 53	! 200
Total Supply	! 180	! 369
<u>Distribution :</u>	!	!
Domestic Consumption	! 176	! 360
Export	! ..	! ..
Ending Stock on hand Dec. 31 st.	! 4	! 9
Total Distribution	! 180	! 369

+) 400 lb. s bales

Djakarta, Desember 22, 1967.

DIRECTORATE GENERAL OF TEXTILE INDUSTRY



Appendix Table B-6

INDONESIA : Supply and Distribution Table for Textiles (Cotton and Synthetics) estimated C.Y. 1967 and forecast C.Y. 1968.

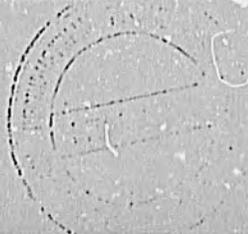
	! Estimated C.Y. 1967	! Forecast C.Y. 1968
	! million meter	! million Yards
<u>Supply</u> :	!	!
Beginning stocks Januari 1	! 99,5	! 107
Domestic production	! 225	! 450
Imports	! 511	! 300
Total Supply	! 835,5	! 857
<u>Distribution</u> :	!	!
Consumption	! 728	! 805
Exports	! 0,5	! 1
Ending stocks on hand Dec. 31 st	! 107	! 51
Total Distribution	! 835,5	! 857

Note :

1. Population in 1967 112 million
2. " " in 1968 115 million

Djakarta, December 26, 1967

DIRECTORATE GENERAL OF TEXTILE INDUSTRY



Appendix Table B-7

INDONESIA : Import of textile by country of Origin
 1963 - 1966 in terms of 1960 Eq.

Country of Origin	1963		1964		1965		1966	
	A	B	A	B	A	B	A	B
1. Hongkong	3,297	804	2,963	914	1,752	604	8,377	2,640
2. Japan	5,015	1,577	4,940	3,312	4,929	7,366	6,002	550
3. Peoples Rep of China	2,161	770	5,797	2,093	6,185	2,685	7,954	4,063
4. Russia	4,727	68	1,523	-	1,798	-	1,070	11
5. Mexico	5,413	-	103	-	1	-	-	-
6. India	194	817	530	1,113	914	508	91	472
7. U.S.A.	98	7	7	14	4,046	21	20	9
8. Yugoslavia	213	-	836	-	2	-	-	-
9. Pakistan	-	-	5	-	1,086	-	1,980	-
10. Singapore	61	96	20	-	-	-	154	10
11. Taiwan	139	-	5	-	-	-	77	-
12. Hanco	-	-	-	-	102	300	203	12
13. Nederland	1	-	4	-	292	-	89	-
14. Fed. Rep. of German Rep.	60	242	30	336	6	229	9	120
15. Hongkong	13	2	290	4	131	-	803	84
16. Bulgaria	36	-	23	-	8	-	4	-
17. Polandia	27	139	165	210	1,047	368	859	537
18. Czechoslovakia	171	10	1	-	6	32	3	-
19. Great Britain	-	4	-	4	-	2	-	3
20. South Korea	-	-	-	37	-	52	-	150
21. North Korea	-	-	-	32	-	34	-	55
22. Italy	-	4	-	27	-	28	-	30
23. Other Countries	62	13	114	40	75	77	109	123
Total	21,691	4,521	17,405	8,139	22,387	12,534	27,804	24,01

A. = Clothing Materials : Shirting, Sheeting, Cambrics, Printed, Velvet etc.
 B. = Other Textiles : Bias, Corda, Zanzibars lamp mantle, embroidered goods etc.

According to the Central Bureau of Statistic the textile imports 1963 - 1967 is as follow :

- 1963 : 218,6 million meters
- 1964 : 240,4 " "
- 1965 : 326,2 " "
- 1966 : 497,5 " "
- 1967 : 511 " "

Country of Origin unpublished

Djakarta, December 27,

