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27 October 1954

PROPOSAL FOR AN EIC STUDY OF  
INDONESIAN ECONOMIC DEVELOPMENTS AND PROBLEMS, IN THE LIGHT OF  
FREE WORLD AND COMMUNIST ECONOMIC INTERESTS AND INFLUENCES

I. Purpose of Study

1. There is serious concern at policy levels in the U.S. Government as to the implications for the U.S. and the Free World generally of emerging developments in Indonesia. As one expression of this concern, for example, the Operations Coordination Board has recently established a working group to watch developments in the Indonesian situation. This group has already requested material from the intelligence community to support an over-all study of the political situation in Indonesia, due early in December.

2. In developing an over-all picture of the Indonesian economic situation, the most important aspects seem to be the following:

a. A careful survey of the economic importance of Indonesia to the Free World and the Soviet Bloc, respectively - as a supplier of important raw materials and as a consumption market for other products.

b. As full as possible a picture of developing internal and external economic pressures within the area. This is needed to guide U.S. and other Free World government policy decisions affecting Indonesia's foreign trade opportunities, and the financial and technical assistance available to her from the Free World - in time to influence effectively her orientation as between the Free and Communist Worlds.

II. Need for a Coordinated Study

1. Several summaries and a number of sector studies on particular aspects of the Indonesian economy are available; but most of these are already several years out of date. The statistical data presented are generally even less recent - being based largely on 1949 to 1951. There is no recent comprehensive study covering the Indonesian economy as a whole.

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State Dept. review completed. On file USDA release instructions apply.

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 CIA has no objection to declass  
 It contains information of CIA interest that must remain classified at TS S  
Date 4-14-80 Reviewer [Signature]

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2. Within the IAC intelligence community only the Department of State has undertaken specific analysis of major aspects of the Indonesian economy within the past 18 months. (A single study completed in September 1954 reflects data later than 1952.) Of NIS-100 on Indonesia, only the supplement on petroleum has been completed. None of Chapter VI - "Economic" - has even been scheduled, and Chapter III - "Transportation and Telecommunications" - is scheduled only for 1955 and 1956.

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3. On the other hand, there is a great deal of material awaiting exploitation - in the form of detailed data, brief reports on specialized items (i.e., petroleum, rubber, land reform, etc.), and background information in the heads of a number of knowledgeable individuals - on which a comprehensive study might be based. Such a project will require drawing on documents and knowledge available throughout the EIC community, particularly in the Department of State, in FOA, in the Department of Agriculture, and in CIA. Important specialized material on transportation and communications aspects could also be contributed by G-2, ONI, and AFOIN.

### III. Recommendation

It is proposed that a comprehensive study of Indonesian economic developments and problems be initiated by the EIC and assigned to a special working group, chaired by the Department of State.

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(HIGHLY TENTATIVE)

POSSIBLE OUTLINE FOR STUDY

OF INDONESIAN ECONOMIC DEVELOPMENTS AND PROBLEMS

- I. General Description of Area, with Principal Regional Distinctions (i.e., between Java/Bali and the various Outer Islands)
  - A. Over-all economic pattern for entire area (including transportation and communications systems)
  - B. Specialized economic situations, by regions (Java/Bali, and other principal island groups, separately)
- II. Analysis of Principal Products of International Importance
  - A. Present over-all foreign trade picture
  - B. Analysis of principal individual products involved (e.g., petroleum, rubber, tin, rice, etc.)
  - C. Significance of above items in trade patterns of Free World and of Soviet Bloc
- III. Principal Indonesian Economic Problems
  - A. In internal economy
    1. Over-population and its results
      - a. Per capita income and saving
      - b. Per capita availability of food and other supplies
      - c. Overcrowding of villages and land (distribution inequities)
      - d. Under-employment, and pressure for transmigration
    2. Shortages of trained administrators, entrepreneurs (special position of Chinese), teachers, and technicians
    3. Limited industrial development (small-industry opportunities)

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4. Internal transport and communications difficulties
  5. Budgetary deficits, and inadequacy of governmental services in education, public health, agricultural production and marketing, etc.
  6. Institutional factors and administrative attitudes impeding economic development
- B. In international balance of payments
1. Trade deficits, and recent depletion of reserves of exchange
  2. Shortage of international capital for investment
  3. Special international marketing problems for Indonesian surpluses (e.g., sugar quotas, COCOM regulations, copra and tin prices, etc.)
- C. Arising out of popular and official attitudes toward economic ties with the Free World and/or the Soviet Bloc
1. Historical ties and strains since World War I (anti-colonialism)
  2. Recent and present U.S.' and other non-Bloc countries' economic policies toward Indonesia (e.g., relatively small aid compared to grants to other countries, artificial barriers to disposal of Indonesian products, etc.)
  3. Soviet economic relations and proffers of assistance
  4. Economic influences of the internal Communist movement
- IV. Analysis of Available Measures which might be Appropriate for Improving Indonesian Economic Conditions, including:
- A. A consideration of the extent to which remedial measures lie within the power of the Indonesian Government, or would appear to depend materially on foreign assistance of various types
  - B. A problem-by-problem discussion of the specific remedial measures necessary, and the specific assistance measures which might be effective economically - provided such aid were considered politically justified

PROPOSED EIC STUDY ON INDONESIAN ECONOMIC DEVELOPMENTS AND PROBLEMS

3. Action: A small working group was established by the EIC to examine the proposed study on Indonesia in order to:

a. Compare the terms of reference proposed by the DDI/CIA, for an EIC study, with planned outlines of studies being undertaken by the State Department as a contribution to the next NIE on Indonesia and for the Hoover Committee on Asian problems of the NSC.

b. Decide whether any additional work would be required to meet the needs of the requestor and, if further work needs to be done, make appropriate recommendations to the EIC as to how additional contributions might be arranged.

Mr. Edward Fried of State was designated as chairman of the group and Mr. Fred Ritchie and Mr. Clarence Purves were nominated as representatives of FOA and Agriculture respectively. The service agencies may wish to designate members at a later date. The Executive Secretary, EIC, was asked to provide secretariat services for the group and any necessary liaison with the principal requestor.

ESTABLISHMENT OF AN EIC WORKING GROUP TO FACILITATE COORDINATION OF ECONOMIC CAPABILITIES CONTRIBUTION BY CIA/ORR TO NIE-11-9-54

4. Action: Approval was given to establishment of an "ad hoc" working group to aid in the implementation of Step Three in the "Procedure" of the Terms of Reference for NIE-11-9-54. Members designated were as follows:

25X1A [redacted] CIA, Chairman  
Mr. Daniel H. Gagon, AFOIN  
Colonel Lyman Bothwell with Mr. Duncan Holmes  
as alternate, G-2  
Commander Burns Spore, ONI (as ONI participation is  
required)  
Mr. John Easton, JCS  
Mr. Lawrence S. Dreiman, EIC, Executive Secretary for group.

Mr. Dreiman proposed that the first meeting be held early the following week.

PROPOSAL FOR WORKING GROUP ON PRODUCTION ASPECTS OF SOVIET GUIDED MISSILES PROGRAM

5. Discussion: The members generally were reluctant to approve the CIA proposal for establishment of a special working group at this time. The Air Force representative suggested that the economic aspects might be covered on a "stop-gap" basis by arranging for ORR participation in the present AFOIN interdepartmental working group already responsible for scientific and technical aspects of Soviet guided missiles production.

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was still premature. Copies of a descriptive note on the EIG - which had been prepared by the ORR representative [ ] - were distributed for general information.

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NIE POST MORTEM

3. Discussion: Dr. Guthe called the attention of the members to the post mortems (TS) of NIE production which appear semiannually and which bring out the principal deficiencies in present research and collection efforts. He suggested that members not already familiar therewith might refer to IAC-D-57/2, 16 November 1954.

STATUS OF INDONESIAN STUDY

4. Discussion: The Chairman reported that the Department of State had submitted an excellent draft outline for the economic section of the new NIE on Indonesia, and that this appeared to be also a most appropriate outline for the study which had been requested by the DDI/CIA. State was proceeding with the preparation of this report as outlined, with G-2 and ONI submitting formal contributions to State on special aspects. It was understood that the finished contribution by State will be circulated to the members of the working group established 2 December 1954, for comments and consideration of the extent to which it meets the requirements of the DDI/CIA. On the basis of comments of the members of the working group the EIC will decide at that time whether or not any revisions of the State Department contribution are needed to incorporate additional material from other members of the EIC community.

The State Department member stressed that OIR would maintain close contact with both FOA and OFAS/Agriculture during the preparation of State's contribution.

SERVICES OFFERED BY THE EXTERNAL RESEARCH STAFF OF STATE DEPARTMENT

5. Discussion: Mr. Howard Penniman, Chief of the External Research Staff of State Department, briefly outlined the facilities and services which ERS generally offers to members of the economic

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September 14, 1955

Mr. Joseph Yager, OIR  
Department of State

Frank M. Charrette, M/RSR

OIR Report "The Status of the Indonesian Economy" (IR 6865)

As a member of the EIC, ICA submits herewith its comments on the subject report.

The report presents an extremely useful picture of the Indonesian economy which will be valuable for reference, briefing and program planning purposes. The generalizations appear to be drawn from a careful weighing of the relevant factors.

The most significant comment to be made relates to developments which presumably could not have been foreseen with assurance when the document was in preparation. Nevertheless, in light of the recent turn in political events in Indonesia, and the changed balance of power which might result from the election this month, the report will be more useful if it is updated and revised accordingly.

The following comments are offered for inclusion in the recommended updated report:

1. It should be made clear that U.S. economic aid to Indonesia was held to small amounts in the last several years because of unpropitious political conditions and questionable receptivity; not because there was no need for more economic assistance.

2. It would be useful to indicate the nature of the sort of U.S. aid program that would advance our interest in Indonesia if political developments take a favorable turn. This should be tied to an up-to-date statement of U.S. economic objectives in Indonesia. This part of the picture might be completed by a projection of the progress which the Indonesian economy could be expected to make in about 5 years with this aid and with such other assistance (loans from IBRD, Export-Import Bank, etc.) as might reasonably be anticipated.

3. Although the impact of past U.S. economic assistance to Indonesia can hardly be distinguished from the effects of Indonesia's own efforts, the uses to which U.S. aid has been put could be elaborated to some advantage.

4. The abstract of the report does not seem to reflect the possible long-term capabilities indicated on page 45.

5. The status of the cottage industries might well be discussed briefly, especially inasmuch as they are so highly organized in Indonesia.

6. It would be helpful if the amounts of foreign aid, discussed on page 35, were integrated briefly in the treatment of government finance on page 15.

7. The section on foreign aid (pages 35-36) does not reflect that Indonesia recently has shown interest in U.S. economic aid programs, i.e., P. L. 480 and development assistance.

8. The U.S. technical assistance discussed on page 35 could be stated with more precision. It amounted to \$4 million in FY 1953 and FY 1954. In FY 1955, it was \$7.5 million, which included \$1.8 million for a special malaria control program.

9. With reference to the role of the J.G. White Co., indicated on page 33, it would be more accurate to state merely that J. G. White, a firm of U.S. construction engineers, has been under contract with the Indonesian Government since 1951 through ICA financing. Inasmuch as J. G. White reports are not made available to the U.S., it is impossible to evaluate their effectiveness.

10. An error appears in table 7 on page 56. The estimated total current account for FY 1954 should be \$-47.8 million, resulting from the trade balance of \$160.0 million and the deficit of \$207.8 million in total invisibles.

CC: Mr. Clarence Purvis (Agriculture)  
[redacted] (CIA)  
Mr. Martin Mulholland (ICA)

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13 September 1955

Members of the Economic Intelligence  
Committee on Indonesia

Clarence M. Purves, Deputy Director,  
Foreign Agricultural Analysis Division, FAS,  
U.S. Department of Agriculture

IR-6865: The Status of the Indonesian Economy

As a member of the EIC working group on Indonesia established last December, I have reviewed the Intelligence Report on the status of the Indonesian economy and have discussed it with other interested members of the Department. In general we feel that it is undoubtedly the most thorough report available on Indonesia and that the State Department did an excellent job in bringing together the material on the Indonesian economy, particularly in view of the short time available.

The factual information on agriculture was essentially in agreement with such data as we have in our files. There are slight differences in a few cases but they are not enough to make any difference in the conclusions reached.

I should like to point out, however, that we had relatively little opportunity to contribute to the preparation of this report. Dr. Anderson, Mr. Koenig and I had one meeting with Mr. Smuckler, at which time they discussed the general outline of the report on agriculture and provided him with such information as we had in our files. Because of the short time for preparing the report, Mr. Smuckler was unable to let us review it before it was published. If we had had a chance for such a review, we would have liked to have made the following suggestions:

1. There are some assumptions as to the importance of world trade of Indonesia with which we do not agree. Indonesia is an important source of rubber, petroleum, tin, bauxite, palm oil products, spices and medical drugs. For many of these products, it has comparative advantage over any other area in the world. These are all products of considerable value to both the free world and the Communist world. We feel the report underestimates the value of the products to both areas. To say that these products are of no immediate importance to the United States and perhaps not even too important to the Sino-Soviet Bloc is a very short-sighted view and one that needs further consideration. While there are surpluses of many of these products at the present time, the situation could change quickly and because of the strategic location of these supplies in Indonesia, they could be extremely valuable to either side.
2. Since Indonesia is primarily an agricultural country and one of the principal problems is developing an expanding agriculture

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- to provide an adequate diet for the people and also to provide some exports in order to obtain foreign exchange, we feel that the agricultural section could have been given a more thorough analysis than was done.
3. It is also our feeling that the report did not adequately appraise the significance of the technical development programs being conducted in Indonesia by ICA and FAO and the problems which these development programs are designed to meet.
  4. A report of this type should give more attention to the longer term aspects of economic development and to the problems which may arise in Indonesia as a result of population growth and efforts to redistribute the population among the less densely settled islands.
  5. The analysis in the report indicates pretty clearly that the economy of Indonesia is in a stagnant condition and that productivity and capital formation are inadequate to assure a tempo of economic development that will bring Indonesia "off the fence" and into the community of free nations, yet there is no analysis of specific measures for accelerating economic development, although several such programs have been discussed between the United States and Indonesian officials in recent months.
  6. The report does not bring out how programs under P. L. 480 might further market development in Indonesia and might also, at the same time, be of great assistance to the Government of Indonesia in replanting her rubber acreage with high yielding clones, thus greatly enhancing productivity among rubber workers.
  7. The analysis in the report might have indicated more clearly the necessity for Indonesia to develop her basic natural resources so as to permit her to earn enough additional foreign exchange significantly to foster productivity. This means procuring the facilities and power and knowhow for processing primary products such as bauxite and tin ores. The report might well have indicated the immense potential demand among 1.5 billion Asiatics for aluminum and tin products.

In view of the above-mentioned limitations to the report and the rather significant changes in recent months, we would like to suggest that the report is now outdated and that more attention should be given to the above points and to the potential significance of the increased interest Indonesia is

showing in certain aid programs and in P. L. 480, which, at the time this paper was written, seemed unimportant to Indonesia.

If the EIC is in agreement with our suggestions to review and expand the report, particularly on agriculture, we would like to suggest that the EIC working group which now consists of representatives of State, ICA, CIA, and Agriculture, be authorized to proceed with the preparation of such a report.

CC: Mr. Joseph Yeager, State  
Mr. Mulholland, ICA

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CMFurves/PM/  
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Attachment 3

(Based on comments of [ ] as a member of the EIC Working Group on Indonesia.)

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STATE DEPARTMENT INTELLIGENCE REPORT No. 6865  
"THE STATUS OF THE INDONESIAN ECONOMY"

This report impresses me as a very comprehensive and well-written summary of OIR materials on the Indonesian economy. It is the most extensive paper on any of the key peripheral non-Bloc economies which has come to my attention in several years. It illustrates admirably the value of having (in the Office of Intelligence Research, State Department) a competent professional staff with the necessary background and available files of material to turn out occasional studies of this type -- on short notice.

On the other hand, the paper shows internal indications of having been essentially the product of a single agency, and somewhat limited in outlook. Although the State Department representative in the EIC Meeting on 17 December emphasized OIR'S intent "to maintain close contact" with the other members of the Working Group during the preparation of this paper, it is my understanding that the only "coordination" which was felt feasible consisted of brief contacts between the author of the paper and individual analysts of Agriculture and FOA (assigned to their Indonesian desks) to obtain certain data from the files of these other offices. I personally urged that the other members of the Working Group be shown this report in earlier draft -- after the NIE rush "deadline" had been met (in February) but prior to its final publication over 90 days later. Had this been done, some rather important ideas of other members of the Working Group might have been easily taken into account by the author -- and the final OIR paper been significantly improved as a result.

At this late date<sup>1</sup> critical evaluation tends to reflect a markedly improved climate of opinion for external aid to Indonesian economic development, as a result of important political changes in Indonesia since last winter. Nevertheless, the following criticisms remain essentially those indicated to our working group Chairman when I first read this paper (as a contribution to a National Intelligence Estimate) some six months ago. In summary -- the paper fails to come to grips with practical problems of Indonesian economic development and with the relationship of U.S. and other external aid programs to such development. Specifically:

1. The analysis includes no adequate discussion of the specific aims, operations, accomplishments, and future possibilities of the Foreign Operations Administration (now ICA), Export-Import Bank and other U.S., U.N. or Netherlands programs for assisting Indonesian economic development. Yet grants and loans under these programs are stated to have

1. The non-IAC members of the Working Group were sent the report only in late June, by which time most of those involved had left town or were tied up for the summer.

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totalled nearly \$300,000,000 since World War II. And more than 100 American technicians have been assisting the Indonesians (on the FOA or engineering-contract staffs) for the past several years.

- a. Even where U.S. aid has directly contributed to such solutions of problems as are discussed in the report, the author fails to indicate any connection. For example, a paragraph on page 4 spells out at length the improved supply of protein which resulted from a sharp increase in the fishing catch -- based on expansion and motorization of the Indonesian fishing fleet and a government distribution program for fingerlings -- yet there is no indication that the U.S. Technical Assistance Program was directly responsible for these developments and actually paid for the motorized trawlers!
- b. The discussion of "foreign aid" (pages 35-36) gives no specifics as to any actual activities undertaken under any of the FOA, Export-Import, Netherlands or UNTA Programs operating in Indonesia; but merely reports the total expenditures involved since World War II. The one substantive indication at the bottom of page 35 is in wholly general terms, except for the reference to the introduction of improved "rice and corn seed" (which is understood to be 50% inaccurate, since work on rice has not been included in the agricultural aid program).
- c. The explanation why foreign aid has been relatively limited in Indonesia is well stated. Since, however, a major change in Indonesian attitudes is reported to have taken place in the last six months (accelerated since the recent change in the Indonesian cabinet) this should substantially increase the whole relative importance of foreign aid possibilities.

2. The paper is to be commended for its excellent detailed statements of many of the particular economic problems in the way of Indonesian economic development. Yet, its very emphasis on the difficulties Indonesia has been encountering tends to minimize Indonesia's "potential" from the point of view of basic-materials resources. The whole discussion of the "strategic importance" of Indonesia's resources, as well as the emphasis on past and present difficulties throughout the paper, definitely plays down the significance of Indonesia's economic potential. This is in sharp contrast with the views of a large number of qualified experts on the Indonesian economy with whom I have discussed this question at length in recent years -- both at the time of Indonesia's liberation from Japanese occupation, and later when the U.S. aid program there was being administered by the Technical Cooperation Administration (then under State Department). It is understood furthermore that both Agriculture and ICA members of our Working Group also believe that the strategic potential of Indonesian resources is considerably greater than here indicated. This illustrates the importance of having more than a single agency's viewpoint reflected in such background papers if they are to serve as adequate guidance of policy-level officials.

3. Perhaps because the importance of the Indonesian potential is so heavily discounted, there is essentially no consideration of the types of

development programs required to expand the Indonesian economy, nor any analysis of the specific difficulties which such programs would have to overcome. Yet, it is understood that a number of specific programs for development, not yet undertaken, have been at least considered in recent years -- and that several of these may soon be brought up again in a reconsideration of the total magnitude of foreign aid to Indonesia. Thus proposals for Indonesia's participating in surplus food disposal under P.L. 408 have been under discussion for more than a year -- quite actively since last March -- yet the possibilities for this rather specialized type of aid program are not even discussed. As another example, the possibilities for using Indonesian hydroelectric power in conjunction with her large (though low-grade) bauxite deposits are barely mentioned in passing. Even if OIR is correct in assigning a low strategic value to the potential importance of Indonesian resources to the Free or Soviet Worlds, nevertheless an expansion of the Indonesian economy is a desirable U.S. objective in itself -- since the geographic location of these islands makes their adherence to the Free World a major political and military imperative. Much fuller consideration should therefore be given to the extent to which -- and the means by which -- Indonesian production of such commodities as aluminum, tin, petroleum, rubber, other agricultural raw materials, and foods might be stimulated, and economically supported by international or internal market demands.

It is my understanding that the author of this report, Mr. Schmucker, is scheduled to visit Indonesia this fall in preparation for certain NIS chapters on which he is to work following his return. He will undoubtedly be briefed, while there, on recently increased Indonesian interest in various foreign aid programs; and it should be easy to arrange through ICA offices here that he be assisted in getting the fullest possible picture of this situation. It would seem logical to me that following Mr. Schmucker's return the technical knowledge of Mr. Mulholland and of Wilhelm Anderson (the key technicians on Indonesia on the staffs of the ICA and Agriculture members of our working group) should be drawn on to assist OIR in revising and "up dating" this paper -- so that it might provide a more adequate background for future U.S. policy and operational decisions.

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Secretary, EIC Working Group on Indonesia

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