

## ECONOMIC ANALYSIS WITHOUT VISION

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### ABSTRAK

*Cukup menarik dan patut dihargai perdebatan para ekonom kita dalam mendiagnosa penyakit-penyakit ekonomi Indonesia khususnya sejak terjadinya krisis ekonomi tahun 1997. Perdebatan-perdebatan tersebut banyak membantu masyarakat umum lebih memahami masalah-masalah mendasar yang dihadapi. Tetapi ada kalanya masyarakat tidak mengerti, bahkan bingung jika perbedaan pendapat pakar-pakar ekonomi ini demikian jauh. Dengan merujuk buku karangan Robert Heilbroner dan William Millberg, **The Crisis of Vision on Modern Economic Thought** (1995) artikel ini ingin menghimbau ekonom Indonesia lebih berpijak di bumi Indonesia dan selalu berpikir dalam konteks ideologi bangsanya yaitu **Pancasila** dalam menguraikan buah pikirannya.*

**Keywords:** *Vision on Economic Thought, People's Economy.*

### INTRODUCTION

Economic news that has been addressed by economic experts has frequently triggered confusion among the public because they are sometimes so different or even in contradiction one from the other. One such difference arose when BPS "revised" the economic growth target of 4% for the year 2000, downward to 1.6%, as reported on the 15th of May 2000. The reasons the growth target needed to be adjusted to a half of its original plan are *political uncertainties, uncertainty on law enforcement, and insecurities* in particular, as this nation was to hold yearly People's Consultative Assembly session in August.

Such downward adjustments have been strongly opposed by government economists who accuse that BPS of being "too pessimistic" on the economy. In contrast, the government is optimistic that the target of 4% should be reachable and may even be surpassed. Recently, Mari Pangestu from CSIS has also made a headline in *Kompas* as she commented that "4% economic growth would not be an easy target to achieve," because most foreign

investors have taken "a wait and see" attitude due to uncertainties and unpredictabilities of political development. If such conditions keep on emerging Indonesia will be one of the least attractive places for foreign investors.

That different predictions have been made using the same "economic theories" is difficult for the public to understand. And the sources of differences are the "non-economic factors" such as political instabilities, dissolutions on law enforcement, and insecurities.

### THE PREDICTIVE POWER OF ECONOMICS

Economics as a social science has a unique job - that is to explain economic phenomena. If more and more economic factors are available and quantifiable, then those explanations are used, *ceteris paribus*, to predict the future. However there are many non-economic factors that are not quantifiable, so that many are not fulfilled. Subsequently the explanations presented are incomplete and the prediction is far from expectations. One of the weaknesses of

economics is over-confidence in forecasting, despite evidence that some economic predictions are incorrect. One recent and obvious example of such incorrect predictions is the *monetary crisis* that happened in August 1997. No foreign or national economists have predicted such a crisis.

We should be wondering, why if economists' predictions have been incorrect a number of times, their predictions on *economic growth* have been in great demand and are announced from time to time by the press? Such behaviour is not easily understood by common people. Perhaps one explanation is the ability to provide exact figures even if thorough explanations on non-economic factors such as political variables that may change an earlier prediction are lacking.

The limitation of economics to make predictions has been acknowledged since the very beginning, and therefore the name of the science when born was *political economy*. Political economy is the science to manage the nation's household, which never separates economic and political factors, because the two elements are inseparable. Rapid developments of the new science in the past centuries encouraged economists to change the name from political economy into economics (Alfred Marshall, 1890). Marshall is known as the father of *Neo-classical* economics replacing The Classical School that was the economic ideology for the previous century.

## VISION ON MODERN ECONOMICS

It was five years ago (1995) when a small book (131 pages) was published with an intriguing title, "The Crisis of Vision on Modern Economic Thought" written by Robert Heilbroner and William Millberg. The title itself is very intriguing if it related to a different opinion of economists exposed every day by large newspapers in this country. The authors were very displeased by the arrogance of their macro economist colleagues who had no vision at all or argued that vision was not

necessary. What they most uphold was "deep analysis", ignoring elements to establish a vision. Such professional behavior was to Heilbroner and Millberg unacceptable, as they state:

*At the heart of our argument is the contention that "vision" sets the stage and "peoples" the cast for all social inquiries....*

*Vision constitutes all-important terrain over which intellectual contest is waged in political and sociological controversy.<sup>1</sup>*

An over emphasis on and too much economic analysis, while ignoring the importance of vision would equip economists to explain *the causes and effect* of economic phenomena. Such ability would not be mastered by other disciplines such as political science, sociology or psychology. Probably these abilities have created a covetous feeling perceived by other social scientists. However if *a vision on economic analysis* is not considered vital then the outcome of the analysis is fatal. As the authors state:

*Analysis has thus become the **jewel** in the **crown** of economics. To this we have no objection. The problem is that **analysis** has gradually become the crown itself, overshadowing the baser material in which the **jewel** is set. To this we do indeed object, for without the setting there would be no **crown**.<sup>2</sup>*

*No social analysis can be without its "visionary" basis. Our concern and the change at which our catalytic effort is aimed is the widespread belief that economic analysis can exist as some kind of socially disembodied study.<sup>3</sup>*

The above quotations have revealed the essence of that book, "The Crisis of Vision on Modern Economic Thought". We expect that Indonesian economists could at least refer their

<sup>1</sup> R Heilbroner & W Milberg, (1995), *The Crisis of Vision on Modern Economic Thought*, halaman 4.

<sup>2</sup> *idem*, hlm 5.

<sup>3</sup> *idem*, hlm 6.

analysis and their findings to the book to be able to achieve better understanding and explanations to current economic phenomena. We should be able to help the public to find ways to come out from economic crisis on finding the best, not to put up more confusion in the public's mind.

### HAS THE INDONESIAN ECONOMY NOT RECOVERED FROM CRISIS?

One of the reasons economists disagree whether Indonesia has or has not recovered from the economic crisis is because the positive economic growth that started mid-1999 was due to the increase of consumption expenditures, not from investment. The programs on banking re-capitalization have not been unimplemented, therefore the manufacturing industries have not obtained fresh capital from the financial sectors to re-start production. So we can draw the conclusion that production lines will not be producing

again if new capital is not injected into Indonesia economy.

Positive economic growth is not going to be sustainable if it is entirely induced by *consumption expenditures* (households or government). Is that true? If economic growth was so high for the past 30 years with significant *increase in people saving* and then the economy was plunged into recession, would it be wrong if the government and households *withdrawn their saving to maintain their consumption level*? An increase in such spending that could induce economic growth by all means can not be overruled. The government's expenditures have produced productive activities to assist and stimulate investors from the private sectors.

Heilbroner and Milberg state:

*Not all government expenditure can be treated as consumption that capital budgeting is essential for the public sector, however difficult it might be.*

**Table 1.** GDP Allocation 1998-2000 (trilyun Rp) at 1993 Constant-Prices

GDP Allocation	1998				1999				2000	
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2
HHConsumption	69,2	68,5	63,8	66,4	67,1	67,3	67,9	69,5	68,0	68,8
Gov't Expenditure	7,1	6,6	6,2	6,9	6,8	7,3	7,2	6,7	6,9	7,5
Investment	25,4	22,0	22,9	19,7	18,0	17,3	17,7	18,1	20,6	21,8
<b>GDP</b>	<b>101,7</b>	<b>97,1</b>	<b>92,9</b>	<b>93,0</b>	<b>91,9</b>	<b>91,9</b>	<b>92,8</b>	<b>94,3</b>	<b>97,0</b>	<b>97,7</b>

Source: BPS

Amartya Sen, the 1998 Noble Laurette also suggests "that a one year recession should not mean the end of the world if the country has accumulated wealth for decades".

*It may be wondered why should it be so disastrous to have, say, a 5 or 10 percent fall in gross national product in one year when the country in question has been growing at 5 or 10 percent per year for decades. Indeed, at the aggregate level this*

*is not quintessentially a disastrous situation.*<sup>4</sup>

It is true that economic activities represented by private consumption dramatically declined. However such decrease took place only up to a 3rd quarter of 1998 (July - September) and since then activities have consistently resumed. Such economic activities include government consumption expenditure. Admittedly the investment decrease continued up to the 2nd quarter in 1999, but started to

<sup>4</sup> Sen, *Development as Freedom*, 2000 p.187

increase also since the 3<sup>rd</sup> quarter of 1999. The increased consumption actually rescued the total Indonesian economy from a ruined situation. We could say that the power of the economy was not derived only from private sectors (big companies), but also from the households and government. These 2 last sectors became stronger and reliable within the economic growth period from 1987 - 1997 and was a buffer to the Indonesian economy during the crisis period. The people's economy, which consists of small, medium enterprises, and households, (the people's demand and government expenditure), are activities that can be categorized as investment, regardless how small its role individually and how the capital has been obtained (not from the formal banking system). Therefore it would be mistaken not to consider activity from the informal financial institution as a form of investment

The brief analysis above indicates how economists have been forgetting the role of *the people's economy* as a foundation of national economy. The people's economy outside the big businesses proved to be strong and reliable as the basis of the national economy. As household's economy becomes stronger, its contribution is so apparent as the people's economy is able to accumulate in the form of deposits, jewelries, lands, cattle and other valuable goods. These activities do not rely on import of raw materials, resulting in the big decrease of import of raw materials by the 2nd quarter of 1999 (Rp 8 trillion, down from Rp 39 trillion at the 1st quarter of 1998). Electronics and chemical industries were seriously affected as import of raw materials dropped dramatically.

These data help to provide understanding of how significant has been the number of *transient poverty*, around 12,3 million people within the period of 1996 - 1999. They became poor because of major inflation shock (77% during 1998). However, as they were able to cope and get used to the changing condition, such depressions were only there temporarily. As prices went back to normal (deflation), they

were no longer poor. The latest figures from BPS have indicated significant decline in the number of poor after the crisis subsided. The poverty figure was 17,9% (36,5 million people) in December 1998 and dropped to 11,7% (24,2 million people) in August 1999. This means that during the economic crisis, the number of poor people in urban areas increased up to 89% but when the economy bounced back to normal again, the figure was only 1% greater than the figure in 1996. And in the rural areas, the figure escalated to about 63%, but then again it has declined to only 10% above the poverty figure in 1996.

*It is entirely possible for poverty to jump dramatically in a transient fashion as households fail to respond to a major inflation shock. As the behavior of prices return to historical trends - as they seem to have done quite quickly in Indonesia - estimated poverty would come down from its dramatic levels and settle to a more stable pattern.<sup>5</sup>*

We must admit that the *Indonesian economic recovery* has been under way regardless of how small its recovery. However a number of economists are not convinced that recovery has taken place; such statements have carried so much *political bias* because the financial market has not been freed to carry on its purposes and the banking sector itself has not yet regained its power as development "agent." Perhaps we could say that economists have relied on free market economic analysis too much, *without any visions on Indonesian ideologies*. If the recovery process had speeded - up, it would result in a big problem as to answer 'who' and 'what' have been the most contributors during the time of recovery so that those elements should be given opportunities to develop even larger. If economic growth was 3,2% during the months of April - December in 1999 and 4,1% during January - March 2000, that was the time when the banking recapitations had not taken place and

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<sup>5</sup> UNSFIR

also the banking sectors and manufacturing industries had not been restructured. Therefore the contributors must be the people's economy (SME's). If the government does not appreciate such activities and still believe that the banking recapitations is the only solution for the Indonesian economic recovery, serious problems can emerge. There are two possible problems:

1. The government should provide a huge funding in the 'annual state budget' (APBN) to pay for the government bonds' interest.
2. If for example the Bank BNI 46, are ready to disburse credits and somehow such credits are channelled to those companies having huge debts, we would repeat the old stories again, that is neglecting the people's economy. And we should not be surprised if Indonesia would experience economic - instability again, and that's not what we would like to have.

Henceforth, Indonesian economic recovery should not be allowed to take the path that led to the crisis. The recommended path that needs to be taken should be systematic program, to achieve equitable growth and justice through the process of empowerment of the people's economy.

The economic crisis that happened in 1997 - 1999 has given valuable lessons for Indonesian economists professionally as well as a more humane perspective. Neo classical economics from the West seems to be "too rational" and puts emphasis too much on "efficiency," while ignoring "equity". It eventually considers investment as the only contributor to *economic growth*. Too much praise of economic growth and investment has caused economists to be enchanted with modern industries. Liberalization and globalization have been adopted and implemented everywhere, overwhelming and ignoring the fact of the people's economy and household's economy. **J.M. Keynes** reminded us in his book published in 1936, that household

economy should be able to play a bigger role in national economy. The possibility to spend on consumption as much as the amount on investment should be significant enough "to pull the nation's economy out of recession."

A good example of opinion ignoring the power of consumption as the source of growth which was called '*artificial*' came from the most prominent economist Prof. Sumitro Djojohadikusumo, who said that "although Indonesian economic growth this year was 3,7%, however such economic growth was deceptive because the growth was triggered by consumption expenditure not investment" (*Jawa Pos*, 24th of April 2000). The other economist who shared that idea was Mari Pangestu reported in *Kompas* on the 24th of May 2000, whereas she also mentioned that the basis of her opinion was from "outside the country."

Toward such opinions we should firmly agree that not all expenditure are "consumptive" but a lot of them are "investment" expenditures. A good example is the development of the 3rd pier this year in Bakauheni, Lampung province. The development of that pier was postponed only for 1 month during the crisis in 1997 - 1998. As for the increase of household consumption expenditures, we should not wrongly perceive what producers have responded to such activities. This response to increasing demand for consumption is certainly investment. It would be incorrect to consider small investment made by the people's economy (small, medium enterprises and households) as not being investment. It is also incorrect if we perceive that only big companies can invest and since the banking system has not provided fresh credit to these companies, then there must be no investment. In order to clear up any misunderstanding that not only "the rich" can contribute to economic growth through their saving and investment, but also "the poor", we can quote J.M. Keynes, from his book of *General Theory* (1936);

1. *In contemporary conditions the growth of wealth so far from being dependent on the abstinence of the rich, as is commonly supposed, is more likely to be impeded by it.*<sup>6</sup>
2. *Experience suggests that .. measures for redistribution of incomes in a way likely to raise the propensity to consume may prove positively favorable to the growth of capital.*<sup>7</sup>

It is now clear that economic growth can be induced by consumption, including consumption of the poor. In contrast, the thrifty way of life of the rich may hamper economic growth.

### THE VISION ON TRUTH AND JUSTICE

If economists seem to be very busy looking after 'the truth' in their scientific activities, they clearly forget 'the vision' and 'the mission' of any society, that is equity and justice. The objective of economic development of Indonesian people as a whole is obviously to achieve *prosperity* and *equity* for every member of Indonesian societies. Fruits of development must be distributed equitably among the people.

A member of AIPI (Indonesian Academy of Science) Emil Salim, who has been several times appointed as Minister during the period of 'the New Order' has spoken about the experiences of economists in the past in a paper called "to build a New Indonesia." He stated that the technocrats during the years of New Order had tried hard and struggled for not letting the regime to undermine them. Whereas in the early stages the technocrats fought hard for the idea of development strategies emphasizing equity, eventually they were paralyzed as the "regime" decided to focus on economic growth instead and to put aside ideas on equitable development.

Such a signal had been previously addressed by Moh Hatta, who formulated economic articles on social welfare in the Constitutions

of The Republic of Indonesia, mentioned in article 33;

*Economic Policies are still based on Pancasila and the 1945 Constitution, but under the technocrats Liberalism was used as the guidance.*

With the above statement of Moh Hatta, it is so apparent that *liberalism* had been accepted to suit well the interests of private enterprises with *Capitalism* as their ideology. As predicted by the famous J.M. Keynes, the result is serious income disparities.

*The outstanding faults of the economic society in which we live are its failure to provide for full employment and its arbitrary and inequitable distribution of wealth and incomes. I believe that there is social and psychological justification for significant inequalities of incomes and wealth, but not for such large disparities as exist today.*<sup>8</sup>

The technocrats tried hard not to be coopted by 'the regime,' but unfortunately they failed to do so, as in the formulation of economic democracy they used the term "controlled market economy" and "managed market economy." Whatever the formulation, still they are unable to establish 'the vision and the mission' to achieve 'truth and equity' within the national economic development strategies.

Radius Prawiro, another important member of the technocrats during the New Order regime has also admitted 'such incapacity' in his book;

*In this precarious state, the government took the bold move of removing all restrictions on the flow of capital into and out of the country. Indonesia's Laws governing the flow of capital thus became some of the most liberal in the world, more so even than those of many of the most developed countries.*<sup>9</sup>

<sup>6</sup> Keynes, (1936, *op cit.* pp. 373)

<sup>7</sup> Keynes, - - - , pp.373

<sup>8</sup> Keynes, - - - , 1936

<sup>9</sup> Radius Prawiro, (1999, p.290)

Long winding economic crises that have happened in Indonesia should be looked at from 2 different aspects. Each party that was involved carried their ideas differently, therefore sometimes collided with each other. One party came from the strong economic groups, which has colluded with the regime and the other party came from weak and poor peoples' economy. If the economists were seriously after the truth and equity, they should be *taking sides* with the second group to fight any collusion that has been well established and so corrupted. Incidentally Adam Smith "predicted" such a danger in 1776;

*People of the same trade seldom meet together, even for merriment and diversion, but the conversation ends in a conspiracy against the public, or in some contrivance to raise prices. It is impossible indeed to prevent such meetings, by any law, which either could be executed, or would be consistent with liberty and justice. But though the law cannot hinder people of the same trade from sometimes assembling together, it ought to do nothing to facilitate such assemblies; much less to render them necessary.*<sup>10</sup>

Taking the side of the weak and the poor, is not violating any scientific principles to try to establish 'equity' and 'justice.' If we let that group do an open battle in capitalistic market system, it is surely well predicted, that the weak will be crushed.

## CONCLUSION

If there was an economist who was strongly opposed to the *ideology of Pancasila* in presenting his vision, mission, and economic analysis, he unconsciously adopted the *Neo-Liberal ideology* which put too much faith in the power of market mechanism, and suspiciously distrust the role of government as the "regulator" of the economy. Neo-Liberal ideology originated in Washington DC some

years ago and has been applied almost perfectly by some countries in Latin America, such as Bolivia and Chile. The ideology has succeeded in guiding those developing countries to ease up the huge debts that they have accumulated. That ideology was apparently a perfect medicine to cure monetary problems within the periods of the 80's.

It has been and will be interesting to watch closely how Indonesian economists present their analysis on the economy. What they should agree on eventually is adopting *the essence of Pancasila's philosophy* as a big visionary picture for developing the nation and Indonesian people as a whole.

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<sup>10</sup> Adam Smith, *Wealth of Nations*, (1776, p.144)