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DOCUMENT NO. AND TYPE	SUBJECT/TITLE	DATE	RESTRICTION
001. memo	Robert E. Rubin to POTUS re: U.S. Exchange Stabilization Facility for Indonesia (3 pages)	10/30/97	P5
002. memo	Karin Lissakers (IMF) to Deputy Secretary Summers, Under Secretary Lipton, & Assistant Secretary Giethner re: Camdessus on Indonesia (1 page)	03/16/98	P1/b(1) Unclass.
003. memo	Mark Sobel (IMF) to Steve Saeger re: Indonesia (1 page)	05/18/98	P1/b(1) Unclass.
004. letter	POTUS to President Soeharto re: Developments in Indonesia (1 page)	05/19/98	P1/b(1) Unclass.
005. memo	Lawrence H. Summers to POTUS re: Your Meeting with President Wahid of Indonesia (1 page)	11/10/99	P5

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[History of the Department of the Treasury - Supplementary Documents] [30]

jp26

RESTRICTION CODES

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INDONESIA

1997-SE-011025

DEPARTMENT OF THE TREASURY
Washington

October 14, 1997

NCC to LS
(reading)
NCCCC to NF
SJ
10/14/97
Please
Log
IN

TO: Deputy Secretary Summers
Under Secretary Lipton

FROM: Timothy Geithner

SUBJECT: Options for US Financial Support for Indonesia

Attached is a draft outlining several different options for US participation in a financing package for Indonesia as discussed at the meeting this afternoon.

DRAFT

International Financial Support for Indonesia: Options for U.S. Participation

As discussions between the IMF and Indonesia concerning a financing package progress over the next several days, we will likely face the issue as to whether the United States should participate in some fashion beyond its shareholdings in the international financial institutions (IFIs). Our preference would be to see a viable financing package emerge that is 100% funded by the IFIs and does not incorporate bilateral assistance. It is likely, however, that some form of Japanese participation will either be offered or requested. It is therefore necessary to consider how the United States should respond to an Indonesian request for assistance or an unsolicited offer by the Japanese.

There are four basic options that can be considered for U.S. participation in a financial support package: a multilateral bridge loan, short-term swap arrangement, an Ex-Im Bank facility, or a medium-term loan.

Multilateral Bridge Loan: A bridge loan to World Bank or Asian Development Bank loans, as was done in the recent case of Thailand and in 1995 with Argentina.

- This is the least problematic option from a legal and legislative perspective, as there is an assured source of repayment and our participation in the Thai bridge did not raise significant Congressional objections.

- The multilateral bridge, however, provides little real financial assistance and in the case of Thailand has proven ineffective in underscoring U.S. support for the restoration of financial stability in Southeast Asia.

Short-term Swap Arrangement: The United States could provide Indonesia with a $500 million to $1 billion short-term swap line, which could be drawn on for periods to 60 to 90 days to provide liquidity support. Conditions could be placed on drawings on the swap line to limit the risks that such an arrangement would undercut IMF conditionality or that the funds would be used to finance imprudent levels of intervention.

- Any drawing could require U.S.and IMF approval, and could require certification from the IMF that Indonesia is in compliance with the Fund program.

- A requirement could be set for the level of gross and net international reserves could be set to insure that the swap line will not be utilized to finance excessive intervention and that there are sufficient reserves to repay the borrowings.

Ex-Im Bank Facility: A credit guarantee facility (CGF) of $1 billion or larger could be established to finance Indonesian imports of U.S. goods.

- This would in essence represent "tied" aid and would provide no newly available financing, as Ex-Im Bank funding is already fully available for exports to Indonesia. The "bogus" nature of this facility would be widely recognized by both the private sector and governments in the OECD and in the region.

- In contrast, financing from the Japan Ex-Im Bank is untied and can be used directly for balance of payments support.

- The primary advantage of a CGF would be the symbolic value of announcing some form of direct U.S. financial support for Indonesia.

- While a CGF for only Indonesia might raise some questions as to why the U.S. did not support Thailand with a similar facility, a broader CGF for the region might reduce this problem.

Medium-Term Loan. A $1 billion loan could come out of the Exchange Stabilization Fund. The mechanism for this would be comparable to what was done in the case of Mexico, although the scale of any loan would be far smaller.

- This approach carries significant political risk, as it would likely provoke a sharp outcry from Senator d'Amato and others who opposed the Mexico bailout. It is particularly risky given the pending status of the NAB on the Hill, and would likely lead to reimposition of the d'Amato restrictions on use of the ESF.

- It would be unprecedented for a loan of this type to be provided without an assured source of repayment. It is possible, however, that an arrangement similar to the case of Mexico could be made using Indonesia's

- The loan does, however, provide the strongest possible signal of U.S. support.

1997-SE-011678

DEPARTMENT OF THE TREASURY
WASHINGTON

UNDER SECRETARY

OCT ?

MEMORANDUM FOR SECRETARY RUBIN
DEPUTY SECRETARY SUMMERS

FROM: David Lipton, Under Secretary (International Affairs)
Timothy Geithner, Assistant Secretary (International Affairs)

SUBJECT: Draft Package of Materials on Asia

Attached is a draft package of materials describing the possible U.S. participation in the IMF-led program for Indonesia and our thoughts on improving economic and financial cooperation with other countries in the Asia-Pacific region.

Contents:

Draft Statement by Treasury Secretary Robert E. Rubin

For the last several months, the Treasury Department and Federal Reserve have been actively involved with other countries in the Asia-Pacific region in supporting efforts to restore financial stability in South East Asia and in exploring ways to strengthen the capacity of the international financial system to prevent and, when necessary, respond to financial crises.

In this context, we welcome the announcement of Indonesia's agreement on a financial support package with the International Monetary Fund, the World Bank and the Asian Development Bank. The United States and a number of other countries in the region are prepared to provide contingent financial support that could be drawn on as a second line of defense for a temporary period, if needed and only after recourse to IMF financing and Indonesia's own resources. These contingent drawings would be made in the context of implementation of an appropriate set of additional measures linked to the IMF program of macroeconomic and structural policies.

We are also in the process of consulting with countries in Asia on ways to enhance mechanisms for regional cooperation and, more generally, to strengthen the role and capacity of the IMF and other international financial institutions to prevent financial crises and deal effectively and promptly with those that actually occur.

The restoration of financial stability in Asia is critical to the interests of the United States. These countries are not only key markets for U.S. exporters, but are also crucial to our efforts to promote growth, peace and prosperity throughout the world. In today's global economy, the health and prosperity of the American economy depend importantly on the stability of the global financial system and the economic health of our major trading partners.

Draft: October 29, 1997; 6:45 pm

U.S. Financial Support for Indonesia
Talking Points for Use on Capital Hill

- The United States has a strong economic and security interest in helping the economies of Asia restore their financial stability and sustain their economic growth.

  -- In today's global economy, developments in the global financial system and the economic health of our major trading partners directly affect our own economic health and prosperity.

  -- In 1996, the United States exported a total of $186 billion to Asian countries. We also have well over $126 billion in foreign direct investment in the region.

- We have played an active role in supporting the development of strong IMF programs were those have been appropriate.

- The IMF is close to announcing a program for Indonesia that will:

  -- employ tight monetary policy to stabilize exchange markets and reverse some of the rupiah's depreciation since July;

  -- tighten fiscal policy through a variety of revenue increases and expenditure reductions aimed at producing a fiscal surplus and improve budget transparency;

  -- strengthen the domestic financial sector through a variety of measures (e.g., recapitalization, mergers) and institute a number of regulatory and supervisory reforms (e.g., improved accounting and loan-loss provisioning);

  -- eliminate some importation and marketing monopolies, reduce tariffs on certain protected sectors and eliminate certain non-tariff barriers, and improve usage of the Reforestation Fund.

- The United States intends to join a number of other countries in the region in providing Indonesia with a second line of defense for use if needed.

- This would take the form of contingent finance [in an amount up to $3 billion] that would be available for a temporary period, only after recourse to IMF financing and Indonesia's own resources, and under other conditions that would be designed both to protect our interests and reassure investors.

- This contingent facility is consistent with existing legal authorities for use of the Exchange Stabilization Fund.

DRAFT

- A visible U.S. commitment in this form will help enhance the prospects that Indonesia will, with determined implementation of the reform measures agreed with the IMF, be able to regain market confidence.
  - -- Such a tangible expression of our interest in the region will be highly valued, not just in Indonesia, but throughout the region.
- This is important to stability in the region as a whole.
- We are structuring our contingent commitment so as to minimize risks to the United States. Among the conditions we will be negotiating with the Indonesians are:
  - -- minimum/maximum gross and net international reserves levels;
  - -- acceleration of repayment;
  - -- requirement for adoption of additional adjustment measures (over and above the conditions agreed and being implemented under its IMF program) in order to draw; and
  - -- short-term maturities.
- The contingent nature of the financing reinforces incentives for timely and full implementation of Indonesia's IMF adjustment program, thus minimizing the likelihood that Indonesia would ever need to draw.

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INDONESIA
Bilateral Financial Support for Indonesia

Question: **Will the United States offer Indonesia bilateral financial support in addition to an IMF program?**

Answer: Secretary Rubin indicated earlier this month that we support Indonesia's efforts to work with the IMF and other international financial institutions to manage to the financial instability it is confronting.

- We have had close discussions with the Indonesian authorities and with officials from the international financial institutions involved. We believe that we will be able to support strongly the IFI centered program of financial support that is currently taking shape.

- We have not made a decision regarding whether or not it makes sense to offer supplemental support financial support for Indonesia, but we do believe that a support package for Indonesia should be centered on financing from the international financial institutions.

  -- We do not see a need for any bilateral cofinancing of an IMF led package.

- Indonesia's discussions with the IMF are on-going and we believe it is prudent to wait until these discussions have concluded before we make a judgement.

- Our decision on whether to extend support will be determined by our judgement about what is in America's interest.

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INDONESIA: U.S. FINANCIAL SUPPORT
Effect on IMF's Role

Question: Won't U.S. Bilateral Support for Indonesia Undercut the Role of the IMF?

Answer: No, it won't. U.S. financial support does not represent cofinancing of the IMF's program; rather, our resources are supplemental. Our resources will only be used if it is determined that additional support is warranted due to unforseen financial market pressures.

- Over the past few months, we have been working closely with the IMF and with countries in the region to make sure the central role of the IMF in responding to financial crises is maintained.

- We have also been working with other potential donor countries to Indonesia to induce them to structure their support in a way that supplements IMF resources.

- In addition, we are currently pursuing a broader strategy in the region to enhance mechanisms for regional financial cooperation that will strengthen the IMF and improve our capacity to prevent financial crises, or deal with those that actually occur.

- Towards this goal, we are setting up a meeting of regional central banks and finance ministries in mid-November in Manila that will discuss these issues in time for the APEC Leaders' Meeting in Vancouver.

DRAFT

INDONESIA: HUMAN RIGHTS

Question: **How can the United States offer financial support to a country with an abysmal human rights network like Indonesia?**

Answer: Our decision to make contingent financial support available to Indonesia was based on our view what was in the national economic interest of the United States.

- In 1996, Indonesia was the United States' 28th largest export market and bought $4 billion of U.S. merchandise exports. It is also a large and increasingly important market for U.S. service providers.
- Indonesia is the largest economy in South East Asia with a population of 200 million people.

then,....either

A. Regarding the human rights situation in Indonesia, I would refer you to the Department of State

or

B: The United States believes that greater transparency and improvements in governance in Indonesia will be important building blocks for allowing Indonesia to reach its true potential. U.S. officials have discussed human rights issues with Indonesian authorities on numerous occaisions in the past.

(I think we need to respond that the USG is not asleep on the job regarding human rights, that we do have concerns, but that this wasn't a factor in our decision.)

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INDONESIA FINANCIAL SUPPORT: THE RIADY FACTOR

Question: **How do you respond to the accusation that the United States has offered financial support to Indonesia as a payback for the financial support offered by wealthy Indonesians like James Riady to President Clinton's 1996 reelection campaign?**

Answer: Such an accusation is simply preposterous and is totally groundless.

- The United States' decision to make contingent financial support available to Indonesia was based on our view of what is in the national economic interest of the United States.

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Indonesia -- Program Outline

To the best of our knowledge, this is what the IMF program with Indonesia looks like with regard to key elements.

Monetary/Exchange Rate Policy

Program will seek to stabilize exchange markets and reverse some of the rupiah's depreciation since July. The rupiah has depreciated by 36% since July which, in the Fund's view, represents an overshooting even in light of depreciation of currencies in neighboring countries. The program will aim to roll back the post-July depreciation to the 20-30% range. . However, just preventing further depreciation is an acceptable outcome within the parameters of the program. The objective will be given priority. Interest rates will have to go higher at the outset and stay high until exchange markets respond. However, the Fund will seek to avoid an excessive and protracted credit crunch that could worsen the banking problem and cause an extended slowdown in the Indonesian economy.

- [Monetary tightening to raise interest rates at the outset of the program; 12-month interest rate (considered the most reliable bench mark) expected to go from current 20% to 24-25%. (No explicit interest rate target.)]

- A foreign exchange floor that would permit total intervention of $5-7 billion, with a $5 billion one month sub-ceiling.

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- A first-round of exchange market intervention of $2-4 billion, only partially sterilized. That is, some of the contractionary effect of intervention on the domestic money supply would be passed through to force up interest rates at the outset.

- Subsequent intervention would be mostly or fully sterilized, i.e. its impact on monetary conditions would be offset by an expansion in domestic credit, aimed to preserve the program's target growth in base money. If intervention is continued because markets do not react, monetary conditions would gradually be tightened so that the path for base money growth would fall to zero from an initial targeted 8 percent annual growth as intervention levels approach the outer limits. Since base money is now, at today's exchange rate, only about $12 billion, the program implicitly envisages considerable sterilization.

__Fiscal Policy__

The fiscal program aims for a 1 percent surplus this fiscal year (ending March 31) and next, primarily to cover the current cost of bank restructuring. Fiscal measures totaling about 1.5 percent of GDP are needed this year to make up for slower growth/revenues and achieve the target.

- Petroleum product price increases to yield 0.7 percent of GDP. (Prices have been frozen for five years.) Government accepts in principle but wants to delay till April to cushion hardship. Fund seeking offsetting measures, including broadening VAT base to cover commodities currently exempt.

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- Contingent VAT increase of XX% if other fiscal measures do not produce the desired result. (Magnitude of increase depends on size of any fiscal shortfall.)

- Expenditures reductions will include delays or cancellations of major infrastructure and other projects. (Most were announced before negotiation began with the Fund.)

- All extra budgetary accounts to be consolidated and brought on budget. Complete data on such accounts to be provided to Fund as prior action, before Board approval of program.

Financial Sector Restructuring

The agreed plan will include bank closings, restructurings and regulatory improvements. Prior to IMF Board decision, the Indonesian authorities will announce:

- Closure of 18-19 small private banks, effective immediately.

- Conservatorship (government takes immediate control) for six small private banks. Banks put under conservatorship will be closed within [2-4 months] unless private recapitalization and/or merger partners have been found by that time. Staff believe all or most will have to be closed. IMF and World Bank technical advisors will assist in conservatorship and restructuring.

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- [Recapitalization by the government of one small private bank followed by its merger with a private healthy Indonesian bank. Estimated cost $150 million. Treatment would be similar to support government provided the six other private banks prior to conservatorship.

  -- Above 26 banks account for 5 percent of total banking assets.

- Two state banks with 9% of total assets will be restructured and merged with healthy state banks using fiscal resources. Estimated cost $300 million. World Bank already helping prepare.

- A few insolvent regional development banks will be restructured and recapitalized with financing by the ADB and regional governments. Very small, but symbolic.

- All deposits up to 10,000 rupiah (about $3,000) will be fully guaranteed by the government. Holders of larger deposits, and other creditors, including the government will share liquidation proceeds.

- Creation of a deposit insurance corporation.

- Regulatory reforms including improved accounting standards, loan loss provisioning requirements, and elimination of special tax exemptions.

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Structural/Governance Measures

- National Car Project. Indonesia to accept WTO ruling, with accelerated implementation. WTO ruling against NCP expected within four months. IMF will use quarterly reviews to leverage, shorter normal 15 month WTO compliance period. [Note: U.S. and Japan have offered to withdraw WTO complaints under certain conditions. Only EU has not offered Indonesia an out.]

- Reforestation Fund (estimated $1 billion annual expenditures.) [Authorities agree to establish acceptable, transparent guidelines for future expenditures from this fund, subject to regular independent audits; guidelines to be approved by Fund in conjunction with first program review; and guidelines to be made public.]

- Elimination of all state trading company Bulog commodity import and marketing monopolies, except for rice. Wheat, wheat flour, and soy beans will be deregulated immediately. Sugar, cloves, garlic and others will be tackled later in the program.

- Elimination of special interest exemptions, including for chemicals and metals from Government's plan to reduce average tariff levels to 10% by 2003, and possibly accelerating the tariff reduction schedule.

- Elimination of importation and marketing monopolies on plywood and clothing. Will be done over the life of the program.

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- Declaration of intent to eliminate special treatment including import subsidies, extra budgetary financing, tariff exemptions, etc., for other strategic investment projects, particularly the national aircraft and ship-building projects. Phase out schedule to be developed as part of IMF program reviews.

- Elimination of export taxes on agriculture products.

Financing

Fund envisages the program will be fully financed by IFIs.

- IMF -- \$6-10 billion (300-500% of quota). Three-year stand-by. Front-loaded. (May use Thailand model where half the money disbursed in first two tranches.)

- World Bank -- 4.5 billion, of which \$2 billion is new, \$2.5 billion already in the pipeline.

- Asian Development Bank -- \$1 - 2.5 billion, including what is in pipeline.

*(Staff estimate \$6 billion (2.2 percent GDP) current account deficit for 1997, \$5 billion in '98. Expect investment inflows to cover.

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EXCHANGE STABILIZATION FACILITY FOR INDONESIA

In light of Indonesia's economic and financial situation and the potential spillover to other countries in the region, U.S. monetary authorities would, with other interested countries, consider provision of back-up short-term financial assistance to Indonesia in conjunction with a prospective IMF program.

Such assistance would be available only on a contingent basis In the event of (a) unexpected adverse circumstances which, despite compliance with other policy conditions under the Fund program, increased the pressure on Indonesia's reserves resulting in substantial depletion of those reserves, and (b) after a determination by the IMF and the U.S. authorities that Indonesia had taken any additional adjustment measures deemed necessary to combat the pressure, the United States would stand ready to consider requests for financing to supplement purchases under the IMF program, subject to Indonesia's continued adherence to the revised set of policy understandings and conditions for purchases, and to certain other conditions specified by the U.S. authorities.

The facility would be activated through a joint decision taken [with other participating countries and] with Indonesia [and the IMF], upon determination that the resources available under the IMF program should be supplemented. The United States would participate through the Exchange Stabilization Fund on the terms and under the conditions outlined below. Other countries would participate in a form reflecting their respective legal authorities and policies.

AMOUNT:

- $3 billion.

DURATION:

- Life of IMF program (3-year Extended Fund Facility) for Indonesia, less 60 days.

DRAWINGS:

- On a revolving basis in the form of short-term swaps that could be renewed at the discretion of the U.S. authorities [throughout the duration of the agreement] [up to a maximum of 360 days for any one drawing].

TERMS:

- *Maturity:* 60 days
- *Interest rate:* Treasury cost of funds (60 days) plus an appropriate risk premium set initially at Credit Reform Act requirements and increasing as outstandings rise above

$[1] billion. Initial CRA premium at annual rate would be approximately:

at Indonesia's present rating:	105 basis points
if downgraded one step	233
if downgraded two steps	360

CONDITIONS:

- Determination by IMF Managing Director and U.S. authorities that, due to adverse circumstances beyond its control, Indonesia needs short-term financing to supplement financing provided under the IMF program;
  - U.S. authorities would expect Indonesia's gross reserves to have declined below $[20] billion.
  - U.S. authorities would expect any use of drawings on the facility for intervention to be matched by use of Indonesia's own reserves.
  - U.S. authorities may require that Indonesian authorities draw comparable amounts under bilateral arrangements with other countries.
- Written notification by IMF Managing Director that borrower remains eligible to make purchases as scheduled under the IMF program;
- Determination by the IMF Managing Director and U.S. authorities that Indonesia has made appropriate use of its own resources and has implemented any additional necessary economic measures to counter the unexpected pressure on its reserves;
- Stipulation by Indonesian authorities that net international reserves (gross reserves net of IMF and other extraordinary official financing, including drawings under the ESF Facility) will not at any time be less than $[10] billion while such drawings are outstanding;
- [Daily][Weekly] reporting on reserves;
- Maximum increase in outstanding drawings of $1 billion in any 90 day period, beginning with date of initial drawing;
- At U.S. option, acceleration provision -- for example, if
  - the Managing Director determines that Indonesia is no longer eligible to make purchases as scheduled under the IMF program;

- Indonesia's net international reserves fall below the above-mentioned threshold;
- Indonesia is no longer making appropriate use of its financial resources, e.g., is repaying other bilateral lenders ahead of schedule.

NOTIFICATION REQUIREMENT:

Under the ESF statute, the President must provide Congress a written statement that unique or emergency circumstances require the loan or credit be for more than 6 months of a 12 month period if it is possible that amounts will be outstanding for more than 6 months. Such a notification would be expected to occur at the time of a drawing. (Notification is not explicitly required by establishment of the credit facility in the absence of an actual drawing. Notification only at the time of the first drawing would underline the presumption that the facility would not be used unless an unexpected development ensued.)

ASSURANCE OF REPAYMENT:

The requirement that Indonesia maintain net international reserves at or above a specified level should provide some assurance that Indonesia is in a position to repay the ESF credit.

On a preliminary basis, Treasury lawyers do not believe that this requirement would amount to a legally assured source of repayment.

Draft: 10/29/97 7:25 pm

DRAFT

ESF BALANCE SHEET

*(as of September 30, 1997)**

ASSETS

- The ESF has total assets of $40.1 billion.
- Of this amount, the ESF has $30.0 billion in available resources:
  - $15.5 billion in dollar balances
  - $14.6 billion equivalent of foreign currency (German marks and Japanese yen).
- The remainder of the $40.1 billion is comprised of $10.1 billion equivalent of SDRs, against which Treasury has issued $9.2 billion of SDR certificates in return for dollars.

LIABILITIES

- The ESF has total liabilities of $15.9 billion, composed of:
  - $9.2 billion in SDR certificates outstanding
  - $6.7 billion in SDR allocations from the IMF.

* *Latest published balance sheet in Treasury Bulletin is for March 31, 1997*

DRAFT

October __, 1997

Dear Colleagues:

It is important that we follow up on our discussions in Hong Kong, where we began a useful process to explore the lessons from the current episode of financial turbulence. Our objective should be to use this knowledge to guide us and the broader international community in further refining global mechanisms to reduce the risks of crisis and to help manage crises that we are not successful in preventing.

A note is attached that outlines a series of topics that our deputies might discuss at their upcoming meeting. The note outlines an approach toward increased monetary cooperation in the region in three areas:

- economic and monetary cooperation;
- IMF resources; and
- the role of the private sector.

A framework along these lines has the potential to improve significantly our capacity to deal with risks in global financial markets.

It would be very helpful if our deputies could meet soon to discuss these issues.

Sincerely,

Robert E. Rubin
Secretary
Department of the Treasury

Alan Greenspan
Chairman
Board of Governors of the
Federal Reserve System

Draft 10/27 /97

A Framework for Economic and Monetary Cooperation in Asia

This note outlines a number of suggestions that might usefully be explored in response to recent economic and financial events in Asia. They are designed to build on proposals now under consideration in the region and in the IMF. They combine a set of regional initiatives to promote closer cooperation on financial issues as well as broader initiatives to promote financial stability that we could collectively support in the IMF and other relevant fora.

A regional forum for surveillance and monetary cooperation

- Support the establishment of a regional forum for closer economic and monetary cooperation among the countries in the Asia Pacific region.
    - The forum would bring together finance ministry and central bank officials from key countries in the region with the IMF in a more intensive process of mutual surveillance and cooperation on macroeconomic and financial policy issues.
    - The objective would be to explore ways to monitor potential economic and financial risks in participating countries, and encourage early actions to minimize those risks.
    - The forum would be designed to complement the ASEAN Finance Ministers' process, the EMEAP group of central banks, and the broader APEC process.

A new cooperative financing arrangement for Asia-Pacific region

- Explore the design of a new supplemental borrowing mechanism for the IMF, possibly modeled on the existing NAB, with participation largely from the Asia Pacific region.

IMF resources: Access and Availability

- The resources available to the international community, through the IMF, to respond to financial crises should be appropriate in terms of size and timeliness with which they are available.
    - Recent agreements to increase IMF quota resources and expand supplementary borrowing that the IMF can draw on through the NAB will increase substantially the amount that the IMF can lend in response to crises with systemic implications.
        - Quota resources will rise by SDR 65 billion ($90 billion), of which some SDR 45-50 billion ($65 billion) will be available for lending.

- The distribution of quota shares will shift in favor of countries, mostly in Asia, that have grown rapidly and figure more prominently in the global economy.

- It would be useful to explore changes in IMF access policies that would provide greater assurance that the IMF is in a position to restore market confidence in situations of severe financial crisis and will be able to provide the predominant share of any official financing that may be needed. These could include:

  - Passing the quota increase through fully into the amounts that countries would normally be able to borrow from the IMF, by leaving unchanged the present (100 percent of quota) limit on normal annual access, and the (300 percent) limit on cumulative access;

  - Reviewing the use of exceptional access provisions with a view to providing assurance that the IMF will be able to provide the predominant share of official financing in circumstances where exceptional financing is justified.

- Consider establishing a new facility within the IMF to provide short term funding on a precautionary basis to augment an exceptional stand-by or EFF program, when deemed necessary to stabilize the markets.

- It would also be useful to explore ways of ensuring that the IMF's supplemental borrowed resources are available in a timely fashion when needed, including for cases where the emergency financing mechanism is used to speed initial disbursement, and that the IMF makes full use of these potential resources.

  - In this context, a review of procedures for activating the GAB / NAB, particularly the interpretation of the associated liquidity test, would be appropriate.

- Examine ways to enhance the prospects that private creditors adequately assess risks and bear an appropriate share of the burden of adjustment and financing in times of crisis.

  - It might be useful to establish a working group of experts from interested countries, particularly from emerging market economies, and relevant international institutions (e.g., BIS and IMF) to carry forward earlier work on orderly workout procedures in light of recent financial market pressures in Southeast Asia.

New Global Initiatives to Promote Financial Stability

- Explore means to further enhance transparency and strengthen disclosure standards. For example, we might want to consider pressing for an amendment of the *IMF's Special Data Dissemination Standard* (SDDS) to provide for:

DRAFT

- Mandatory disclosure of official liabilities (current and forward), with greater frequency.

- Broader coverage of financial institutions in order to provide a clearer picture of non-performing assets and degree of reliance on external sources of finance.

■ Develop concrete proposals to promote stronger, deeper and more efficient domestic financial systems, which would enhance integration with global financial markets while at the same time strengthening an economy's ability to withstand shocks. Among the topics that might be considered are:

- Mechanisms for closer cooperation among market regulators and supervisors in response to events that might develop in one country or outside the region but affect markets across the region.

- How national authorities can better monitor and prevent a rapid rise in the external liabilities of the financial and corporate sectors and a shortening in the maturity of those liabilities.

- A proactive strategy for the adoption and implementation of strong frameworks for financial sectors.

- Ways for the IFIs and international supervisory authorities to assist domestic authorities in strengthening and deepening their financial markets. For example, we could support an increase in World Bank and Asian Development Bank resources directed at financial sector reforms, improved financial supervision, banking system restructuring and capital market development.

A regional group on improvements in financial markets

■ Discuss steps to improve the depth, efficiency, and integrity of financial markets in the region, through improvements in transparency, financial supervision, capital market development and other measures that might help reduce the vulnerability of thin markets to large swings in capital flows.

B. Setser & J. Gagnon/ IMI
DRAFT: October 24, 1997

IMPACT OF ASIAN CURRENCY TURMOIL ON THE UNITED STATES

SUMMARY

The Treasury Department examined the possible impact of recent currency depreciations and slower growth in Southeast Asia, Korea, and Taiwan on the U.S. economy. *Based on developments to date, we believe that the situation in Asia is likely to reduce the growth rate of the U.S. GDP in 1998 by a small but significant amount, about 0.2 to 0.4 percentage points.*

U.S. TRADE WITH ASIAN COUNTRIES

- 14% of U.S. exports go to the ASEAN 5 plus South Korea and Taiwan.
- Most of the U.S. exports are to countries in the region -- Singapore, Taiwan, and Korea -- that have been least affected by the crisis.
- The four countries most affected by the crisis, Indonesia, Thailand, Malaysia, and The Phillipines, account for only 4% of U.S. exports.
- In comparison, Mexico accounted for 10% of U.S. exports in 1994, just before the peso crisis.

IMPACT ON THE UNITED STATES

- **The impact on the United States is not likely to exceed 0.4% of U.S. GDP**.
- **Estimated fall in U.S. exports**: a $13.5 billion fall in U.S. exports to Korea, Taiwan, and the five leading Southeast Asian economies in 1998, 0.15% of GDP, relative to baseline projections.
- **Estimated rise in U.S. imports**: a $21.4 billion real increase in imports from Korea, Taiwan and the five leading Southeast Asian economies in 1998, 0.25% of GDP.
- For technical reasons, Treasury estimates probably **overestimate the size of the impact on the United States**, particularly on the import side.

OASIA (Steve Saeger)
To. LS
NCC to RER (reading)
NCC cc to MF
SS
10/29/97
Please Log In

1997-SE-011766

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C.

ASSISTANT SECRETARY

October 30, 1997

ACTION

MEMORANDUM FOR **SECRETARY RUBIN**
DEPUTY SECRETARY SUMMERS

FROM: Timothy F. Geithner, Assistant Secretary TFG
(International Affairs)

SUBJECT: Memorandum to President Clinton on U.S. Exchange Stabilization Facility for Indonesia

ACTION FORCING EVENT

You need to brief the President on our plan to announce the United States' willingness to extend financial support to Indonesia to back-up its IMF program tomorrow in the event that Indonesia and the IMF announce their agreement on policies reforms necessary for an adjustment program.

RECOMMENDATION

That you sign the attached memorandum to the President

✓ Agree ________ Disagree ________ Let's Discuss

ATTACHMENTS

Tab A: Memorandum to President Clinton on Exchange Stabilization Facility for Indonesia

cc: U/S Lipton, DAS Zelikow, DAS Atkinson, Todd Crawford, Jim Lister

NCC original to WH (Hank.)

NCC to LS (reading)

NCC cc to MF SS

10/30/97

Please Log IN

...ETARIAT

Withdrawal/Redaction Marker
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DOCUMENT NO. AND TYPE	SUBJECT/TITLE	DATE	RESTRICTION
001. memo	Robert E. Rubin to POTUS re: U.S. Exchange Stabilization Facility for Indonesia (3 pages)	10/30/97	P5

This marker identifies the original location of the withdrawn item listed above. For a complete list of items withdrawn from this folder, see the Withdrawal/Redaction Sheet at the front of the folder.

COLLECTION:

Clinton Administration History Project

OA/Box Number: 24126

FOLDER TITLE:

[History of the Department of the Treasury - Supplementary Documents] [30]

jp26

RESTRICTION CODES

Presidential Records Act - [44 U.S.C. 2204(a)]

P1 National Security Classified Information [(a)(1) of the PRA]
P2 Relating to the appointment to Federal office [(a)(2) of the PRA]
P3 Release would violate a Federal statute [(a)(3) of the PRA]
P4 Release would disclose trade secrets or confidential commercial or financial information [(a)(4) of the PRA]
P5 Release would disclose confidential advise between the President and his advisors, or between such advisors [a)(5) of the PRA]
P6 Release would constitute a clearly unwarranted invasion of personal privacy [(a)(6) of the PRA]

C. Closed in accordance with restrictions contained in donor's deed of gift.
PRM. Personal record misfile defined in accordance with 44 U.S.C. 2201(3).
RR. Document will be reviewed upon request.

Freedom of Information Act - [5 U.S.C. 552(b)]

b(1) National security classified information [(b)(1) of the FOIA]
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b(3) Release would violate a Federal statute [(b)(3) of the FOIA]
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TREASURY CLEARANCE SHEET

NO. ____________
Date October 30, 1997

MEMORANDUM FOR: ☒ SECRETARY ☐ DEPUTY SECRETARY ☐ EXECUTIVE SECRETARY
☒ ACTION ☐ BRIEFING ☐ INFORMATION ☐ LEGISLATION
☐ PRESS RELEASE ☐ PUBLICATION ☐ REGULATION ☐ SPEECH
☐ TESTIMONY ☐ OTHER ____________

FROM: Assistant Secretary Geithner
SUBJECT: Memorandum from Secretary Rubin to President Clinton

REVIEW OFFICES (Check when office clears)

☐ Under Secretary for Finance	☐ Enforcement	☐ Policy Management
☐ Domestic Finance	☐ ATF	☐ Scheduling
☐ Economic Policy	☐ Customs	☐ Public Affairs/Liaison
☐ Fiscal	☐ FLETC	☐ Tax Policy
☐ FMS	☐ Secret Service	☐ Treasurer
☐ Public Debt	☐ General Counsel	☐ E & P
	☐ Inspector General	☐ Mint
☐ Under Secretary for Int'l Affairs	☐ IRS	☐ Savings Bonds
☐ International Affairs	☐ Legislative Affairs	
☐ OCC	☐ Management	☐ Other ____________

NAME (Please Type)	INITIAL	DATE	OFFICE/ROOM NO.	TEL. NO.
INITIATOR(S)				
A. Velthaus	AMV	10/29	INA/5221	622-1405
REVIEWERS				
DAS Zelikow	AMV/for	10/29	IN/3222	622-7222
Russ Munk	RLM	10/29	GC/2314	2-1899
Ed Knight	[illegible] for	10/30	GC/3000	2-0287

SPECIAL INSTRUCTIONS

☐ Review Officer Date: ☐ Executive Secretary Date

THE DEPUTY SECRETARY OF THE TREASURY
WASHINGTON

November 3, 1997

Dear Colleague:

I attach a slightly revised draft of a possible G7 statement, which could be released after the announcement on Wednesday of the IMF Board decision on Indonesia. We have attempted to take account of the views expressed yesterday, and would be happy for a statement of this kind to be released if others support this. I regard the last paragraph as integral to the statement, as it is responsive to the concerns of some IMF members that the Fund may not be able to play an appropriate role in resolving a financial crisis in their case.

I found our discussion yesterday very helpful and thought-provoking, and would like to thank you for convening our small group. I expect to write again in the next day or so to set out some of our thinking on how to take things forward.

Sincerely,

LHS.

Lawrence H. Summers

1997-SE-011920

THE DEPUTY SECRETARY OF THE TREASURY
WASHINGTON

November 3, 1997

Dear Colleague:

I attach a slightly revised draft of a possible G7 statement, which could be released after the announcement on Wednesday of the IMF Board decision on Indonesia. We have attempted to take account of the views expressed yesterday, and would be happy for a statement of this kind to be released if others support this. I regard the last paragraph as integral to the statement, as it is responsive to the concerns of some IMF members that the Fund may not be able to play an appropriate role in resolving a financial crisis in their case.

I found our discussion yesterday very helpful and thought-provoking, and would like to thank you for convening our small group. I expect to write again in the next day or so to set out some of our thinking on how to take things forward.

Prepared by OASIA
David Lipton

Please log
and file
11/3/97

November 3, 1997 6.30 p.m.

Draft G-7 Statement on Developments in Financial Markets

G-7 Finance Ministers and Central Bank Governors have been monitoring recent market developments in their countries and in emerging market economies. They believe that economic fundamentals in the G7 remain generally encouraging, given the progress in achieving non-inflationary growth and fostering sound public finances. They agreed that all countries share an interest in achieving financial stability around the world and, in this context, welcomed today's decision by the IMF Executive Board to support the program of reforms being undertaken by the Indonesia Government.

Sound macroeconomic policies in emerging economies coupled with structural reforms, in particular to strengthen banking and financial systems and promote transparency, are the key to growth and stable financial conditions. Ministers and Governors noted the steps that had been taken to strengthen the IMF's capacity to prevent and, when necessary, respond to financial crises, including the recent agreement to increase the quota resources of the IMF, the progress toward ratification of the New Arrangements to Borrow (NAB) to supplement Fund resources, and the emergency financing procedures which had enabled the IMF to move speedily to provide exceptional access in Thailand and Indonesia.

They agreed to continue to keep in contact on developments in financial markets, and to consider ways to ensure that the IMF and other international financial institutions have enhanced capacity to play an appropriate central role in supporting sound policies in emerging markets, promoting financial stability and reacting promptly in case of balance of payments crises.

1997-SE-012306

THE DEPUTY SECRETARY OF THE TREASURY
WASHINGTON

November 7, 1997

MEMORANDUM FOR THE PRESIDENT

THROUGH: Robert E. Rubin

FROM: Lawrence H. Summers
David A. Lipton

SUBJECT: Sachs Critique of the Indonesian Adjustment Program

You raised the question of whether Jeff Sachs' article in Wednesday's *New York Times* was basically accurate in its concerns over the IMF approach to Indonesia. Our view is that he is right to distinguish between the case of Indonesia -- which is primarily a crisis of confidence, partly borne out of contagion from markets nearby -- and the usual crises that countries face when they call in the IMF, where high inflation and bulging budget deficits are the main concerns. However, we think that between them the IMF and the Indonesians have devised the correct approach.

The program was largely designed by reform-minded members of the Indonesian administration, who were able to get accepted ideas they had been pushing for years. The controversial points toward the end of the negotiations -- such as eliminating the Suharto family-controlled food import monopoly -- had little to do with austerity. They were about improvements in governance and the transparency of policy making, which Indonesia badly needs and the markets have welcomed. The reduction in import monopolies, in particular, will benefit the real incomes of Indonesian workers by bringing down food prices.

The program takes essentially the same approach to the banking sector that Sachs recommends -- offering liquidity to those that are healthy, but closing those that are blatantly insolvent, including a few owned by Suharto family members and associates. It also sets up formal deposit insurance to reassure individual depositors and forestall further runs on banks. The problems in the banks are a large part of the justification for the modest tightening of fiscal policy, which is also needed to offset the cost of large government subsidies that are not included in the budget.

As for macroeconomic policy, the exchange rate has already depreciated a great deal -- it had fallen more than 40 percent by the time the program was announced. Restoring stability is crucial to avoid large-scale flight of domestic and foreign investors. This requires determination by the Indonesian authorities. An approach of responding to capital flight by not raising interest rates was tried in Mexico in January 1995, to disastrous effect. By contrast, a firm commitment to tighten monetary policy, following our support, helped convince investors that stability would be restored. As then, international support for Indonesia, including ours, will help create the confidence needed for growth to return and interest rates to decline.

THE PRESIDENT HAS SEEN
11-4-97

Secy Rubin /
Gene S

It's right
isn't we this
concerned about
that

Bill

The New York Times
MONDAY, NOVEMBER 3, 1997

The Wrong Medicine for Asia

By Jeffrey D. Sachs

CAMBRIDGE, Mass.

In a matter of just a few months, the Asian economies went from being the darlings of the investment community to being virtual pariahs. There was a touch of the absurd in the unfolding drama, as international money managers harshly castigated the very same Asian governments they were praising just months before.

The International Monetary Fund has just announced a second bailout package for the region, about $20 billion for Indonesia. That should, in principal, boost confidence. But if it is tied to orthodox financial conditions, including budget cuts and sharply higher interest rates, the package could do more harm than good, transforming a currency crisis into a rip-roaring economic downturn.

In the Great Depression, panicked investors fled from weak banks in the United States and abroad. Since banks borrow short term in order to lend long term, they can be thrown into crisis when a large number of depositors suddenly line up to withdraw money. In the days before deposit insurance, individual depositors would all try to be first in line for withdrawals.

In 1933, the Federal Reserve played it disastrously wrong. Rather than lending money to the banks to calm the panic and to show the depositors that they could indeed still get their money out, the Fed tightened credit, as financial orthodoxy prescribed. Confidence sank, and the banking system crumbled.

The Asian crisis is akin to a bank run. Investors are lining up to be the first out of the region. Much of the panic is a self-feeding frenzy: even if the economies were fundamentally healthy at the start of the panic, nobody wants to be the last one out when currencies are weakening and banks are tottering because of the rapid drain of foreign loans.

It is somehow comforting, as in a good morality tale, to blame corruption and mismanagement in Asia for the crisis. Yes, these exist, and they weaken economic life. But the crisis itself is more pedestrian: no economy can easily weather a panicked withdrawal of confidence, especially if the money was flooding in just months before.

The I.M.F. has arrived quickly on the scene, but the East Asian financial crisis is very different from the set of problems that the I.M.F. typically aims to solve.

The I.M.F.'s usual target is a government living beyond its means, financing budget deficits by printing money at the central bank. The result is inflation, together with a weakening currency and a drain of foreign exchange reserves. In these circumstances, financial orthodoxy makes sense: cut the budget deficit and restrict central bank credits to the government. The result will be to cut inflation and end the weakening of the currency and loss of foreign exchange reserves.

In Southeast Asia, this story simply doesn't apply. Indonesia, Malaysia, the Philippines and Thailand have all been running budget surpluses, not deficits. Inflation has been low in all of the countries. Foreign exchange reserves, until this past year, were stable or rising, not falling.

The problems emerged in the private sector. In all of the countries, international money market managers and investment banks went on a lending binge from 1993 to 1996. To a varying extent in all of the countries, the short-term borrowing from abroad was used, unwisely, to support long-term investments in real estate and other non-exporting sectors.

This year, the bubble burst. Investors woke up to the weakening in Asia's export growth. A combination of rising wage costs, competition from China and lower demand for Asia's exports (especially electronics) caused exports to stagnate in 1996 and the first part of 1997. It became clear that if the Asians were going to compete, their currencies would need to fall against the dollar so their costs of production would be lower. It also became clear that with foreign lending diverted into real estate ventures, there was some risk that the borrowers, especially banks and finance companies, would be unable to service the debts if the exchange rates weakened. After all, rentals on real estate developments would be earned in local currency, while the debts would have to be repaid in dollars.

> The old rules and remedies don't apply in the new overseas economies.

The weaknesses in the Asian economies were real, but far from fatal. The deeper strengths — high savings, budget surpluses, flexible labor markets, low taxation — remain in place, and long-term growth prospects are solid. But, as often happens in financial markets, euphoria turned to panic without missing a beat. Suddenly, Asia's leaders could do no right. The money fled.

In this maelstrom, the I.M.F. is now reportedly pressing the Asian countries to raise existing budget surpluses still higher and to tighten domestic bank credit. In the Philippines recently, short-term interest rates were briefly pushed above 100 percent a year to meet I.M.F. credit targets.

And, in a move that is supposed to engender confidence but almost surely does the opposite, the I.M.F. has reportedly called on Thailand

and Indonesia to close down several weak banks that have been caught up in the boom-bust cycle of foreign lending. Since the treatment of depositors in such cases is open to doubt (as deposit insurance is implicit rather than explicit), these calls for bank closings also worsen the investor flight from the region. Of course, one can't be absolutely sure what the I.M.F. is advising, since I.M.F. programs and supporting documents are hidden from public view. This secrecy itself gravely undermines confidence.

The Asian region needs more creative policies than these. The first step would be for the international investment community to tell the truth: the currency crisis is not the result of Asian government profligacy. This is a crisis made mainly in the private, albeit under-regulated, financial markets.

The next step would be to let the Asian currencies float downward, so that these countries' exports will be cheaper and therefore more competitive. Once export growth starts to pick up, then panicked money market managers will begin to remember why they were until recently singing the praises of the region. This is what happened in the aftermath of the 1994 Mexican crisis, when money managers who swore they had left Mexico for good quickly reconsidered in the wake of an export boom.

Floating the exchange rate would have two more advantages: foreign reserves would not be squandered in a failed attempt to defend the currency, and interest rates would not need to be raised in an illusory quest to keep the currency strong.

The third step would be to moderate the strong forces pushing Asia into a recession, rather than adding to them. The region does not need wanton budget cutting, credit tightening and emergency bank closures. It needs stable or even slightly expansionary monetary and fiscal policies to counterbalance the decline in foreign loans. Interest rates will drift higher as foreign investors withdraw their money, but those rates do not need to be artificially jacked up by a squeeze on domestic credit. The regulation of the banking sector should be strengthened not by hasty bank closures, but by pushing weak banks to merge with stronger ones and by pushing the banks to raise their capital bases.

Southeast Asia surely needed a correction to restore its competitiveness. A moderate cut in foreign lending was needed; the panic was not. If the currency crisis is well managed, Asia will be able to resume its rapid economic growth. If it is managed with unthinking orthodoxy, the costs could be very high, for Asia and the rest of the world.

Jeffrey D. Sachs is director of the Harvard Institute for International Development and an economic adviser to governments in Asia and other parts of the world.

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DOCUMENT NO. AND TYPE	SUBJECT/TITLE	DATE	RESTRICTION
002. memo	Karin Lissakers (IMF) to Deputy Secretary Summers, Under Secretary Lipton, & Assistant Secretary Giethner re: Camdessus on Indonesia (1 page)	03/16/98	P1/b(1) Unclass.

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COLLECTION:

Clinton Administration History Project

OA/Box Number: 24126

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[History of the Department of the Treasury - Supplementary Documents] [30]

jp26

RESTRICTION CODES

Presidential Records Act - [44 U.S.C. 2204(a)]

P1 National Security Classified Information [(a)(1) of the PRA]
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RR. Document will be reviewed upon request.

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b(8) Release would disclose information concerning the regulation of financial institutions [(b)(8) of the FOIA]
b(9) Release would disclose geological or geophysical information concerning wells [(b)(9) of the FOIA]

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

April 6, 1998

Recommended Telephone Calls

MEMORANDUM FOR SECRETARY RUBIN

THROUGH: Linda L. Robertson
Assistant Secretary
Legislative Affairs & Public Liaison

FROM: Rick Sinkfield
Deputy Assistant Secretary (International)

SUBJECT: Congressional consultations regarding the expected announcement of the latest IMF agreement with Indonesia

DISCUSSION:

We recommend the following strategy to inform Congress about ongoing developments regarding the economic crisis in Indonesia and the IMF-led efforts to restore stability. This IMF agreement will be heavily scrutinized in light of the ongoing debate regarding the President's FY 98 supplemental budget requests for U.S. participation in the IMF. You, D/S Summers U/S Lipton, and A/S Geithner will communicate directly with Members. U/S Lipton, A/S Geithner and other Treasury staff will communicate with senior Hill staff and conduct confidential and non-confidential briefings as needed. The calls we are recommending encompass the key Senators who were involved in successfully adding the IMF to the defense and natural disaster supplemental bill and the House Members who will be key to preserving the IMF in conference and maintaining the broadest amount of bipartisan support needed to ensure passage of the conference report on the House floor.

The attached talking points have been drafted in a manner that discusses the latest agreement in the context of the issues that have concerned Congress the most with respect IMF and borrower country policies: moral hazard; crony capitalism; trade liberalization; austerity; labor/human/environmental rights; and transparency (IMF and borrower country).

*Note: The asterisk denotes that a Member is out of the country, but the call should be placed.

House

Speaker Gingrich (RER) ~50600

c Speaker Gingrich is reported to be avoiding meetings with outside groups regarding the IMF; his last public statement indicated his disagreement with Majority Leader Armey about the kinds of conditions that should accompany the IMF funding. He asserted that more Congressional oversight was appropriate. You also have a call into the Speaker re: the assault weapons ban (4/6 announcement).

Minority Leader Gephardt (RER) ~50100

c Leader Gephardt previously offered to act as a Congressional voice, buttressing the Administration's position regarding the possibility of Indonesia's implementation of a currency board. He is very conscious of his Caucus' concerns about Indonesia's labor and human rights record. We will need his active assistance in convincing Democratic Members that this new agreement is worthy of their support. You should highlight the possibility of IMF/World Bank/Govt. of Indonesia/labor talks.

*Chairman Livingston (RER) ~53015

c Chairman Livingston is reported to be planning a quick vote on the House floor just after recess in order to make it possible for the House to assent to keeping IMF in the defense supp. conference. His staff has maintained that the Chairman wants to see IMF move quickly. You also placed a call to him re: the assault weapons announcement.

Rep. Obey (RER) ~53365

c Rep. Obey wants the IMF to do everything it can to prevent President Suharto and his clan from personally benefitting from the IMF program. He is also interested in the role played by private financial institutions ("hair cuts").

*Chairman Callahan (RER) ~54931

c Rep. Callahan, due to a constituent's concerns, is particularly concerned about the Indonesia plywood monopoly. You should highlight the fact that the monopoly has been terminated. In a similar area, Rep. Callahan has written to the Dept. regarding the softwood lumber Customs ruling. He advocated reversing the Customs ruling, thereby preventing the pre-drilled studs from coming in to the U.S. outside of the May 1996 Agreement. You should inform him generally of Customs' plans to publish a federal register notice of a proposed revocation of the ruling.

Rep. David Bonior (RER) ~(810) 469-3232

c Rep. Bonior was quoted last week as supporting the IMF, because it is acting as a backstop, preventing a flood of excessively cheap imports from coming into the U.S., thereby jeopardizing U.S. jobs. Rep. Bonior is also scheduled to attend a CEO luncheon event this week where Secy. Daley will discuss, among other things, the trade and market access aspects of IMF programs.

Majority Leader Lott (RER) ~46253

c You have an outstanding call to Sen. Lott re: the assault weapons ban and the softwood lumber issue. On the latter, we believe that he will look favorably upon Customs' expected action. With respect to Indonesia, his main concern, expressed by Senator Gramm, is about the elimination of crony capitalism. You should highlight the fact that the most recent bank closings affect the holdings of Presidential family members.

Minority Leader Daschle (RER) ~45556

- We have worked with Senator Daschle's staff on an "Administration" paper that discusses achievements and next steps in the IFI's and more broadly in the labor and environmental areas. The timing for completing and releasing such a paper is still uncertain, but we believe that he may raise it. We agree that it should be a useful tool in giving Democratic Members something substantive to support in these areas, similar to the statement of Administration Policy during the fast track debate last year.

Senator Sarbanes (RER) ~44524

- Senator Sarbanes has not expressed any particular concerns about Indonesia, but during the Senate floor debate was very helpful in working out Democratic and Republican amendments that addressed toughening IMF policy with respect to Indonesia.

Chairman Helms (RER) ~46342

- Chairman Helms' main concern is with Indonesia's failure to hold free, Democratic elections. He was reported to have, but did not offer, an amendment that would have withheld U.S. participation in the IMF quota increase until Indonesia agreed to hold free elections. We expect the State conference report to go to the Senate floor shortly after recess ends; thus, his interest has been focussed on achieving its passage (with Mexico City language attached). Although he is pro-life and does not favor linkage, he believes that the Administration has not been flexible enough on this issue.

Chairman D'Amato (RER) ~46542

- Chairman D'Amato has been consumed by the debates on ISTEA and financial modernization. His primary concern will be whether any bilateral U.S. funds will be used in this round or in the future.

Senator Hagel (RER) ~44242

- You recently spoke with Senator Hagel regarding the assault weapons announcement. He wanted to discuss House IMF strategy. You should seek his counsel on what other steps we need to take to maintain Members' support in light of the revised agreement with Indonesia. You also spoke with him some time ago regarding the disposition of his constituent, Cal Energy, in Indonesia. A/S Geithner has communicated with Cal Energy recently. Cal Energy is pleased with Treasury's continued involvement and believes that their project is still extant. We will continue to monitor this situation to ensure that Indonesia employs a transparent, fair policy when determining which projects should proceed.

Chairman Stevens (RER) ~43004

c You spoke with him concerning the assault weapons announcement. He is still concerned about the national security aspect of maintaining stability in Indonesia. His staff and Chairman McConnell's staff are reported to be traveling to Indonesia on a fact-finding mission during the recess.

ATTACHMENTS: Talking Points

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C.

ASSISTANT SECRETARY

April 27, 1998

MEMORANDUM FOR DEPUTY SECRETARY SUMMERS
UNDER SECRETARY LIPTON

FROM: Assistant Secretary Geithner TFG

SUBJECT: Indonesia--Worker Rights

I sent the attached memorandum to State Assistant Secretaries Roth, Larson, and Shattuck recommending a letter from Secretary Albright to Indonesian Foreign Minister Alatas emphasizing U.S. concerns about the poor worker rights situation.

This issue will be a subject of discussion at the Wednesday, April 29 meeting chaired by Gene Sperling.

Attachment (1)

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C.

April 27, 1998

ACTION

ASSISTANT SECRETARY

MEMORANDUM FOR STANLEY ROTH
ASSISTANT SECRETARY OF STATE
EAST ASIA AND THE PACIFIC

ALAN LARSON
ASSISTANT SECRETARY OF STATE
ECONOMIC POLICY

FROM: Timothy Geithner
Assistant Secretary
International Affairs

SUBJECT: Indonesia--Worker Rights

ISSUE:

Despite high level discussions that State has had, serious roadblocks remain for the release of Mr. Pakpahan. The IMF believes it has made some headway, but that significant progress may only be achievable if the U.S. weighs in at a high level with the Indonesians, beginning with the Foreign Minister, to convince President Suharto that progress in these areas is critical for Indonesia's international standing and broad international support for Indonesia at this time.

ACTION REQUEST:

In the context of a broader message to the Government of Indonesia on human rights, we think it would be helpful if Secretary Albright wrote to Foreign Minister Alatas to emphasize the following points:

- We are writing to raise our serious concerns about Indonesia's respect for human and labor rights.
- We appreciate that Indonesia has recently indicated its intention to adopt three more ILO conventions related to core labor standards.
- To make adoption of additional conventions meaningful, Indonesia needs to conform its laws so that both the letter and spirit of these commitments are met.
  - o We understand that the Director General of the ILO has offered additional assistance to help Indonesia move to full implementation of its ILO commitments.
- In addition to adopting all of the ILO conventions related to core labor standards, we believe it is equally important to respond to the repeated ILO concerns over the past decade regarding freedom of association and the right to form independent unions.

- In this regard, Mr. Pakpahan, leader of the Indonesia Prosperity Trade Union, should be freed from jail at once.

- Further, the international community will be closely watching Indonesia's treatment of student demonstrators and for a noticeable improvement on its poor record on human rights.

- A lack of significant progress in all of these areas will be harmful to Indonesia's standing and to broad international support for Indonesia at this time.

- In addition, U.S. representatives in the international institutions will be raising these matters vigorously in the period ahead.

BACKGROUND

The IMF pressed Indonesia on specific labor issues: 1) the release of Mr. Pakpahan, the jailed leader of the Indonesia Prosperity Trade Union; and 2) ratification of the four remaining ILO conventions on core labor standards, including freedom of association.

The Indonesian economic team (Minister Ginandjar, in particular) indicated that it was, in principle, prepared to take some concrete steps on labor rights, but not in response to overt IMF pressure, nor did it want any of these steps to be part of an IMF program. Also, the team told the Fund that President Suharto would need to be convinced that the international community is paying close attention to these and associated issues (i.e., disappeared people, treatment of student demonstrators, respect for human rights), and that a lack of progress in these areas would harm Indonesia's international standing and broad international support for Indonesia at this time.

As you know, Indonesia's record on respect for worker rights is poor. Although Indonesia has adopted two of the six ILO conventions related to core labor standards (prohibition on forced labor and freedom to organize and bargain collectively), it has been criticized by the ILO for over a decade on its practices related to freedom of association and the right to bargain collectively. Moreover, recently there have been allegations of serious violations of Convention 29 on forced labor.

Therefore, although the Indonesian announcement that it would ratify three more ILO conventions on core labor standards (abolishing forced labor, freedom from non-discrimination, and prohibiting use of child labor) and would conform its laws to these conventions, it is important to understand that their standing in the international labor community would be better served if they made serious efforts to address long standing ILO concerns. Ratification of ILO conventions is welcome, but what is more important is action to address problems with existing commitments.

Indonesia would not commit to ratify the convention on freedom of association, which is the sixth ILO convention related to core labor standards. It is unclear whether Indonesia intends to address this convention.

cc: State A/S Secretary John Shattuck

April 22, 1998

Indonesia: Memo to State recommending a letter from Sec. Albright to GOI on worker rights

Drafted by: JMKotze/IDB JMK 622-1516

Reviewed by: MSobel/KLissakers JMK for MSobel
USED-IMF

JEichenberger/IDB JBE 4/22/98
D. Zelikow/IN DMZ 4/22/98
WSchuerch/ID WSS 4/22/98
xDxxtx

Clear M
[A. Samet/DOL cleared 4/24
[Bernard/NEC cleared 4/27

DEPARTMENT OF THE TREASURY
Washington

May 19, 1998

TO: Secretary Rubin
Deputy Secretary Summers
Assistant Secretary Robertson

FROM: Timothy Geithner TFG by dla

SUBJECT: Indonesia

Here are a few useful pieces on the IMF's role in the crisis in Indonesia.

We are in the process of drafting a short piece for the Secretary to send to the President.

Indonesia
Is the IMF Program Responsible for Indonesia's Collapse?

Question:

Isn't the IMF responsible for the current political unrest by imposing harsh austerity measures on the Indonesian people?

Answer:

- It is important not to confuse the doctor with the disease. The basic underlying cause of the crisis in Indonesia has been a fundamental loss of confidence in the policies of the Indonesian government. This led to a sharp decline in the value of the rupiah, intensifying inflationary pressures, and an accompanying deterioration in the economic situation.

- The IMF began working with the Indonesian government in November in an effort to help it deal with the effects of the broader Asian crisis on its economy. The program of economic reforms agreed to with the IMF at that time provided a sound foundation for restoring financial stability and improving long-run competitiveness in Indonesia.

- Indonesia's economic and financial situation continued to deteriorate, however, as the Indonesian public and international investors began to question the government's willingness to implement the reform measures agreed to with the IMF.

- This led to a profound loss of public confidence in the policies of the Indonesian government, causing the rupiah to plunge in value and the economic and financial situation to deteriorate markedly. This helped to provoke demonstrations by university students protesting against the government's failure to address the financial crisis and attacking government corruption.

- In the wake of the deteriorating economic conditions, the Indonesian government and the IMF agreed on a revised economic reform program in April. The government's earlier failure to act decisively to address the causes of the crisis meant that much stronger, and potentially more painful, medicine was required to restore financial stability.

- The government of Indonesia did make important progress in implementing the revised IMF reform program during April. These efforts, however, were quickly overwhelmed by the growing public dissatisfaction with the government of President Suharto and intensifying student protests throughout the country.

- While the energy price increases announced on May 4 do appear to have sparked some rioting and protests in Medan when they were announced, more recent violence in Jakarta appears to have been driven primarily by anger over the unprovoked shooting of university students by security forces and public support for political reforms.

    - It should be noted that the Indonesian government chose both the timing and size of the fuel price increases. The IMF program did not require fuel price increases until June 30 and allowed for more gradual increases in prices.

- We continue to believe that decisive implementation of the IMF reform program represented the surest and most effective way for Indonesia to restore financial stability.

- It is now clear, however, that economic reform measures will not be successful unless accompanied by political reforms desired by the Indonesian people. It is not the business of the IMF or the United States to impose these political changes on Indonesia.

SSS/INA; 5/19/98
IMFCAUSE.M19

Indonesia
Rollback of Required Energy Price Increases

Question:

Does Indonesia's rollback of energy price increases jeopardize the IMF program?

Answer:

- The Government of Indonesia (GOI) chose the timing and size of the fuel price increases announced on May 4. This action was not required under the IMF program until the end of June and could have been phased in more gradually at the discretion of the GOI.

- The IMF and Indonesia had previously agreed that kerosene prices were to be raised by less than other prices in an effort to limit the impact of these increases on the poor.

- According to the Indonesian government, the partial rollback of price increases announced on May 15 will cost approximately 2 trillion rupiah (more than $200 million). This increased spending on subsidies will have to be financed in some way, a difficult task given the large budget deficit (3.8% of GDP) that has already been projected for this fiscal year.

The economic and political situation in Indonesia has deteriorated significantly since the last IMF disbursement on May 4.

- The political unrest has heavily influenced market developments, with the rupiah depreciating significantly relative to the levels envisioned in the IMF program. This has important implications for inflation and the effect of fuel and food subsidies on the budget deficit in Indonesia.

- These developments will likely result in a reassessment of the economic assumptions and targets that form the basis of the IMF program.

Background:
The Indonesian government increased energy and fuel prices on May 4, although this step was not actually required until June 30 in the revised program. Indonesia also chose to fully implement the agreed price increases, rather than phase them in gradually.

- The Government's announcement of the price increases helped to spark violent protests in Medan in the following days. More recent violence in Jakarta appears to have been driven primarily by anger over the unprovoked shooting of university students by security forces and public support for political reforms, including the ouster of President Suharto.

Selected Fuel and Energy Price Increases (Rupiah per Liter):

	Prior to May 4	Effective May 5	% Change from May 4	Announced May 15	% Change from May 4
Kerosene	280	350	25.0%	280	0.0%
Gasoline	700	1200	71.4%	1000	42.9%
Auto Diesel	380	600	57.9%	550	44.7%

SSS/INA; 5/18/98
ENERGPRI.M18

Indonesia and Fuel Price Subsidies

In recent days, questions have arisen as to whether Indonesian fuel price increases -- consistent with a provision in Indonesia's IMF program to raise energy prices in the second quarter of this year -- triggered recent turmoil. As Deputy Secretary Summers stated the other day, however, one should not confuse the doctor with the disease.

Indonesia began experiencing a serious banking crisis last autumn which continues to this day. This crisis was influenced by the general Asia crisis and spread throughout the economy.

- o As confidence was lost in the banking system, depositors depleted accounts in weak banks and capital fled the country. The authorities provided massive liquidity support to weak banks, rather than closing them despite their insolvency.

- o This liquidity support triggered a huge surge in inflation and collapse in the rupiah. In the first quarter of this year, inflation rose at a 160%+ annualized rate, in contrast with Indonesia's recent history of single digit inflation. In January, the rupiah fell at one point by 70% against the dollar. Also due to the crisis, unemployment surged. In short, high prices and unemployment had begun ravaging Indonesia's poor many months ago.

- o Also, the authorities aggravated the crisis by refusing to tackle structural reform and corruption, firing the central bank's senior management and the head for bank restructuring and proposing a currency board rather than addressing central problems.

Against the background of the seriously deteriorating situation, Indonesia asked to resuscitate its IMF program. For the latter part of March and all of April, the IMF helped Indonesia design and begin implementing a revised package that would promote stability.

- o To gain control over the money supply, Indonesia cordoned off liquidity support to 14 banks that had been major uses of central bank financing.

- o The IMF insisted that the Suharto government break up monopolies, in such areas as cloves and forestry, that were associated with the President's children and friends.

The IMF staff also helped Indonesia redesign its 1998 budget with the objective of allowing for higher subsidies on some food and essential items to cushion the impact of the crisis on the poor, while holding to a workable budget that would not create further inflationary pressures.

- o Instead of a projected budget surplus of 1% of GDP, the program allowed for a deficit of 3.8% of GDP. This level of deficit is seen the maximum consistent with Indonesia's financing realities. Were Indonesia's deficit to rise much further, it is likely the central bank would print money, causing another surge in inflation and further rupiah collapse.

- o Government spending this year is projected at under 16% of GDP. The cost of subsidies will be 2.3% of GDP, making subsidies the second largest spending item. This estimate assumes a much stronger rupiah than now exists.

- o The cost of subsidies has been rising sharply due to the collapse in the rupiah. For example, the rupiah is now R11,000 per dollar. Many subsidized items are imported at world prices, while consumers are being charged at a cost of R6,000 per dollar with the budget making up the difference. Since Indonesia cannot target subsidies on the poor (e.g. through food stamps), all people -- rich and poor -- benefit from the subsidies.

- o To keep the level of subsidies consistent with Indonesia's financial envelope, Indonesia decided to reduce subsidies by 1-1/4% of GDP from what they otherwise would have been. Toward this end, prices of many items needed to be raised, and these were structured to protect the poor. For example, kerosene fuel prices were raised 25% as this is heavily consumed by the poor, but gasoline for cars was raised 71%. Subsidies for rice, the basic food staple of the poor, have been protected.

Withdrawal/Redaction Marker
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DOCUMENT NO. AND TYPE	SUBJECT/TITLE	DATE	RESTRICTION
003. memo	Mark Sobel (IMF) to Steve Saeger re: Indonesia (1 page)	05/18/98	P1/b(1) Unclass.

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jp26

RESTRICTION CODES

Presidential Records Act - [44 U.S.C. 2204(a)]

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P2 Relating to the appointment to Federal office [(a)(2) of the PRA]
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b(8) Release would disclose information concerning the regulation of financial institutions [(b)(8) of the FOIA]
b(9) Release would disclose geological or geophysical information concerning wells [(b)(9) of the FOIA]

May 15, 1998

Indonesia

Key points on Price Rises

A variety of concerns have been reported in the press as being among those responsible for the recent breakdown of law and order in Jakarta. These include, pre-eminently, questions of political reform and corruption. Certain reports have also referred to the price increases introduced under Indonesia's program with the IMF. However, as in all such cases, no precise assessment of causes is possible. It should be clarified that, in all cases, the IMF does not "impose" arbitrary or artificial timetables for price liberalization or subsidy removal measures; rather they are actions that are part of an agreed package of measures that is supported by IMF resources. This has been the approach followed in Indonesia, as in other countries.

In Indonesia, while price increases to help reduce subidies and control the budget were part of the package, the authorities in fact had wide discretion on the timing and pacing of those increases. The Indonesian authorities chose to implement the entire increase in one shot.

It should also be noted that kerosene and diesel—used by the poorer segments of the population—had much smaller price rises, by design, than gasoline—used in cars and more upscale public transport.

Finally, it should be pointed out that the wide ranging structural reforms envisaged in Indonesia's program have had no significant criticism from key opposition leaders and strong support from the public at large. The recent student demonstrations have had political reform as their objective. A number of permanent opposition leaders (Amien Rais, for example), have noted that economic reforms are essential for political reform.

1998-SE-006374

to: ______________________ Department of the Treasury

room: ________ date: ________ Executive Secretary

5/19

Mr. Secretary:

Mike asked me to fax the attached to you and ask that you call Tim about it this evening.

Neal

Neal C. Comstock
room 3408
phone 622-0064

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DOCUMENT NO. AND TYPE	SUBJECT/TITLE	DATE	RESTRICTION
004. letter	POTUS to President Soeharto re: Developments in Indonesia (1 page)	05/19/98	P1/b(1) Unclass.

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*** TX REPORT ***
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Comstock FYI

1998-SE-006436

'98 MAY 19 PM5:18

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C.

THE PRESIDENT HAS SEEN
5-20-98

SECRETARY OF THE TREASURY

May 19, 1998

Not log – will associate when rec'd
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MEMORANDUM FOR PRESIDENT CLINTON

FROM: Robert E. Rubin R.E.R.

SUBJECT: Criticism of IMF Policies in Indonesia

A number of recent press articles have suggested that the IMF bears responsibility for the deteriorating economic situation in Indonesia, as well as the recent surge in violence. According to these critiques, the IMF-backed reform program imposed unnecessarily harsh or ill-advised reform measures on Indonesia, causing a sharp fall in the value of the rupiah, a run on the banking system, and an unnecessary increase in sensitive prices that helped precipitate the recent violence. These criticisms confuse the reasons for and the effects of the crisis with the appropriate response.

The pain which the Indonesian people are currently suffering is the result of the economic and financial crisis, a series of policy missteps by the Indonesian government, and by a profound loss of confidence in President Suharto. The policy reform measures supported by the IMF and the financial assistance provided by the international financial institutions were designed carefully to restore stability and growth as quickly as possible and to cushion the impact of the crisis on Indonesia's most vulnerable citizens.

The IMF program did not induce the crisis or magnifiy its costs on the Indonesian people. The broader loss of confidence that is the cause of the current political and economic crisis occurred not because of the policies backed by the IMF, but as a result of the Indonesian government's *failure* to decisively and fully implement its commitments under the IMF program.

The Indonesian government must therefore bear responsibility for the current political unrest and violence. The reform program originally agreed to by the IMF and the Indonesian government in November provided a sound foundation for restoring financial stability and improving the long-run competitiveness of the Indonesian economy. Had the Indonesian government enacted necessary economic reforms four months earlier when first prescribed by the IMF, it could have avoided the massive hardship and pain which millions of its citizens must now endure.

- The progress both Korea and Thailand have made in restoring financial stability in recent months is a testament to the fact that implementation of sound policy measures prescribed by the IMF is the surest path to economic and financial recovery.

Among the most serious mistakes made by the Government of Indonesia in its handling of the economic crisis was the provision of massive and uncontrolled liquidity support to the banking system. This is the primary economic factor underlying the fall in the rupiah and accelerating inflation, which must ultimately be reflected in fuel and food prices. The government's failure to decisively implement structural commitments in its IMF program also contributed to the loss of confidence in the Indonesian government, leading to a further fall in the value of the rupiah.

- The Indonesian government's failure to prevent violence directed at Chinese-Indonesians earlier this year may have also contributed to the flight of capital that exacerbated the initial crisis.

The Government of Indonesia did make important progress in implementing the revised IMF reform program during April. These efforts, however, were quickly overwhelmed by the growing public dissatisfaction with the government of President Suharto and intensifying student protests throughout the country.

- While the energy price increases announced on May 4 do appear to have sparked some rioting and protests in Medan when they were announced, these increases were part of the difficult measures needed to address the crisis, and it is the crisis, not the measures to deal with it, that is the real cause of political instability. The more recent violence in Jakarta appears to have been driven primarily by a strong public desire for political reform and anger over the unprovoked shooting of university students.
    - It should be noted that the Indonesian government chose both the timing and pacing of the fuel price increases. The IMF program did not require fuel price increases until June 30 and allowed for more gradual increases in prices, but the Government of Indonesia decided to increase prices more quickly and more precipitously.
    - Given the depreciation of the rupiah, fuel price increases were unavoidable if the Indonesian government was to bring its budget deficit under control. The budget deficit will rise to at least 3.8% of GDP this fiscal year and would have been much higher if the Government of Indonesia had failed to take steps to reduce fuel subsidies.
    - The large projected budget deficit will be financed primarily by the IMF and other international financial institutions. Without this international support, energy prices would have had to rise even faster and higher, as Indonesia does not currently have the capacity to finance this deficit domestically. The only alternative would have been to finance these subsidies by printing more rupiah, which in turn would have resulted in a debilitating hyperinflation that strikes most deeply at the poor.

The IMF showed considerable flexibility in working with the Indonesian government to ease the burden on the poor as much as possible.

- It allowed Indonesia to run higher budget deficits than originally agreed to in order to give the government greater latitude to provide subsidies.

- The price of kerosene, which is heavily used by the poor, was increased only 25%, significantly less than the rate of inflation during the first four months of the year. Its real price has therefore declined. By contrast, the price of premium gasoline, primarily consumed by middle and upper-class citizens of Indonesia was raised by slightly more than 70%. Even with this price change, gasoline prices are estimated to be only half of international prices at current exchange rates.

We continue to believe that the prescriptions advocated by the IMF have represented, and continue to represent, the best possible path for Indonesia to restore financial stability and growth to its economy. It has become increasingly clear, however, that these reforms can no longer be successful unless accompanied by significant political reforms. While President Suharto's announcement of his intention to stand aside is a hopeful sign, it is unclear that this will be enough to stabilize the situation. We will continue to follow events in Indonesia closely in conjunction with the Department of State.

CHIEF OF STAFF TO THE PRESIDENT

THE PRESIDENT LIKED THIS ~~~~ AND WANTS ALL SPOKESPEOPLE TO READ IT.

1998-SE-006651

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C.

ASSISTANT SECRETARY

JUN 0 1998

MEMORANDUM FOR **SECRETARY RUBIN**
DEPUTY SECRETARY SUMMERS
UNDER SECRETARY LIPTON

FROM: Timothy Geithner
Assistant Secretary (International Affairs)

SUBJECT: Indonesia

This is an update on Indonesia and the choices we face in the short-term.

Economic and Financial Assessment: Hubert Neiss debriefed the Board on his mission to Jakarta yesterday and delivered a bleak assessment of the current economic and financial conditions. Indonesian economists are now predicting a decline in GDP of 10-15%, with inflation accelerating to as high as 100% (consumer price inflation data for May released yesterday already put year-over-year inflation at 52%). Manufacturing capacity utilization has been slashed and the distribution networks were severely disrupted by riots last month and the resulting flight of many ethnic Chinese traders. The banking system is also teetering ever closer to collapse, as deposit runs directed at banks associated with the Suharto regime underscore continuing doubts about the credibility of the government's guarantee of bank liabilities.

Fiscal Situation: The continued weakness of the rupiah (still stuck below 11,000), deteriorating banking system and plunging economic activity will put even greater pressure on the government's budgetary situation. While the revised IMF program agreed to in April allowed for a budget deficit of 3.8% of GDP, the combination of rising subsidy costs for essential imports, bank recapitalization, and declining tax revenues could lead to a deficit of as much as 6%-7% of GDP during this fiscal year.

- There appears to be relatively little scope to reduce the deficit given the political and social sensitivity to further price increases that would reduce the cost of subsidies. The increased deficit therefore likely will require \$3-\$4 billion of additional financing, much of which will need to come from external official sources given the difficulty of tapping domestic or international investors for deficit financing.

- The IMF is likely to seek additional up-front money in order to close this financing gap. There appears to be only limited scope for acceleration of existing IFI financing plans for Indonesia, so it is likely that bilateral sources will also be sought.

Corporate Debt Talks: The IMF reports that substantial progress was made on corporate debt restructuring talks with the co-chair banks last week in New York. These talks have reconvened in Frankfurt this week with the full creditor steering committee. The Fund thinks that the co-chairs now have a much more realistic view of what is possible from the standpoint of Indonesia's fiscal situation, although it is unclear whether the broader steering committee is fully on board.

- There are still some issues to work out on the tentative agreement to roll over interbank lines and to maintain trade finance exposures, but these should not prove to be a major stumbling block to a final agreement. It is nonetheless true that Indonesia's trade financing problems now appear to be driven primarily by the unwillingness of Indonesian banks to take on any exposure to Indonesian corporates, not the lack of available funds to back letters of credit.

Political Situation: The political situation is substantially better than we could have hoped for three weeks ago, although it remains fluid, with considerable uncertainty about the nature and timetable for the political transition now underway. President Habibie and parliamentary leaders have reportedly agreed on a two-step process that could take as long as 18 months before a new presidential election. While some key opposition leaders such as Amien Rais appear willing to give the Habibie government a year in which to institute necessary political reforms, others continue to favor an immediate session of the MPR (parliament) to put in place an interim administration. The military has remained noticeably silent, with some former generals publicly advocating Habibie's immediate ouster.

- Even if the Habibie government further clarifies its timetable for planned political reforms, it is unlikely that there is a solution that will satisfy all elements of Indonesian society. Political jockeying has intensified as potential rivals for the presidency try to figure out what type of reform process will best suit their aims.

IFI Plans: The World Bank, Asian Development Bank and IMF are all making preparations to restart the substantial amounts of assistance now in the pipeline.

- With our encouragement, the World Bank board approved a $225 million rural employment project loan today.

- The managements of the World Bank and the ADB would also like to schedule board dates for consideration of two large loans, a $1 billion WB structural adjustment loan and a $1.5 billion ADB financial sector loan. We have suggested that both institutions delay setting dates for consideration of these loans until we have the opportunity to assess whether the political transition scenario outlined by the new government will generate the restoration of confidence necessary for a successful program.

  - The World Bank appears to be on a trajectory that would allow the Fund team to spend next week in Jakarta working on the macroeconomic framework, with Board consideration of the SAL on June 16 or 18. This timing will give us some additional time to assess the political situation without necessarily appearing to be obstructive.

- The IMF plans to send a new team to Jakarta late this week and expects to spend between two and three weeks revising the program before asking the Board to consider the next tranche.

Short-Term Policy Choices: We face the following policy choices in the short-term:

What types of assurance about the political outlook will be necessary before we support a resumption of non-humanitarian IFI assistance?

We are likely to face increasing pressure from the international community to move ahead, in the face of considerable uncertainty and risk about the political outlook. The proponents of early reengagement can make a credible case that delay now could cause serious further damage to the people of Indonesia, even though they would acknowledge that ultimately there will be no enduring recovery with confidence in the political situation.

- In this context, we have been encouraging State to urge Habibie to lay out a clearer, shorter timetable for a transition process that will enjoy widespread support.

- We must recognize, however, that the current uncertainty over the political transition may not dissipate over the next several weeks, even if Habibie follows our advice.

What approach should we take if we fail to see greater clarity on the political outlook?

We are likely to be isolated internationally if we attempt to further delay non-humanitarian funding unless there is a renewed deterioration in the political situation. This also may be accompanied by charges that the U.S. is attempting to dictate the course of Indonesia's political transition.

- A delay of ADB and WB board consideration of non-humanitarian lending until the third week of June is justified on both technical and political grounds. It will take until the end of next week for the Fund mission to get a better handle on the macroeconomic situation. This delay would also allow us some time to see whether opposition forces in favor of a much faster transition can muster significant popular and/or military support. The World Bank now appears to be on this trajectory.

- It also will be helpful to get Stan Roth's assessment of the situation in Jakarta following his trip there this week.

Should we be more proactive in indicating our support for relaxation of the Fund program's fiscal targets and rephasing of price increases?

The IMF is unlikely to push for the types of strong policy measures (increasing controlled prices and cutting expenditures) that would be necessary to close the fiscal deficit given its understandable desire not to be blamed for further rioting or protests.

- Flexibility on the fiscal situation in Indonesia appears to be justified given our concern that the impact of the crisis on the Indonesian people be cushioned as much as possible.

- We may want to signal publicly our support for IMF flexibility on these issues, while also stressing that the IFI's should play a critical role in strengthening Indonesia's social safety net. While the IFIs appear to share our views, it may be helpful in our relations with some on Capitol Hill and in the region to highlight our support for this approach.

- We should also recognize, however, that loosening the fiscal targets in the IMF program will most likely require the Indonesians to seek increased official financing. This may well lead to a push for more direct bilateral financial support from the U.S..

Should we support more front-loading or acceleration of IFI money, provided the IMF has a strong case?

- IFI management may be resistant to accelerated or additional financing from the ADB and World Bank at this juncture given high existing exposures to Indonesia. The existing pipeline of loans already figures into the IMF's financing scenarios from April, so acceleration would most likely require moving forward with loans currently planned for 1999 and beyond.

  - The IMF currently is scheduled to disburse approximately $2.8 billion in additional funding over the next three months, with additional tranches of $780 million each scheduled for November and February 1999. The remaining $1.6 billion of the Fund program is spread out with quarterly disbursements from May 1999 to October 2000.

  - The World Bank currently has a $400 million agricultural SAL, $600 million financial sector SAL, and $300 million urban employment project loan in its pipeline for its next fiscal year (starting July 1). The Bank has no additional plans for adjustment lending for Indonesia.

  - The ADB committed $1.7 billion in crisis-related financing for Indonesia in addition to the $1.8 billion that will likely come up for board approval this month. The Bank does not currently appear to have done any planning regarding the timing or nature of these additional lending operations.

- It is likely that additional bilateral support will be sought to cover part of the financing gap. The Japanese, Australians and Malaysians have all offered to disburse portions of their second line of defense funding in one form or another, although most of this financing does not appear to be designed to provide budgetary support.

- The only viable domestic source of financing in the near-term is most likely Bank Indonesia's foreign currency reserves, which could be run down slightly by allowing for some growth of net domestic assets.

  - According to the most recent public releases by Bank Indonesia, liquid reserves totaled $12.5 billion on May 22, which would provide coverage of nearly 5 months of imports at current levels.

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DOCUMENT NO. AND TYPE	SUBJECT/TITLE	DATE	RESTRICTION
005. memo	Lawrence H. Summers to POTUS re: Your Meeting with President Wahid of Indonesia (1 page)	11/10/99	P5

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Presidential Records Act - [44 U.S.C. 2204(a)]

P1 National Security Classified Information [(a)(1) of the PRA]
P2 Relating to the appointment to Federal office [(a)(2) of the PRA]
P3 Release would violate a Federal statute [(a)(3) of the PRA]
P4 Release would disclose trade secrets or confidential commercial or financial information [(a)(4) of the PRA]
P5 Release would disclose confidential advise between the President and his advisors, or between such advisors [a)(5) of the PRA]
P6 Release would constitute a clearly unwarranted invasion of personal privacy [(a)(6) of the PRA]

C. Closed in accordance with restrictions contained in donor's deed of gift.
PRM. Personal record misfile defined in accordance with 44 U.S.C. 2201(3).
RR. Document will be reviewed upon request.

Freedom of Information Act - [5 U.S.C. 552(b)]

b(1) National security classified information [(b)(1) of the FOIA]
b(2) Release would disclose internal personnel rules and practices of an agency [(b)(2) of the FOIA]
b(3) Release would violate a Federal statute [(b)(3) of the FOIA]
b(4) Release would disclose trade secrets or confidential or financial information [(b)(4) of the FOIA]
b(6) Release would constitute a clearly unwarranted invasion of personal privacy [(b)(6) of the FOIA]
b(7) Release would disclose information compiled for law enforcement purposes [(b)(7) of the FOIA]
b(8) Release would disclose information concerning the regulation of financial institutions [(b)(8) of the FOIA]
b(9) Release would disclose geological or geophysical information concerning wells [(b)(9) of the FOIA]

EXECUTIVE SECRETARIAT CORRESPONDENCE MEMO COVER SHEET

Wednesday, November 10, 1999

PROFILE #: 1999-SE-012313

DATE CREATED: 11/10/1999

ADDRESSEE: Lawrence H. Summers
Secretary

AUTHOR: Geithner, Timothy
International Affairs

SUBJECT: POTUS Note On Indonesia For Visit Of President Wahid

ABSTRACT: POTUS note on Indonesia for visit of President Wahid.

RM 3419

TO REVIEWERS

IN:

TO EXECUTIVE SECRETARY

IN:

TO THE SECRETARY

DATE SIGNED:

DISTRIBUTION: AS, INTERNATIONAL AFFAIRS

11/10 NCC to LS (signature)

11/11 LS ok to autopen per NCC

NCC autopenned

NCC original to WH

11/12 NCC cc to SE (reading)

SS
TS
CK
AK/PA

11/10/1999 05:07:05 PM

1999-SE-012313

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C.

UNDER SECRETARY

November 10, 1999

ACTION

MEMORANDUM FOR SECRETARY SUMMERS

FROM: Timothy F. Geithner, Under Secretary
(International Affairs)

SUBJECT: POTUS Note on Indonesia for Visit of President Wahid

Action Forcing Event

President Wahid of Indonesia will be in Washington on November 12 and is scheduled to meet with POTUS.

Background

Strong leadership from President Wahid will be needed on critical economic and governance issues. A note to POTUS is an effective means of bringing to POTUS's attention key economic issues that we believe he should raise with President Wahid.

Recommendation

That you sign the attached memo.

Agree _______ Disagree _______ Let's Discuss _______

Attachment:

Tab A: Memorandum to the President

cc: A/S Truman

TREASURY CLEARANCE SHEET

NO.________
Date 11/10/99

MEMORANDUM FOR: ■ SECRETARY ☐ DEPUTY SECRETARY ☐ EXECUTIVE SECRETARY
■ ACTION ☐ BRIEFING ☐ INFORMATION ☐ LEGISLATION
☐ PRESS RELEASE ☐ PUBLICATION ☐ REGULATION ☐ SPEECH
☐ TESTIMONY ☐ OTHER

FROM: Timothy F. Geithner
Under Secretary (International Affairs)

SUBJECT: POTUS Note for Meeting with Indonesian President Wahid

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☐ Under Secretary for Finance
☐ Domestic Finance
☐ Economic Policy
☐ Fiscal
☐ FMS
☐ Public Debt
☐ Inspector General
☐ IRS
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☐ Customs
☐ FLETC
☐ Secret Service
☐ General Counsel
☐ Mint
☐ Savings Bonds
☐ Other
☐ Policy Management
☐ Scheduling
☐ Public Affairs/Liaison
☐ Tax Policy
☐ Treasurer
☐ E & P
☐ Under Secretary (International)
☐ Legislative Affairs
☐ OCC

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SPECIAL INSTRUCTIONS

☐ Review Officer Date ☐ Executive Secretary Date

DO F 80-02.1 (04/89)