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Corporate Governance in Indonesia: A Study on Governance of Business Groups

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1. Introduction

Since the high growth period praised as the "East Asian Miracle" collapsed due to the Asian economic crisis in 1997, good governance has come to be a key issue in the IMF-led reforms in the crisis-hit Asian countries. In these countries, IMF conditionality contained wide-ranging institutional reforms that were, in a word, a reform of governance of the government and corporations. In the case of Indonesia, the long-standing authoritarian regime fell during the crisis, and vigorous public hopes for democracy emphasized a need for institutional reform not only in the political sphere but also in the economic sphere.

One of the key issues in economic reform is corporate governance. After the crisis, a negative view of the governance of Asian firms became widespread. The World Bank (1998) presented its view that the economic crisis could be attributed to the institutional vulnerability of the financial and corporate sectors, stating that "the poor system of corporate governance has contributed to the present financial crisis by shielding the banks, financial companies, and corporations from market discipline" (ibid, p.57). Research by World Bank economists showed that East Asian firms were characterized by high leverage, concentrated ownership, a high level of ultimate control by a few families, and the expropriation of minority shareholders, and argued that these characteristics led to weak corporate governance and impeded legal and regulatory developments.[1] Based on this argument, new institutions of the Anglo-American type, such as independent commissioners/directors, internal auditing/remuneration committees, and protection for minority shareholders, have been introduced for better corporate governance in the crisis-hit Asian countries, including Indonesia.

This chapter deals with the issue of corporate governance in the case of Indonesian business groups. It attempts to examine how failures of corporate governance actually took place, what factors can be attributed to the failures, and what factors affect the structure of corporate governance in the Indonesian institutional setting. It then aims to draw some lessons for improving corporate governance in this country. Section 2 below reviews theoretical and empirical arguments on corporate governance and sets out a framework for the analysis of our cases with the presence of controlling owner-managers. Section 3 constructs hypotheses on what conditions make corporate governance work or fail to work, based on theory as well as insights from observation. Section 4 looks at six case studies of Indonesian business groups and examines characteristics of corporate governance in each one. The last section summarizes major findings of the case studies and discusses the validity of the hypotheses.

2. An Analytical Framework — Corporate Governance with the Presence of Owner-managers

2.1 Recent Evolvement of Analytical Perspectives on Corporate Governance

The problem of corporate governance originally arises from the separation of ownership and management. The standard definition of corporate governance refers to the defence of shareholders' interests against the interests of managers. It deals with the ways in which shareholders control managers so that managers effectively maximize the value of their firm without taking opportunistic actions that hurt shareholders. This is a straightforward agency problem between shareholders as principals and managers as agents. This shareholder-value perspective pre-supposes Berle and Means-type managerial firms, in which ownership is widely dispersed and management is in the hands of salaried professional managers (Berle and Means 1932).

Still on the shareholder-value perspective, Shleifer and Vishny (1997) extend a scope of analysis beyond the pre-supposition of Berle and Means. They define corporate governance as an agency problem between financiers (or investors) and managers. They ask about "the ways in which suppliers of finance to corporations assure themselves of getting a return on their investment", and "how (do) the suppliers of finance get the managers to return some of the profits to them" (ibid., p. 737). Their answer is that legal protection of investor rights can help investors to get their money back. In the case of weak legal protection, financiers can get more effective control rights over managers by being large, that is, in the form of large shareholders, takeovers, and large creditors (ibid., p. 753).

The largeness of financiers can be effective in solving the agency problem, but it may inefficiently redistribute wealth from other minor financiers to the large financiers. This extended framework conforms better to the results of a recent study showing that concentrated ownership with large shareholders is more commonly observed than widely-dispersed ownership.

Recent heated argument over corporate governance shows a trend in moving away from the traditional concept of shareholder value towards the broader concept of the stakeholder society. Managerial decisions do affect investors, but also exert externalities on various other stakeholders of the firm, such as employees, customers, suppliers, communities where the firm is located, potential pollutees, and so forth (Tirole 2001, p. 3).[2] From the stakeholder-society perspective, corporate governance is "the design of institutions that induce or force management to internalize the welfare of stakeholders" (ibid, p.4), and a governance system is "the complex set of conditions that shape the outcome of the *ex post* bargaining over the quasi-rents that are generated in the course of a relationship" (Zingales 1998).

Based on the analytical framework provided by Tirole (2001) on the governance of the stakeholder society, Aoki (2001, Chap. 11) further develops a comprehensive foundation for analyzing a diversity of corporate governance mechanisms. From the viewpoint of the comparative institutional analysis employing game theory, he sees corporate governance as "self-enforcing mechanisms that govern (such) strategic interactions among the players" and defines it as "a set of self-enforceable rules (formal or informal) that regulates the contingent action choices of the stakeholders (investors, workers, and managers) in the corporate organization domain" (ibid., p. 281). Aoki first identifies three major types of corporate organization from the viewpoint of an information processing structure, that is, (i) hierarchical decomposition, (ii) participatory hierarchy, and (iii) horizontal hierarchy. He then analyzes governance mechanisms which conform to three organization types respectively, that is, (i) owner control, (ii) co-determination by managers and workers, and (iii) relational contingent governance, with insider control in the case of higher output level, and with outsider (relational monitor) control in the case of lower output level. Owner control is further classified into (i) owner-manager control over workers (in the Hart-Moore firm[3]) with no debt; (ii) owner-manager control over workers regulated by debt contracts; and (iii) shareholder control over managers. Aoki's framework thus goes beyond the confrontation of shareholder-value and stakeholder-society perspectives, and provides a broader scope of comparative (not normative) analysis on governance mechanisms, connecting the domain of corporate organizations with other domains of financial transactions, labour transactions, political regimes and so forth.

2.2 Key Elements of Corporate Governance in Asia

In the context of corporate governance in Asia, one of the key elements to be taken into account is ownership concentration. Concentrated ownership with large shareholders, compared to the traditional Berle and Means proposition of dispersed ownership with atomistic shareholders, has attracted more interest in recent empirical literature. La Porta, Lopez-de-Silanes and Shleifer (1999) shows that widely-dispersed ownership is not prevalent around the world except in the United States and the United Kingdom; rather, concentrated ownership is a more common organizational form for modern firms in developed countries.[4] The outbreak of the Asian currency crisis in 1997 called attention to corporate ownership structure in Asian developing countries in relation to corporate governance and performance. Researchers, headed by Stjin Claessens of the World Bank, have traced the ultimate owners of East Asian firms and have found that corporate ownership is concentrated in the hands of few families. They provide evidence of the expropriation of minority shareholders with a gap between the control rights and the cash flow rights of controlling shareholders, and suggest that insider-control contributed to the firms' weak performance and risky investment prior to the crisis (Claessens, Djankov and Lang 1999b; Claessens, Djankov, Fan and Lang 1999a). Concentrated ownership and the associated problems of Asian firms have thus become hot issues in the negative sense.

Another key element, which closely relates to ownership concentration but should be distinguished from it, is the coincidence of ownership and management, or the existence of large shareholders who concurrently hold top managerial positions. How can we deal with such owner-manager firms in corporate governance analysis? The traditional shareholder-value perspective pre-supposes separation of ownership and management. The logical consequence is that, if ownership coincides with management, firms have no agency problem, so the self-governance of owner-managers works perfectly. In the Shleifer and Vishny extended framework of financiers and managers, relations between owner-managers and other financiers, such as minority shareholders, general investors through stock markets, creditors, and potential takeovers, and the way in which these financiers make owner-managers assure their return are worth analyzing. The stakeholder-society perspective would provide wider possibilities of analysis; relations between owner-managers and other stakeholders, for example, salaried professional managers, employees, joint venture partners, and the government (or power elite) as licensing authorities or patron. In the Aoki framework, the relevant governance mechanism in this context is (i) and (ii), namely owner-manager's control over workers with or without a threat of liquidation imposed by outside investors/creditors.

There are some empirical studies on owner-manager-led firms in Asia that put forward different views.[5] The World Bank (1998), based on the studies of Claessens group, argues that firms with controlling owners expatriate other investors, pursue personal non-profit-maximizing objectives, and impede the development of professional managers. Yeh, Lee and Woidtke (2001) in their Taiwan study compare firm performance with levels of ownership concentration and representation of the owner family on the managerial board. Their result is that HILO firms (firms with a high level of family ownership and a low level of family board representation) show the highest performance, followed by HIHI and LOLO firms, and LOHI (firms with a low level of family ownership and a high level of family board representation) have the lowest performance. They see this result as consistent with their view that firms have lower agency problems when owner families have higher cash flow rights (decreasing conflict with minority shareholders) and the board is more likely to monitor the controlling family-managers (ibid., pp. 39–45). In contrast to this result, Suehiro (2001), in his Thai study, found that concentrated family ownership as well as the owner family grip on top management do not always result in poor corporate performance, and argues that family ownership management itself is not wrong, but its internal innovation is a relevant key for corporate reform.

While the above studies shed light on the fact that minority shareholders and salaried professional managers are important stakeholders in the owner-manager firms, another key stakeholder to be focused on is the creditor. The Asian economic crisis brought the corporate debt issue into sharp relief, revealing that most large firms heavily depended on borrowing from foreign and domestic creditors. Although corporate insolvency was primarily caused by a sharp drop in currency values; an 80% drop from the pre-crisis value in the case of the Indonesian Rupiah, it is still probable that firms had over-borrowed to finance their excessive investment in the pre-crisis period. It is worth examining whether creditors have been able to effectively monitor the firms' owner-managers to get them to repay debts. Some empirical studies argue that although owner-manager-led corporate governance economizes transaction costs at the initial stage of growth, agency costs increase between owner-managers and external financiers as business expands and requires large amounts of external finance (Khan 1999, p. 22; Lang 2001b, p. 11). For Indonesia, the debt problem is relevant, because corporate debts became a crucial issue in the post-crisis corporate restructuring, and the major debtors of overseas borrowing were large business groups, unlike Thailand where banks or non-bank financial institutions were major debtors.

2.3 Analytical Framework of This Chapter

This chapter deals with the corporate governance of Indonesian business groups. We decided on business groups rather than individual firms as an object of study, for the purpose of observing the ultimate owners who manage multiple firms. A business group is simply defined as a group of firms under the same ownership. The owner can be a single individual, a single family, plural non-family individuals, or plural families.

In most Indonesian business groups, owners coincide with top management of the group. As discussed above, coincidence of ownership and management is contradictory to one of the original concepts of corporate governance that pre-supposes separation of ownership and management. However, recent evolution of analytical frameworks on corporate governance accommodates analysis of owner-manager-led firms, concentrating on the relations between owner-managers and other financiers/stakeholders.

Although one of the prospects of this study is to extend its analytical scope to various related stakeholders in a wide sense, we start this chapter by narrowing the scope down to two key stakeholders. One is creditor as a major outside financier, and another is salaried professional manager as a main inside stakeholder. We look at an example of failure of corporate governance through an incidence of over-borrowing,[6] and examine whether creditors and professional managers can prevent owner-managers from excessively borrowing, and if not, why not. In this context, domestic creditors should be distinguished from foreign creditors, and when talking about domestic creditors we should distinguish between state-owned banks and private banks, as their behaviour and capabilities may be different.[7] Therefore, within this simple framework, the focal point of observation is the relationship between business group owner-managers and creditors, and between owner-managers and professional managers, concerning the problem of controlling excess borrowing.

3. Setting Up Hypothese — Under What Conditions Does Corporate Governance Fail to Work?

Theoretically, debts provide discipline to owner-managers. Discipline is imposed in at least two ways. Debt repayment decreases free cash flow; a part of the net gain of corporate activities that managers can use freely, and therefore restrains managers from spending money on excessive investment. In addition, an owner-manager who performs poorly in debt management would find it difficult to renew debt contracts with creditors, or might even be threatened with liquidation of the firm by creditors. Needless to say, creditors have the motivation to monitor owner-managers of borrower firms in order to have them repay their debts properly.

Nevertheless, how does over-borrowing of firms take place? Why do creditors allow the firms to behave in this way?

One possible reason for the failure of creditors' governance over owner-managers of borrower firms is the asymmetry of information. Owner-managers provide creditors with only good information so as to borrow more, while it costs too much for creditors to gain all the needed information on the firms' management. The asymmetry can be more serious in case of business group management. Thus the first hypothesis is formulated as follows.

[H-1: information asymmetry hypothesis] Governance by creditors fails to work because owner-managers provide creditors with only good information.

Another possible reason for the failure of creditors' governance over owner-managers is the lack of a threat of liquidation or other sanctions. First, this is a matter of incomplete laws and institutions regarding the liquidation of poor-performance firms. The situation is generally true of Indonesia in the pre-crisis period, when a bankruptcy law and commercial courts did not function. Secondly, the lack of a threat of liquidation may relate to collusion with the government. Let us think of collusion between creditors and the government, that is, government back-up to creditors, as could be the case with state-owned banks. The creditors are less motivated to get their money back from borrowers, as they can expect the government to absorb a risk of irrecoverable debts.[8] As a result, creditors' governance loses effect. Similar logic applies to collusion between owner-managers and the government (or power elite), or government back-up to firms. State-owned corporations, business groups run by President Soeharto's family, and those closely linked to political power would be examples of this (Pangestu and Harianto 1998, p. 13). These firms can make use of their advantageous positions to draw more funds from creditors, and the creditors expect the government to assure debt repayment in case the firms become insolvent. Thus creditors' governance fails. The second hypothesis is as follows.

[H-2: collusion hypothesis] Governance by creditors fails to work when either creditors or owner-managers collude with the government (or power elite), because creditors as well as owner-managers expect the government to absorb a risk of governance failure.

An analysis of ownership-management patterns and the economic performance of Indonesian publicly-listed companies in the pre-crisis and post-crisis period in Sato (2004) provides an insight into the corporate governance issue. According to the study, the difference in a firm's profitability (ROA and ROE) and debt dependency (D/E: debt to equity ratio) is not significant by ownership pattern (concentrated or dispersed) or by separation of ownership and management (not separated or separated). Rather, the difference is obvious by affiliation to business groups (group or non-group) and by types of business groups (established group or rapid-growth group).[9]

The result in Table 4.1 shows that, first, firms affiliated to business groups are characterized by high profitability and high debt dependency compared to non-group-affiliated local private firms. Secondly, firms affiliated to nine established business groups showed high profitability and high debt dependency in the pre-crisis period and a relatively high rate of survival of the crisis as seen in their still high shares of sales and assets in total listed companies. Thirdly, firms affiliated to eight rapid-growth business groups showed low profitability and high debt dependency in the pre-crisis period and suffered heavily as a result of the crisis. Although firms belonging to the established groups and those belonging to the rapid-growth groups have an equally high level of debt dependency, the profitability and the degree of survival after the crisis are higher in the established groups than the rapid-growth groups. What factors can this difference in performance be attributed to? What are the possible factors which make the governance structure different between the established and the rapid-growth groups?

The first possibility lies in differences in fund raising behaviour. The established business groups, with their reputations as leading actors on the Indonesian economic stage and business experience of more than two decades, had relatively easy access to overseas sources of funds. Their preference for overseas sources of funds was economically rational, because the cost of foreign funds was at the average interest rate of 9% (from 1987 to 1996), and also the managed Rupiah depreciation was within 4% annually, much lower than the average interest rate of 18% for domestic loans (Husnan 1999, p. 8). On the contrary, rapid-growth business groups with no such reputation depended heavily on domestic sources of funds, especially state-owned bank loans (Sato 2002, pp. 77–85). So the difference is that the firms affiliated to established groups borrow mainly from foreign creditors and those affiliated to rapid-growth groups borrow mainly from domestic creditors. It is likely that foreign creditors have a higher ability to investigate and monitor customer firms than domestic creditors and therefore the firms of the established groups were able to maintain higher profitability and survive the crisis. Thus the third hypothesis is as follows.

[H-3: hypothesis of creditors' ability] Governance by creditors works due to the fact that foreign creditors have a higher ability to investigate and monitor the management of customer firms than domestic creditors.

As Table 4.1 shows, the number of listed companies affiliated to established groups is almost double the number of those affiliated to rapid-growth groups in the pre-crisis as well as the post-crisis periods. This fact indicates a possibility that the more the group firms are publicly listed on the stock exchange markets, the better the governance by outside

Table 4.1 Change of Shares and Performance of Listed Companies in Indonesia by Type of Business Groups

	No.of company		Share in sales		Share in assets		Average ROA		Average ROE		Average D/E	
	1996	2000	1996	2000	1996	2000	1996	2000	1996	2000[d]	1996	2000
Business Group												
Established[a]	20	18	39.9	36.1	35.5	21.9	4.0	–2.9	17.7	–20.1	10.5	–13.2
Rapid-growth[b]	12	9	12.3	6.4	21.8	6.7	3.2	–20.9	10.9	–43.4	5.3	-4.7
Other group	26	17	17.9	13.0	16.1	7.8	4.4	–16.2	12.9	3.8	3.6	0.3
Group total	58	44	70.0	55.5	73.4	36.3	4.0	–11.5	14.3	–14.5	6.3	–6.3
Non-group private	29	27	14.9	15.0	8.9	7.8	4.3	–3.3	11.6	–30.9	2.5	1.9
State	5	16	11.1	22.5	16.3	52.9	10.3	6.4	16.2	–2.1	2.7	7.7
Foreign[c]	8	13	3.9	7.0	1.4	3.0	6.9	10.1	15.4	14.5	1.9	1.6
Total	100	100	100.0	100.0	100.0	100.0	4.8	–3.5	14.2	–11.9	4.7	–0.8

Source: compiled from ECFIN (various years).
Note: a: 9 business groups which satisfy the 3 conditions concurrently; (1) started its core business in the 1970s or before, (2) ranked in the 20 largest groups in the 1980s, and (3) ranked in the 10 largest groups in 1996.
b: 8 business groups which satisfy either of the 2 conditions; (1) started its core business (or its discontinuous spurt) in the 1980s and ranked in the 30 largest groups in 1996, or (2) ranked below the 20th in the 1980s but in the 10 largest groups in 1996.
c: Excludes 4 'apparent foreign companies' owned by Indonesians. Those are treated as domestic private companies.
d: Excludes 23 companies with negative equity due to excess debt (liabilities exceed assets), because ROE becomes extraordinary large value.

List of established business groups
1. Salim
2. Astra
3. Sinar Mas
4. Gudang Garam
5. Lippo
6. Ongko (or Arya Upaya)
7. Bob Hasan
8. Djarum
9. Rodamas

(All are owned by ethnic Chinese businessmen.)

List of rapid-growth business groups
1. Bimantara (owned by the second son of President Soeharto)
2. Gajah Tunggal
3. Nusamba (owned by foundations led by President Soeharto)
4. Barito Pacific
5. Humpuss (owned by the third son of President Soeharto)
6. Danamon
7. Raja Garuda Mas
8. Texmaco (owned by ethnic Indian-Tamil)

(All without notes are owned by ethnic Chinese businessmen.)

financiers works, not only by markets but also by creditors, because the financiers can obtain more information disclosed to the public about the business group. Thus the fourth hypothesis is as follows.

[H-4: hypothesis of public listing effect] Governance by creditors works better, because more group-affiliated firms are publicly listed and more information on the business group is disclosed to the public.

Apart from the creditors' governance over the owner-managers of business groups, the degree of presence of salaried professional managers is another possible factor in distinguishing the performance of established groups from that of rapid-growth groups. Although existing studies do not provide clear evidence, it is likely that the presence of professional managers is higher in the firms in established groups than those in rapid-growth groups, as the former has longer history of organizational development. If so, the hypothesis that a higher presence of professional managers enables a better check on owner-managers would hold true. The findings of Yeh, Lee and Woidtke (2001) that firms with a combination of high levels of family control and low family board representation have the highest relative performance give supporting evidence to this hypothesis. The last hypothesis is as follows.

[H-5: hypothesis of the function of professional managers] Corporate governance works better with a higher presence of salaried professional managers who function as a check on owner-managers.

4. Case Study on the Corporate Governance of Six Business Groups

This section is devoted to a case study on the corporate governance of business groups in Indonesia in order to examine the validity of the above hypotheses. We look into the structure of the corporate governance of six selected business groups in relation to such attributes as (1) ownership and management patterns; (2) levels of debt and main creditors; (3) levels of investment; (4) levels of market disclosure; (5) presence of professional managers; and (6) relations with the government.

The six business groups have been selected bearing the following three points in mind. The first is representation in scale of sales and debts. As Table 4.2 shows, the six groups ranked within the top 30 in annual sales in the pre-crisis period, accounting for 32% of the aggregate amount of sales of the 30 groups. The outstanding foreign and domestic debts of the six groups in total in the post-crisis period account for 41% and 42% respectively of those of the total 30 groups. This means that the six groups are relatively large in sales and heavily indebted.[10] Relatively indebted groups are intentionally selected for the purpose of examining

Table 4.2 Summary of 6 Business Groups (1) : Sales and Debts

Name of business group	Name of owner=manager*		Group sales (1996) (tri. Rp.)	Group sales (1996) ranking	Group debt** Foreign (bil.US$)	Group debt** Domestic (tri.Rp.)	Indicator for over-borrowing Foreign debt/ /annual sales	Indicator for over-borrowing Domestic debt/ /annual sales
1 Gudang Garam	Rachman Halim	Ch.	9.4	4	negligible	-	0.00	0.00
2 Sinar Mas	Eka Tjipta Widjaja	Ch.	20.2	3	3.8	0.7	0.55	0.03
3 Astra	owner≠manager	-	20.2	2	5.1	0.4	0.74	0.02
4 Gajah Tunggal	Sjamsul Nursalim	Ch.	4.2	7	3.0	1.5	2.08	0.36
5 Texmaco	Marimutu Sinivasan	In.	1.8	26	1.5	17.3	2.43	9.61
6 Humpuss	Hutomo Mandala Putera	Pr.	2.3	18	0.4	5.7	0.51	2.48
Total of 6 groups			58.1		13.8	25.6	0.69	0.44
Share in total of 30 groups (%)			(32.2)		(40.4)	(42.1)	0.98	0.22

Source: Group sales from *Warta Economi*, 9(27), 24 Nov. 1997 / outstanding foreign debts are estimation by CISI Raya Utama/ domestic debts from IBRA (2001).

Note: * Ch.=ethnic Chinese, In.=ethnic Indian, Pr.=native Malays (pribumi).

** Foreign debts are as of the end of 1997. Domestic debts are the amount of irrecoverable bank loans transferred to IBRA, as of 2001.

Table 4.3 Summary of 6 Business Groups (2): Ownership/Management Pattern, Level of Debt, Disclosure and Investment, and Governance Structure

Group name	Group type	Ownership/management pattern	Debt/creditors	Investment	Major business
Gudang Garam	Established	Ownership=management by founder family	Low	Low/Limited diversification, domestic	Clove cigarette
Sinar Mas	Established	Ownership=management by founder family	High/Foreign	High/ Multi-nationalization, export	Pulp & paper, agribusiness, financial services, property
Astra	Established	Semi-dispersed ownership, semi-separated management after 1992	High/Foreign	Medium/ Less diversification, domestic	Automobile, agribusiness, financial services
Gajah Tunggal	Rapid-growth	Ownership=management by founder family	Very high/ Foreign	High/Diversification, mega projects, export and domestic	Tire, chemical, cable, shrimp farm, financial services, property
Texmaco	Rapid-growth	Ownership=management by a founder (ethnic Indian)	Very high/ Domestic and Foreign	High/Mega projects, export and domestic	Synthetic fiber, machinery
Humpuss	Rapid-growth	Concentrated ownership by a founder (pribumi), semi-separated management	Very high/ Domestic	High/Diversification, domestic	Services, transportation, mining, property, retail trade

Table 4.3 Summary of 6 business groups (2): Ownership/management pattern, level of debt, disclosure and investment, and governance structure (*continued*)

Group name	Market disclosure by publicly listing	Presence of salaried managers	Relation with the government	Structure of corporate governance	Problems
Gudang Garam	Partial disclosure by listing only a core	Low	None	Self-governance by founder family owner-managers	Less rapid growth. Should be take relation with employess into account.
Sinar Mas	Majority disclosure by listing several divisional holding companies	High at the group company level	Out of favor with the Soeharto government	Governance by foreign creditors and markets over owner-managers — failed to work	Eventual debt crisis
Astra	Whole disclosure by listing a group holding company	Highest. Boards of directors are mostly professional management.	Most out of favor with the Soeharto government up to 1992	Management by professional managers of the headquaters, governance by market and creditors — debt crisis, but restructured	Concentration of foreign creditors' lending due to its rare transparancy
Gajah Tunggal	Partial disclosure by listing well-performing companies	High at the group company level	Close to high Army officers in the Soeharto government	Governance by foreign creditors over owner-managers — failed to work	Mechanism of supplying fund raised by listed companies to other group operations
Texmaco	Majority disclosure by listing major companies	Low	Close to the former President Soeharto	Governance by domestic creditors over owner-managers — failed to work	Collusive state-bank loans owing to powerful political backup
Humpuss	Undisclosed. Only one listed company	High	Owned by the President Soeharto's third son	Governance by domestic creditors over owner-managers — failed to work	Collusive state-bank loans owing to powerful political backup

Source: by author.

a corporate governance structure that may allow over-borrowing. The second is a balance of established and rapid-growth groups. The first 3 groups in Table 4.2 are selected from the established and the second 3 are from the rapid-growth. It appears that the rapid-growth groups have large debts in relation to their annual sales. The third is a variety of groups with the attributes raised above. We can see whether or not different attributes affect their borrowing behaviour and governance structure. Table 4.3 provides a summary of the main attributes of the six business groups as examined below.

We use over-borrowing as a measurement of failure of corporate governance. As the state of over-borrowing is not so self-evident, we judge it by combining three kinds of indicators. The first is the amount of debts compared to annual sales (liability to sales) at the business group level, as shown in Table 4.2. When the ratio is above 0.5, or 6 months, the debt level is evaluated as high.[11] Using this standard, all the 6 groups except Gudang Garam are evaluated as high; especially the three rapid-growth groups above 2.0 which are extraordinary high. The second is debt to equity ratio (D/E) at the level of group-affiliated company. Data is only available for listed companies (see Appendix 4.A1a). When the ratio in 1996 is above the average of the largest 100 companies, that is, 4.7 (1.7 for non-financial companies), the debt level can be evaluated as high. Using this, Gudang Garam is low, Gajah Tunggal is just on the average, and others (except Humpuss with no data) are higher than the average. The third is the fact of whether the group actually encountered a debt crisis. The three rapid-growth groups and Astra fell into debt crisis just after the 1997 currency crisis, but Astra succeeded in debt restructuring after a one-year negotiation with creditors. Sinar Mas fell into crisis in 2000.

Putting these results together, the three rapid-growth groups are judged as probably having over-borrowed, and Gudang Garam is judged as obviously not. As for Astra, at least its major listed companies were over-borrowing, but *ex post* governance was successful. On the contrary, Sinar Mas was not so evidently over-borrowing in the pre-crisis period, but after three years obvious over-borrowing was revealed.

4.1 Gudang Garam Group

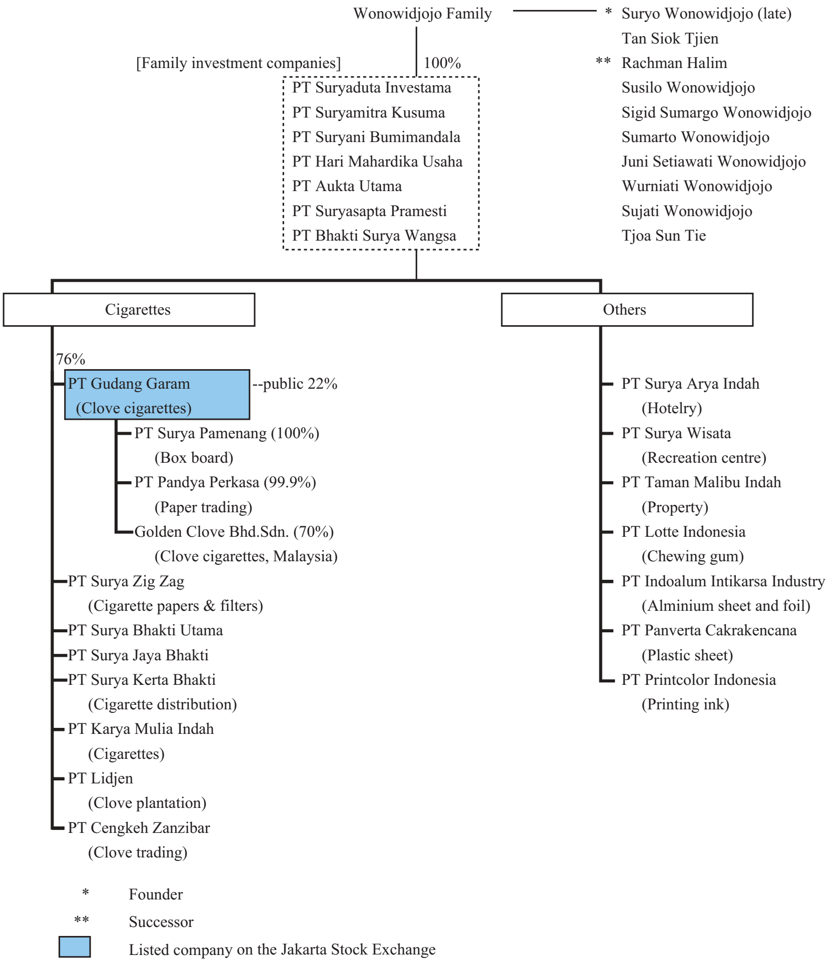
Gudang Garam Group is the fourth largest business group in Indonesia with Rp.9.4 trillion annual group sales (US$3.9 billion) in 1996 and has long been the largest producer in the Indonesian cigarette industry. The group's core company, PT Gudang Garam, is a publicly listed company on the Jakarta Stock Exchange and the second largest of all listed companies with annual sales of Rp.15.0 trillion (US$1.7 billion) and more than 41,000 employees in 2000. PT Gudang Garam was established as a clove cigarette manufacturer in 1958 in Kediri, East Java, by the late Surya Wonowidjojo (Tjoa Ing Hwie). He was an immigrant from Fujian Province, China, and after his death, his first son, Rachman Halim (Tjoa To Hin), took over the whole business.

Among many Indonesian business groups, the Gudang Garam Group is the most extreme case of exclusive ownership and management by a founder family. Ownership by the family (Rachman Halim, his mother, his brothers and sisters, and his children) accounted for 94% of total shares in 1985 (7 affiliated companies), 80% of shares in 1996 and 76% in 2000 (only PT Gudang Garam).[12] Managerial posts occupied by the family accounted for 64% (1985), 33% (1996), 80% (2000) on the Board of Commissioners (Dewan Komisaris), and 71% (1985), 54% (1996), and 19% (2000) on the Board of Directors (Direksi).[13] Although posts on the Board of Directors were drastically shifted to non-family salaried managers after the crisis (from 46% to 81% for PT Gudang Garam in the period from 1996 to 2000) the owner family's presence on the Board of Commissioners ensures a continuing firm grip on management. The scope of the activities of salaried managers is limited to non-strategic daily management at the single company level.

The group shows high profitability and low debt dependency. PT Gudang Garam is one of the most profitable companies in Indonesia, as shown by an ROA and an ROE of over 20% to 30%, even higher in the post-crisis than in the pre-crisis period. Debt equity ratios were below 1.0 in 1996 as well as in 2000. This is an extremely low level given that the ratio of the established business groups on average was 10.5 in 1996 and fell to negative value in 2000 due to excess of debts to assets.

Such features of the group as exclusive family ownership-management and high profitability with low debt level are closely related to the peculiarity of the group's core business, namely the clove cigarette industry. This industry holds a huge and stably-growing domestic market, the value-added of which constantly accounts for around 10% to 12% of total manufacturing value-added throughout the period from 1980 to 2000. It is said that the production of clove cigarettes (*kretek*) needs a special recipe, which is secretly handed down in the family. This may motivate the family to keep a firm grip on a core part of management. The conservative nature of the group influences its investment and fund-raising behaviour. Since it was founded the group has undertaken no large diversification investment except in related businesses such as cigarette paper, filters, packaging and distribution. Diversification into unrelated businesses is limited to property, plantations and small scale banking. PT Gudang Garam is the only publicly listed company in the group, and other businesses are organized under unlisted family investment companies (see Figure 4.1).

Figure 4.1 Ownership Structure of the Gudang Garam Group



Source: ECFIN (annual), Sukmawaty (2000), CISI Raya Utama (1990, 1999) and other materials.

As for relations with the government, the group has kept some distance from political affairs. When the third son of the then President Soeharto, Hutomo Mandala Putra (Tommy) Soeharto, set up a monopolistic regulatory organ of clove distribution in the early 1990s, the group bravely confronted this manoeuvre, which proved a failure before long.

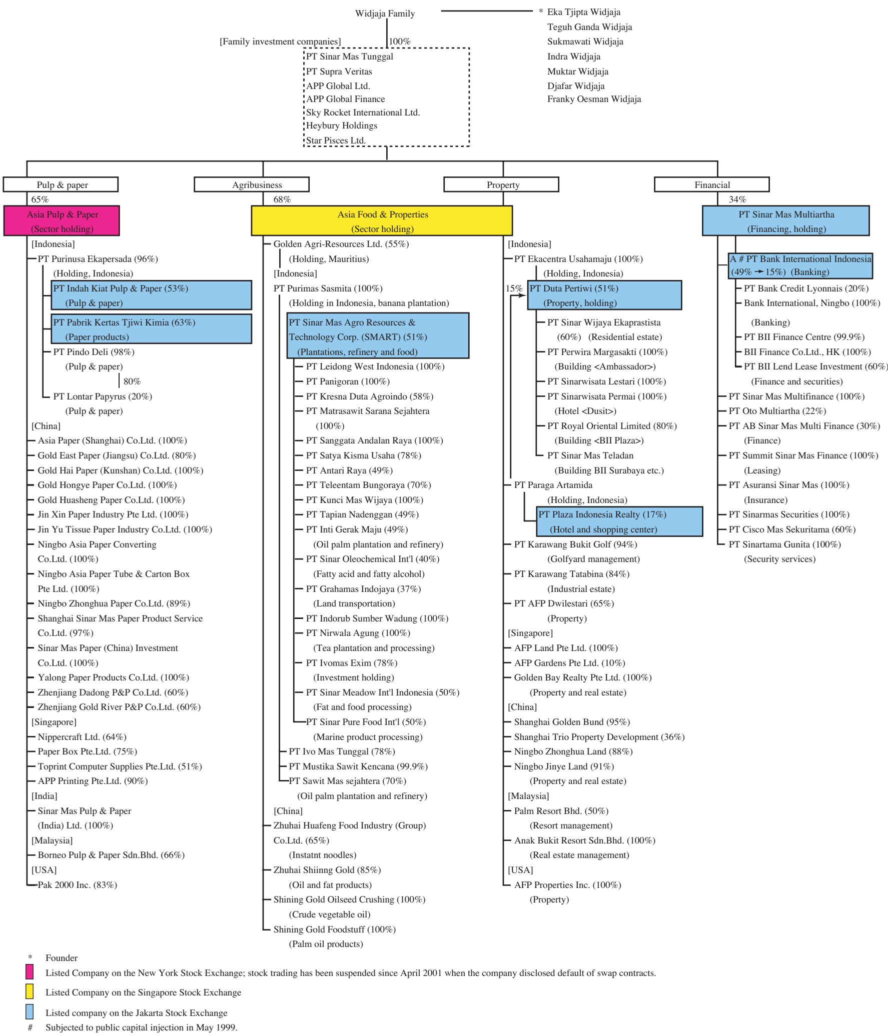
The structure of the corporate governance of the Gudang Garam Group is almost entirely self-governance by owner-managers, due to the high presence of the founder family in both ownership and management, the limited presence of public investors and salaried managers, and the absence of large creditors. This self-governance seems to work well, as the group avoids excess borrowing and over-investment, keeps high profitability, and keeps a distance from the government. This case provides evidence that concentrated family ownership without the separation of management itself is not a negative factor for corporate governance. Corporate governance by owner-managers can work well on condition that there is no other major stakeholder.[14] As a consequence of low leverage, the growth of the group has not been so rapid, but is still quite stable owing to the profitable nature of the clove cigarette industry. The success of the self-governance of the group is considerably supported by the peculiarity of the core business.

4.2 Sinar Mas Group

The Sinar Mas Group ranked third after the Salim Group and the Astra Group in the ranking of Indonesian business group sales in 1996, with Rp.20.2 trillion annual sales (US$8.5 billion). The Group's core business is in four industries, namely, (i) pulp and paper; (ii) agribusiness and food; (iii) property; and (iv) financial services. The group had 7 listed companies engaged in the four industries in 1996, but the number decreased to 6 in 2000 as the Group's bank, Bank International Indonesia (BII), was subject to capital injection by the government. The Group's development started with the establishment of the first core company, PT Bimoli (Bitung Menado Oil Ltd.), a coconut oil refinery, in 1970 in Manado, North Sulawesi. The founder was Eka Tjipta Widjaja (Oei Ek Tjhong) who emigrated from Fukian, China to Sulawesi. Of his eight children by his first wife, five sons and one daughter are major owner-managers of the group business (see Figure 4.2).

The Sinar Mas Group is also categorized as a typical case of family ownership and management, though it is not as exclusive as the Gudang Garam Group. The founder family accounted for 75% of the ownership of total shares in 1985 (35 affiliated companies), 57% in 1996, and gradually decreased to 45% in 2000 (listed companies in average). The weight of the family in management accounts for 40% (1985), 65% (1996), 47% (2000) in Komisaris, and 39% (1985), 42% (1996), 49% (2000) in Direksi (Appendix 4.A1a and b). The family presence in management increased from the mid-1980s to the mid-1990s, and after the crisis it decreased only in Komisaris. In spite of typical family control of ownership and management, it is also true that the group actively employs competent professional managers, regardless of their nationality. Eka's sons take

Figure 4.2 Ownership Structure of the Sinar Mas Group



Source: ECFIN (annual), Sukmawaty (2000), Lang (2001a), CISI Raya Utama (1999), APP's homepage (http://www.asiapulppaper.com/) and other materials.

charge of each of four divisions; the eldest son, Teguh Ganda Widjaja (Oei Tjie Goan), of pulp and paper; the third son, Indra Widjaja (Oei Pheng Lian), of financial services; the fourth son, Muktar Widjaja (Oei Siong Lian), of property; and the youngest sixth son, Franky Oesman

Widjaja (Oei Jong Nian), of agribusiness. They are fully supported by a group of professional salaried managers.

The Group's two manufacturing industries, pulp & paper and agribusiness (palm oil refineries and plantations), are resource-based profitable businesses with high export competitiveness. The investment behaviour of the Sinar Mas Group has not been a conglomerate diversification into unrelated business, but a concentration on four core businesses. In addition to the sound foundation of its business lines, the relative transparency of the group ownership structure also contributed to enhancing its reputation. The group has three divisional holding companies; Asia Pulp & Paper (APP) for the pulp and paper division, Asia Food & Properties for the agribusiness and property divisions, and PT Sinar Mas Multiatha for the financial service division, and two sub-divisional holding/operating companies; PT Sinar Mas Agro Resources & Technology Corp. for the agribusiness division and PT Duta Pertiwi for the property division, all of which are listed on the Stock Exchange markets in Jakarta, Singapore or New York and regularly report their consolidated financial statements. Another four companies engaged in key undertakings are also publicly listed. As a result, information on the majority of the group's business activities is disclosed to the public.

Owing to these advantages, the group has attracted investment funds mainly from overseas in the forms of off-shore consortium loans, supplier's credits and corporate bonds, in addition to direct financing from the stock markets. Before the Asian currency crisis, the outstanding external debts of the group were estimated to be US$3.8 billion. The debt equity ratio of seven domestically listed companies was 5.5 on average (for 5 non-financial companies, 1.9) in 1996. This is a subtle level of debt; higher than the average, but not heavily over-borrowing, and it was not considered a serious problem as long as the high profitability of the core business could absorb debt repayment and investment costs. In fact, even after the currency crisis the group successfully kept attracting funds for investment into the multi-nationalization of the pulp, paper and forestry business (China, India, Malaysia and Singapore) and of the property business (Singapore, China, Malaysia and the United States).

With a sharp decline in international market prices of pulp and paper in 2000, the Group's holding company for the pulp and paper division, Asia Pulp & Paper (APP), suffered an insolvency crisis due to huge external debts, which swelled to US$ 20 billion in total at the end of 2000. The group had a series of debt restructuring negotiations with foreign creditors.[15]

The Sinar Mas Group has never had collusive relations with the government, except for some cases of business cooperation between Eka and National Army officers in the early days of development. Rather, the group was out of favour with the Soeharto government. That seems to be one of the reasons why the group's most lucrative business, that of edible oils with its top brand 'Bimoli', was eventually taken over by the Salim Group allied with Tommy Soeharto. The group as an ethnic Chinese conglomerate also often became a target of criticism for nationalistic ministers of the Soeharto government.

The Sinar Mas Group has positive characteristics; a competitive export business, a clear core business strategy, a divisional structure of group ownership, a high degree of information disclosure by listing divisional holding companies, a relatively high presence of professional managers, and a minimum collusive factor. Unlike the Gudang Garam Group, this group has key stakeholders such as foreign creditors, professional managers and public investors, who could have monitored the owner-managers. Nevertheless, over-borrowing took place, followed by the group's debt crisis. This case is evidence that all the above-stated positive attributes, foreign creditors and markets are not sufficient conditions to prevent debt crisis *ex ante*.[16]

4.3 Astra Group

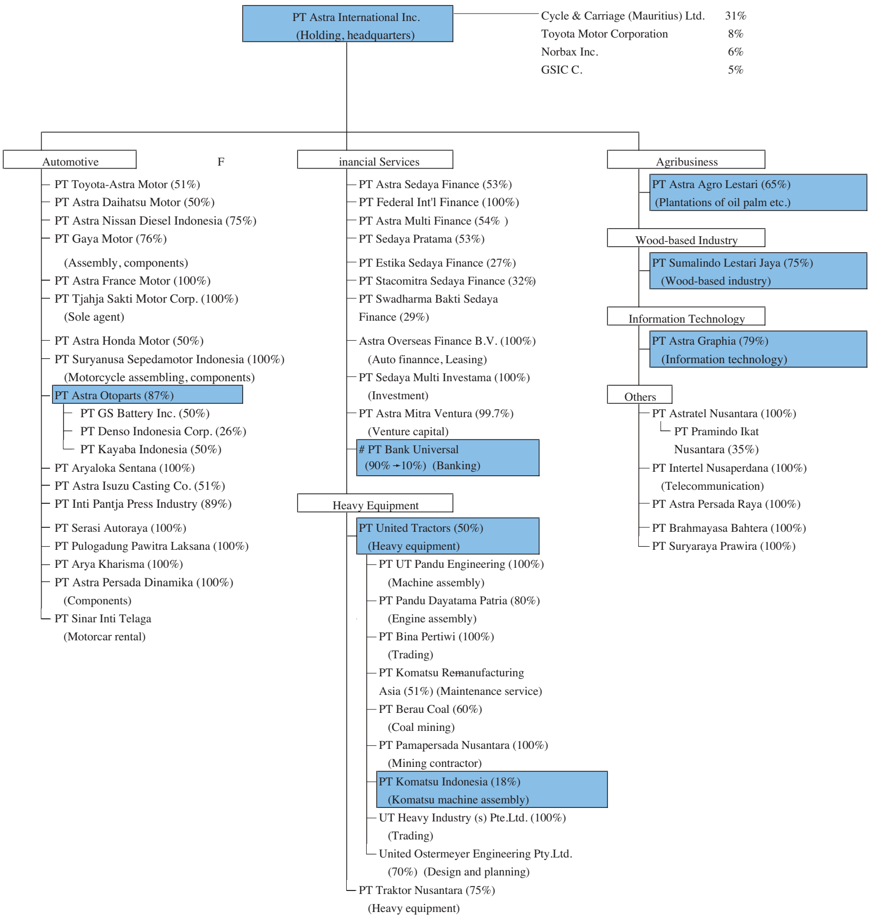
The Astra Group is a leading Indonesian business group ranked second with Rp.20.2 trillion (US$8.5 billion) annual group sales in 1996. The Group's headquarters-cum-holding company, PT Astra International, Inc., is the largest listed company in Indonesia even after it was hit by the crisis, with annual sales of Rp.28.4 trillion (US$3.3 billion) and 91,000 employees as of 2000. PT Astra International (AI), which is also the mother company of the Astra Group, was established in 1957 in Jakarta by Tjia Kian Tie and his friend. Tjia's eldest brother, William Soeryadjaya (Tjia Kian Liong), gradually took the position of major owner-founder, especially after Tjia's death in 1979. William Soeryadjaya is a seventh generation ethnic Chinese born in West Java. The Astra Group started its rapid growth after AI acquired a series of chances to be sole agent and joint venture partner with leading Japanese machinery manufacturers such as Toyota, Daihatsu (automobiles), Honda (motorcycles), Komatsu (heavy equipment) and Nippon Denso (electrical components) in the 1970s. The group is now known as a leading machinery manufacturer in Indonesia.

The Astra Group is a unique example in Indonesia of separation of ownership and management. The separation was a result of a series of unscheduled events. In 1992, when Bank Summa of the Summa Group led by William's eldest son fell insolvent, William and his family were forced to liquidate their shares in AI which had become the collateral for Summa's borrowing. The family shares were transferred to creditors (state-owned underwriters and banks), and then bought by several business groups close to President Soeharto, such as the Barito Pacific, the Bob Hasan, the Salim and the Danamon Groups. Since William was obviously out of favour with President Soeharto, the Soeharto government did not save the Soeryadjaya family from their debt crisis, and went as far to make the well-linked capitalists undergo a substantial take-over. After the 1997 currency crisis, as these business groups faced the repayment of central bank liquidity support loans or state bank loans, they transferred their stakes in AI to IBRA as a repayment, and then IBRA sold 24% of AI shares through tender to a consortium led by Cycle & Carriage of Singapore in 2000. Thus the ownership came to be dispersively held by strategic investors/investment companies unrelated to either the founder family or the government, with the Singapore consortium at the head of the shareholder list with around 30% shareholding (see Figure 4.3). This can be referred to as 'semi-dispersed ownership'.

It is noteworthy that the group's management was not substantially disturbed by the changes in ownership. A group of long-serving top professional managers at the headquarters succeeded in maintaining Astra's unity, identity, quality of management and its reputation after the withdrawal of the founding family. This was possible because the group had long made efforts to institutionalize group management by bringing Astra-bred managers up through the ranks, not only from ethnic Chinese but also from *pribumi* circles, since the early days of group development in the 1970s. At present, the composition of managerial boards is as follows; at AI headquarters, representatives of the semi-dispersed ownership sit on the Komisaris and AI's top professional managers sit on the Direksi; at AI's affiliated company level, AI's directors often occupy some key posts on the Komisaris, and the company's own professional managers occupy the posts of Direksi. In a word, Komisaris represents ownership and Direksi represents pure professional management. We can call this 'semi-separation of ownership and management' which makes good use of the two-tier managerial board system. This structure may become a mode of 'governance through Komisaris' in the institutional framework of Indonesia.

The uniqueness of the Astra Group lies not only in its semi-dispersed ownership with semi-separated management, but also because it is a group holding company which is concurrently publicly listed. In this system, information on the business activities of the group as a whole is disclosed to the public through AI's consolidated financial statement. We can safely say that the degree of information disclosure of the Astra Group is the highest of all Indonesian business

Figure 4.3 Ownership Structure of the Astra Group



Listed company on the Jakarta Stock Exchange

\# Subjected to public capital injection in May 1999. Merged with other 4 banks to become Bank Permata in September 2002.

Source: Annual reports and homepage information of PT Astra International Inc. and PT United Tractors, ECFIN (annual), Sukmawaty (2000) and other materials.

groups. In addition to AI, the Group lists six affiliated companies as of 2000 (not including Bank Universal which was recapitalized by the government).

In addition to the Astra Group's close business ties with Japanese manufacturers, which have helped in modernizing the group management system, the high degree of information disclosure constitutes an advantage for the group. In Indonesia, this kind of financial transparency through information disclosure was so scarce that the group won a good reputation with foreign creditors. This resulted in a concentration of foreign creditors' lending to Astra. As of 1996, the outstanding external debts of the group were estimated to have reached US$5.1 billion, the second largest amount after the Salim Group's US$5.5 billion. The debt equity ratio of AI was far above the average level of non-financial companies, at 4.6 in 1996, jumping up after the currency crisis to 15.1 in 2000.

The Astra Group's core business, the machinery industry, which accounts for more than 80% of total group net sales, is domestic-market-oriented with a dependency on imported inputs. The currency crisis in 1997 directly hit the group with sharp rises in import prices, a contraction in domestic demand, and the swelling burdens of dollar-denominated debt repayment. The group soon became unable to service its debts owed to foreign creditors, which amounted to more than US$1.0 billion. Through one-year of hard negotiation between foreign creditors and AI's top professional managers, it eventually managed to win rescheduling (mainly from Japanese creditors) and a cutting down (mainly from Anglo-American creditors) of debt services and started a drastic restructuring of group business in line with a debt rescheduling plan monitored by foreign creditors. The Astra Group is an example which was hardest hit economically, but also successful in restructuring debt and business. The fall of the Soeharto government had no negative impact on the group, as it had no connection to the long-standing president.

The Astra Group is an example of a structure of 'semi-dispersed ownership' with 'semi-separated management', which may become a model of evolved corporate governance through the Komisaris system suited to the Indonesian institutional setting, although it is currently a rare case. The group also has a high degree of transparency due to the fact that it is a group holding company which has gone public. It shows that high exposure to the markets cannot be a sufficient condition for the prevention of excessive borrowing by the group. On the contrary, the high degree of transparency invites an over-concentration of lending by creditors due to the scarcity value of such a group. Regarding governance by creditors, this case shows that even foreign creditors who are regarded as having a higher ability to monitor customer firms were not able to control over-borrowing *ex ante*. But they did impose discipline in the *ex post facto* debt restructuring process.

4.4 Gajah Tunggal Group

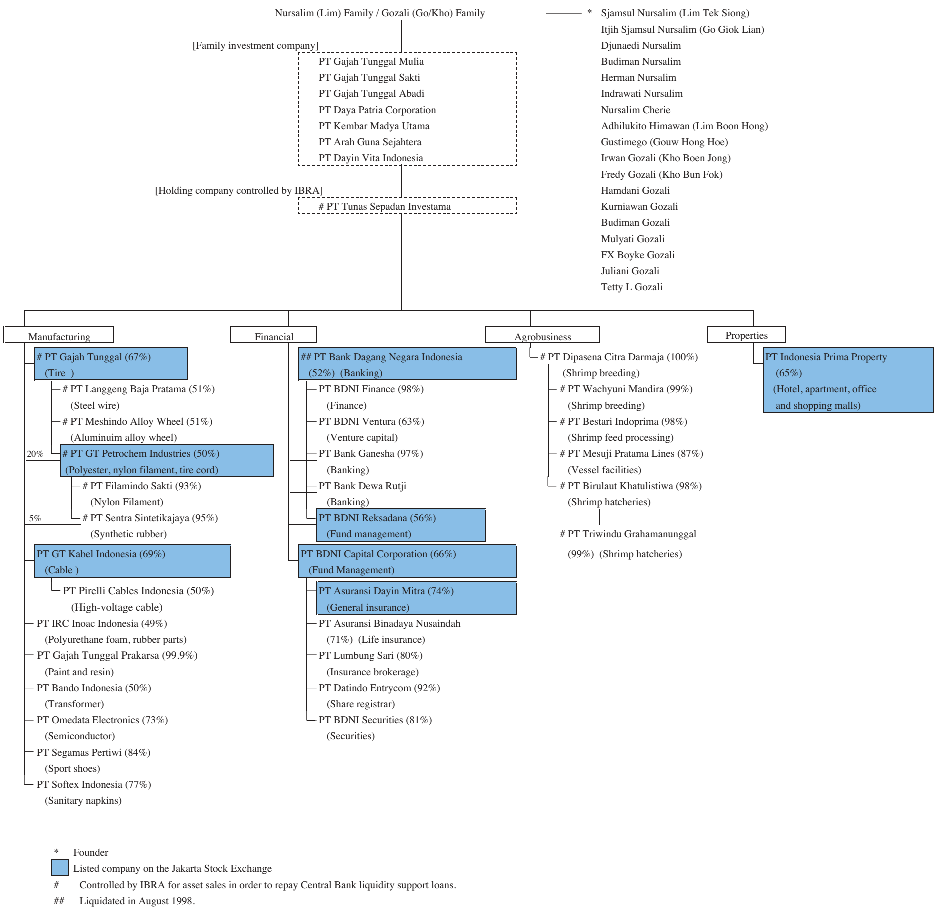
The Gajah Tunggal Group is ranked as the seventh largest Indonesian business group with Rp.4.2 trillion (US$1.8 billion) group annual sales as of 1996, although it was not ranked in the 20 largest business groups in 1988, showing the group's rapid growth in the 1990s. The group is not new, but has a long history. The group's mother company, PT Gajah Tunggal, was established in 1951 in Jakarta as a small factory of tires for *becak* and bicycles. In 1970, the present owner of the group, Sjamsul Nursalim (Lim Tek Siong), acquired this company with its brand. After that, he and his wife, Itjih Sjamsul Nursalim (Go Giok Lian), not only developed PT Gajah Tunggal into the largest tire producer in Indonesia, but also formed a highly-diversified business group. He is an ethnic Chinese born in Lampung, at the southern end of Sumatra island in 1942, the son of a primary product trader and rubber refinery owner.

In the 1970s, the Group had already shown its orientation toward diversification into such fields as rubber products, paints, metal cables, sanitary products, and banking. At the end of the 1980s, it went into large-scale investments for diversification into shrimp breeding and fishery, petrochemicals (polyester, nylon filament and synthetic rubber), and fund management services. An example of one of the group's ambitious investment plans in the mid 1990s was the expansion of its integrated shrimp processing farms in Lampung to 70,000 ha., the largest scale in the world. In fact, the Group's old and new core businesses of tire manufacturing and shrimp breeding were resourced-based industries with big markets, and the group's multi-faceted financial business in banking, insurance, financing, securities, fund management and venture capital was highly profitable with no large capital investment. The group seems to make full use of its advantage in competitive business lines to raise more funds for further diversified investment.

The Gajah Tunggal Group had 8 listed companies on the Jakarta Stock Exchange as of 1996. Of these, four were engaged in the financial services sector, three in manufacturing (tire, polyester, and cable), and one in property (Figure 4.4). Unlike Sinar Mas and Astra, these listed companies were not holding companies by nature but pure business undertakings. Therefore their function as a window of information disclosure or as a conduit for investment funds was limited.

Nevertheless, it was found that the group had a mechanism of intra-group lending, where PT Gajah Tunggal played a central role. PT Gajah Tunggal, as the most reputable listed company of the group raised external

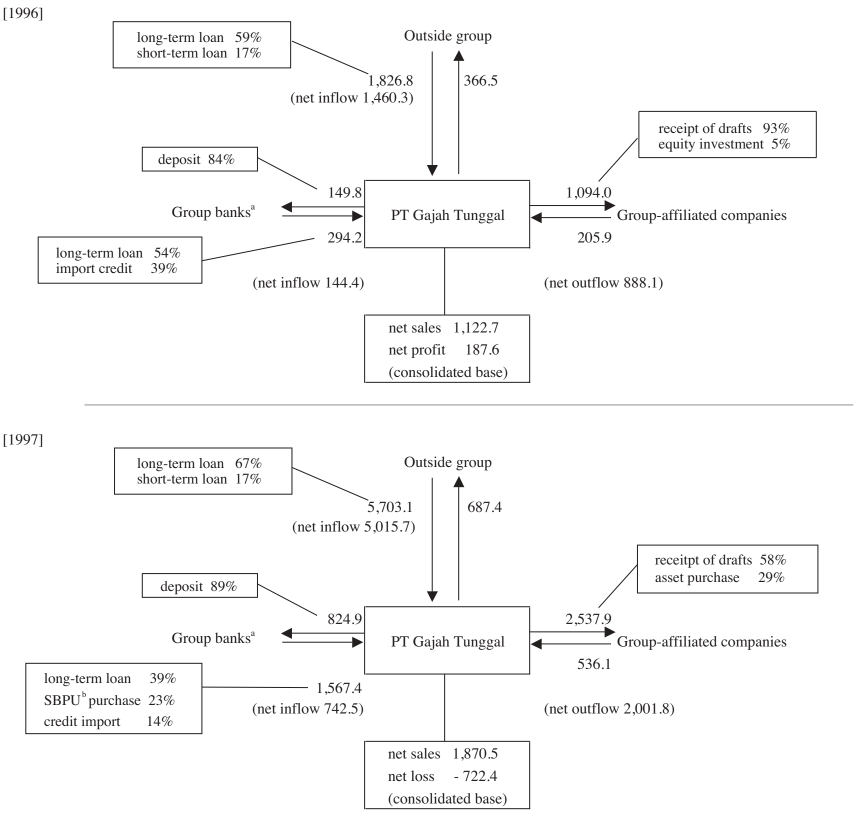
Figure 4.4 Ownership Structure of the Gajah Tunggal Group



Source: ECFIN (annual), Sukmawaty (2000), CISI Raya Utama (1990, 1999), consolidated financial statements of PT Gajah Tunggal 1996–1997 and other materials.

funds and provided them for group companies by utilizing draft transactions. Figure 4.5 illustrates the flow of funds of the Gajah Tunggal Group as of 1996 and 1997, as observed in the consolidated financial statements of the company. Major flows of funds are (i) net inflow from outside to PT Gajah Tunggal; (ii) net inflow from group banks to PT Gajah Tunggal; and (iii) net outflow from PT Gajah Tunggal to other group companies. Major findings are as follows:

Figure 4.5 Flow of Funds of PT Gajah Tunggal



Source: Calculated from consolidated financial statements of PT Gajah Tunggal 1996–1997.
Note: a: BDNI (Bank Dagang Negara Indonesia), Bank Ganesha, and Bank Dewa Rutji.
b: SBPU (Surat Berharga Pasar Uang) is money market securities, a monetary instrument for monetary expansion. It is in the form of promissory notes issued by companies in connection with their borrowings from banks or trade bills drawn by companies and endorsed by a bank.

1. Net inflow of external funds to PT Gajah Tunggal amounted to Rp.1.46 trillion (1996) and Rp.5.02 trillion (1997), which was much larger than the company's annual consolidated sales, amounting to Rp.1.12 trillion (1996) and Rp.1.87 trillion (1997).
2. A major source of external funds (accounting for 59% to 67% of gross inflow) was long-term syndicate loans borrowed by the subsidiaries of PT Gajah Tunggal.

3. Net inflow from group banks to PT Gajah Tunggal amounted to Rp.0.14 trillion (1996) and Rp.0.74 trillion (1997), far smaller than direct inflow of external funds to the company. There was no evidence that intra-group bank lending played an essential role.
4. A major part of inflow from group banks was long-term loans, but PT Gajah Tunggal mostly utilized the group banks as suppliers of import credits and as deposit banks.
5. Net outflow of funds from PT Gajah Tunggal to group companies amounted to Rp.0.89 trillion (1996) and Rp.2.00 trillion (1997), almost on the same scale as the company's consolidated annual sales.
6. A major means of supplying funds to group companies (accounting for 58% to 93% of gross outflow) was that PT Gajah Tunggal allowed the group companies to draw drafts receivable and the company received those drafts.
7. Around 60% of funds supply from PT Gajah Tunggal was allocated to unlisted family holding companies and the remaining 40% was allocated directly to business undertakings. The role of the family holding companies was possibly to pool, coordinate and channel the funds for all the group business, especially for new business that needed fresh funds.

Out of the total net inflow to PT Gajah Tunggal from outside and group banks, the amount of 55% (1996) and 35% (1997) was supplied to group companies, mainly via family holding companies. A long-term overseas bank loan was a major means of fund-raising, while drawing drafts receivable was a dominant means of intra-group fund supply. By this mechanism, the publicly-listed reputable company functioned as an external fund raiser and an internal fund supplier for investment.

Just before the crisis, the total outstanding external debts of the Gajah Tunggal Group as a whole are estimated to have reached US$3.0 billion. Although this amount is less than that of the three largest groups, Salim, Astra and Sinar Mas, the amount is 2.1 times as much as the group's annual sales in 1996, whereas for the three groups the ratios of external debts to sales are 0.3, 0.7, and 0.6 respectively (Table 4.2). It may be safely said that the Gajah Tunggal Group was obviously in a state of over-borrowing. The mechanism as illustrated above is considered to have promoted the group's inclination for over-borrowing and for active diversification investment. From the viewpoint of corporate governance by creditors, the above mechanism widens the asymmetry of information between creditors and owner-managers by disclosing only the well-performing part of the group activities, when actually the creditors' funds are being substantially supplied to other undisclosed parts of the group.

The Gajah Tunggal Group is also a case of family ownership and management. The group's ownership pattern appears to be concentrated ownership by Sjamsul Nursalim and his wife's family, accounting for 62% (1996) and 67% (2000) of listed companies on average (Appendix 1). In management, the weight of family, which was relatively low in 1996 at 46% and 30% in Komisaris and Direksi respectively, further decreased to below 30% after the crisis. It means that the degree of presence of professional managers at the group company level is high. It is also known that management organizations of the group are well structured.

After the crisis in 1997, the Gajah Tunggal Group faced two kinds of debt problems; one was external debt and another was the repayment of central bank liquidity support loans. One of the leading private banks in Indonesia, Bank Dagang Negara Indonesia (BDNI), owned by the group, received emergency loans from the central bank to cope with bank runs amid the crisis, but eventually it was closed by the government. The Sjamsul Nursalim family as owner of the bank was obliged to repay the loans amounting to Rp.28.4 trillion in cash or by sales of assets in four years, so they placed their assets equivalent to the repayment amount under the IBRA's control for sale. These assets included family shareholdings in the group's major businesses, namely, tires, shrimp farming and petrochemicals (marked # in Figure 4.4). As the group's repayment performance was poor, it was criticized by the domestic public, and it was reported that the family tried to gain access to the post-Soeharto governments in order to secure their strategic businesses. On the occasion of formal negotiations with IBRA, Itjih and her niece, Mulyati Gozali, as a top financial director, took charge of the task,[17] showing that the right of final decision making in financial management is still in the hands of the owner family despite the high presence of professional managers. While it seems difficult for the owner family to secure the group's major assets that were heavily debt-burdened, IBRA (substantially the Indonesian government), as well as foreign creditors, had no choice but to accept the low recovery rates of their claims.

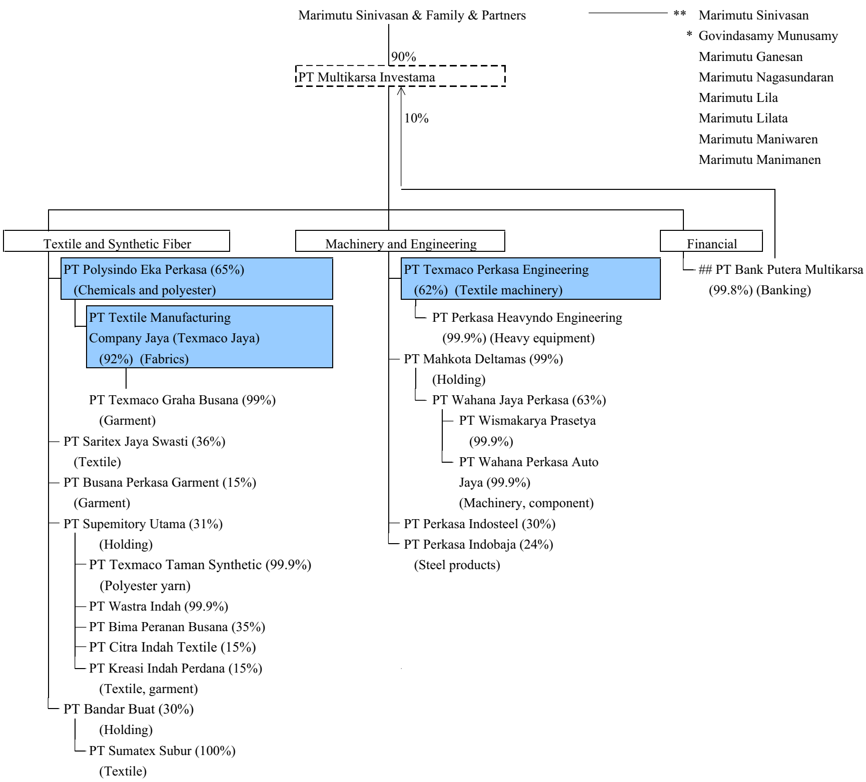
The case of the Gajah Tunggal Group demonstrates that partial disclosure of a business group's information can do more harm than good. This is because external financiers can get information relating only to good business, whereas the funds supplied may be utilized in other group businesses, thus widening the asymmetry of information between owner-managers and outside financiers. Another point shown by this case is that a high presence of professional managers does not mean that professional managers can keep owner-managers in check, as the latter has the right of final decision making, at least in financial matters, at the group level.

4.5 Texmaco Group

The Texmaco Group is one of the largest integrated producers of textiles in Indonesia. The Group has expanded its scale of business remarkably in the last decade, raising its rank in the Indonesian business group sales ranking from 99th in 1990 to 26th in 1996, although the Group has a history of more than two decades. The group's mother company, PT Texmaco Djaja (Textile Manufacturing Company Djaja), was established as a weaving factory in 1970 in Pemalang, central Java. The group expanded its scope of business from weaving to polyester filament yarn spinning in the late 1970s, and to garments in the 1980s. One of the group's unique features lay in its strategy of entering textile machinery manufacturing. The group had become the first producer and exporter of Indonesian-made air jet looms by the early 1990s. This success was highly valued by the then President Soeharto. Owing to Soeharto's support, the group pushed on with a further integration of heavy machinery, trucks and trailers, and their component manufacturing. At the same time, it also moved into upstream integration of the synthetic fiber industry, namely, PTA (purified terephthalic acid) production. Expansive investments into these capital-intensive synthetics and machinery industries accelerated in the 1990s. The annual sales of the group in pre-crisis 1996 reached Rp.1.8 trillion (US$0.8 billion) and its estimated assets were Rp.5.5 trillion (US$2.3 billion).

A major founder and owner-manager of the Texmaco Group is Marimutu Sinivasan, a fourth generation ethnic Indian of Tamil descent born in Medan, North Sumatra in 1937. His father, Sinnaja Marimutu, who engaged in *batik* trading with Malaya, moved from Medan to central Java during the Confrontation period with Malaysia in the 1960s. Weaving factories in the early days of the group's development were set up by his father, a friend of his father, Marimutu Sinivasan and his brothers and sisters. However, a discontinuous spurt in the group's operation after the early 1980s was spearheaded by Sinivasan himself, supported by his younger brothers and professional managers. The group publicly listed three major operating companies (Figure 4.6). In 1996, the ratio of concentrated ownership by Marimutu Sinivasan, his brothers, and the group companies was 72% of the total shares of the three listed companies. The weight of Sinivasan and his brothers in management was 35% on the Komisaris and 77% on the Direksi, as Sinivasan gained the position of President Director of all three listed companies. This is a typical case of founder control of ownership and management.

Figure 4.6 Ownership Structure of the Texmaco Group



** Key figure in developing a business group. A mother company, PT Texmaco Jaya was founded by his late father, Sinnaja Marimutu, and a non-family co-founder in 1970.
* Co-founder
▢ Listed company on the Jakarta Stock Exchange
Liquidated in February 2000.

Source: ECFIN (annual), Sukmawaty (2000), CISI Raya Utama (1999), IBRA's press release No.058, 2 July 2002, and other materials.

The Texmaco Group is the most obvious case of over-borrowing in this case study. Two years after the crisis, it transpired that the Texmaco Group had been granted special financial facilities in 1997 by the Soeharto government in order to avoid a corporate default, and that the group was the largest debtor of irrecoverable loans from domestic banks with a total amount of Rp.17.3 trillion (as of 2001). This amount is 9.6 times as much as the group's annual sales in 1996 (Table 4.2). The Group owed Rp.10 trillion of the debt to the then largest state-owned bank, Bank

Negara Indonesia. As the amount was far in excess of banking regulations on single-customer exposure, the Attorney General stepped in to investigate but dropped the case in the end. Taking into consideration that the group's large-scale capital-goods industry was of 'strategic' importance, the post-Soeharto governments and the IBRA finally decided to take the special step of long-term restructuring for the group. By swapping the bad debt into the IBRA's equity, the IBRA set up a new holding company for the group's indebted affiliated companies and let the holding company issue convertible bonds and repay the debt preferentially to the IBRA.

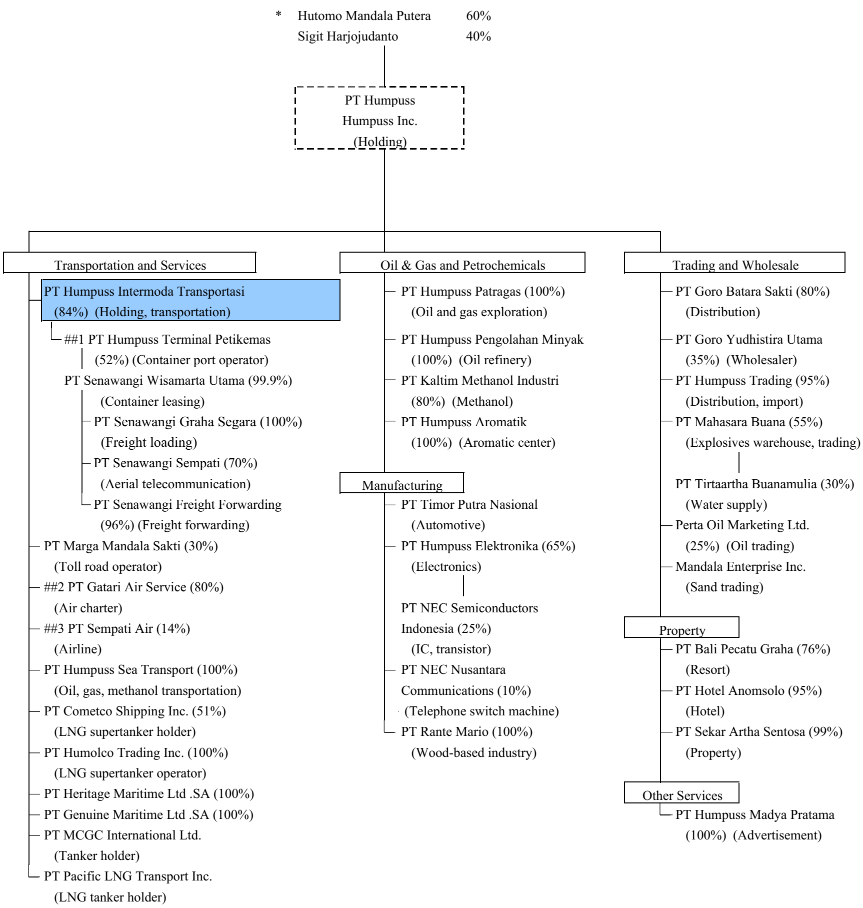
In Texmaco's case, its remarkably rapid growth with aggressive investment in the last decade was supported by the Soeharto government and by excessive loan disbursement by a state-owned bank. As the state bank loans turned irrecoverable after the crisis, the IBRA took over the claims and accountability for the group's financial restructuring. The government also shouldered the costs of bank restructuring. The case of the Texmaco Group demonstrates that exposure to the market by listing major group companies did not help to control the group's behaviour in pursuing excessive borrowing by colluding with the state bank.

4.6 Humpuss Group

The Humpuss Group is led by Hutomo Mandala Putera Soeharto (commonly called Tommy Soeharto), the third son of the former President Soeharto. 'Humpuss' is an abbreviation of his name. The group started with the establishment of PT Humpuss, the group's holding company, in 1984. Within ten years, the Group was ranked in the top 20 business groups, recorded as the most rapid-growth group along with the Bimantara Group, led by his elder brother, Bambang Trihatmodjo. In 1996, the Humpuss Group ranked 18th with Rp.2.3 trillion annual sales (US$1.0 billion).

60% of PT Humpuss was owned by Tommy and 40% by his eldest brother, Sigit Harjojudanto (Soeharto's first son). Tommy was the President Director, and Sigit was the President Commissioner of this holding company, although Sigit's commitment to management was nominal. Seen as a group, ownership of the Humpuss Group was highly concentrated, while management was semi-separated. In most of the 40 affiliated companies, PT Humpuss owned a majority (51% to 100%) of shareholding (Figure 4.7). All the president directors of the affiliated companies were occupied by salaried professional managers. They were without exception *pribumi* who had high educational and professional careers. Tommy was a decision-maker regarding the top personnel of the affiliated companies, as he had a managerial position in the holding company or on the Komisaris of affiliated companies. The degree of

Figure 4.7 Ownership Structure of the Humpuss Group



* Key figure in founding and managing a business group until 1998.
Listed company on the Jakarta Stock Exchange
##1 Taken over by the government in May 1999.
##2 Sold by IBRA in 1999.
##3 Went bankrupt in July 1999.

Source: ECFIN (annual), Sukmawaty (2000), Yayasan Humpuss Group (1994) and other materials.

information disclosure of the Humpuss Group was quite low, as the group had only one listed affiliated company. The Group's plan to make PT Humpuss go public was not realized. Instead, the Group published a decennial corporate history, which was not common practice for

Indonesian business groups. With regard to financial data, however, it contained a minimum of information.

Business lines of the Humpuss Group were highly diversified; (1) sea and air transportation and related services such as port and road construction and management; (2) oil and gas excavation and petrochemicals; (3) manufacturing, for example electronic products; (4) trade and wholesale; (5) property; and (6) advertising. There were at least two strategies which contributed to Humpuss's rapid growth. One was the securing of licence or agency businesses: for example, Humpuss became sole marketing agency for methanol and PTA which Pertamina (the state-owned oil and gas company) started to produce in 1987, obtained the sole domestic marketing licence in 1989 for high-graded gasoline '*Premix*', got involved in a capital participation in 1989 into a Pertamina spot oil marketing company in Hong Kong, obtained a 20-year licence from Pertamina for LNG marine transportation in LNG exports to Taiwan, and so on. The second strategy was, under the banner of privatization, to become the first local private company entering into fields that had been monopolized by state-owned or foreign companies: for instance, possession of LNG tankers, and oil and gas excavation that had so far completely depended on foreign companies, construction and management of a container terminal, waterworks, and storage and distribution of explosives for industrial use that had been exclusively managed by state-owned enterprises. These strategies explain why the group's business foundation lay in the distribution, transportation, and oil and gas industries, in which acquisition of licences was a matter of great importance. Needless to say, Tommy's direct blood ties with ultimate power enabled him to pursue the strategies.

After the crisis, the IBRA revealed that the Humpuss Group was the third largest debtor of irrecoverable loans from domestic banks, mainly from state banks, with a total debt of Rp.5.7 trillion (as of 2001). This amount is 2.5 times the Group's annual sales in 1996. Of the total irrecoverable debt, more than half was borrowed by PT Timor Putra Nasional, a sole importer-cum-assembler of 'Timor', the national car project, which started in early 1996 under the strong leadership of Tommy and the then President Soeharto. Other large borrowers included the owner of several tankers (Humpuss Inc.), a container terminal project in Jakarta (PT Humpuss Terminal), a domestic aviation service (PT Sempati Air), an oil and gas excavator (PT Humpuss Patragas), and the holding company PT Humpuss. The group's debt was partly repaid to the IBRA in assets and was partly pending in court, while Tommy seceded from the group's ownership and management and was found guilty of crimes that he had committed after the collapse of the Soeharto's rule. While the Humpuss Group lost momentum of expansion as a united business entity, its major businesses survived under the respective professional management.

The Humpuss Group is one of the extreme cases of an owner-manager having a close link to the power centre. Owing to its political backing, the group could draw loans worth more than twice as much as its annual sales. Along with the acquisition of various business licences, this abundant borrowing contributed to the group's remarkably rapid expansion. The group's structure of ownership and management was rather straightforward and modernized. However, as the holding company did not disclose information in the form of consolidated financial statements, there was no way of getting an overall picture of the investment and outstanding debt of the group, which was revealed only after the collapse of the political power.

5. Conclusion

In the last section, our task is to reconstruct findings of the case studies in Section 4 in the light of the hypotheses presented in Section 3, to re-examine their validity, and to draw some implications on better corporate governance in the Indonesian context.

First of all, as for concentrated ownership without separation from management that is often negatively evaluated, the case of the Gudang Garam Group clearly demonstrates that that in itself is not an impediment to good corporate governance. Self-governance by owner-managers can work effectively on condition that there is no other key stakeholder and that there is no collusion with the government. Given no major external financier, the natural consequence should be a slow growth of business. However, the Gudang Garam Group succeeded in developing into one of the largest business groups. This is largely owing to the peculiarity of the profitability and growth of their core business, the clove cigarette industry.

Second, there is at least one good example to support the validity of the first hypothesis that information asymmetry between owner-managers and creditors is a possible cause of governance failure, and that is the case of the Gajah Tunggal Group. In this case, information asymmetry becomes serious when business groups disclose partial information by listing only good-performing businesses. The good-performing listed company functions as a fund-raiser from outside and a fund-supplier to various group businesses, which cannot be monitored by creditors due to the unavailability of information. This mechanism allows owner-managers to pursue over-borrowing for the sake of over-investment.

Third, the second hypothesis of collusion with the government as a possible cause of governance failure is also evidenced as valid by the cases of the Texmaco Group and the Humpuss Group. In both cases, the owner-managers colluded with political power, so that they could successfully draw large-scale loans mainly from state-owned banks. The owner-managers were able to utilize political backing to put pressure to banks to lend to them, while the state banks would not refuse the request at the risk of political punishment and because they knew that their possible losses would be borne by the government as a last resort. In fact, the irrecoverable claims of state banks in the crisis were eventually carried over by government finance (substantially by the Indonesian nationals who were taxpayers). Thus in the Indonesian institutional setting, political collusion was one of the causes of the malfunction of corporate governance by domestic creditors. One of the differences between Texmaco and Humpuss is that the former has publicly-listed companies. However, the outcome is not different, showing that exposure to market does not put the brakes on the behaviour of owner-managers in their collusion with the government.

Fourth, the third hypothesis of foreign creditors' monitoring ability as a possible cause of good governance is proved invalid in every case where there was a dependency on foreign debts, namely, in the Sinar Mas, Astra, and Gajah Tunggal Groups. Even in the Astra case, where the group holding company discloses almost all the group business activities so that information asymmetry is regarded as minimum, over-lending to the holding company by foreign creditors took place. This indicates that when there are obvious profit-making opportunities, even foreign creditors with high monitoring ability will put higher priority on pursuit of profits rather than exerting rigorous discipline over customer firms. The Astra case, however, also shows that, in the *ex post facto* debt restructuring process, negotiations with foreign creditors can give the firms discipline.

Fifth, the fourth hypothesis that the effect of public listing is a positive factor in corporate governance is refuted in two ways. First, as the case of the Gajah Tunggal Group shows, public listing of only good lines of business within the group can do more harm than good, because it leads outside financiers to make mistakes in their evaluation of the activities of the whole group, allowing business groups to pursue over-borrowing. To prevent this, information should be disclosed on not just a limited part but on a major part of business group activities by listing group holding companies or divisional holding companies. Second, we should bear in mind that public listing is not necessarily a panacea. As the Astra case shows, it is not always true that the more the disclosure of information on business groups takes place, the better the governance by outside financiers functions. Astra discloses information on its whole group activities by listing its group holding company, but the consequence is a concentration of financiers supplying funds to the company, resulting in over-borrowing. Thus, public listing does not necessarily ensure financiers' governance with an *ex ante* check on excessive borrowing and investment in any way.

Sixth, the final hypothesis that professional managers' function as a check on owner-managers is a positive factor for governance is evidenced as invalid. Both the Sinar Mas Group as an established group and the Gajah Tunggal Group as a rapid-growth group have a relatively high degree of presence of professional managers in managerial posts. Nevertheless, as far as placing a check on the right of the owner-manager to have the final say in decision making in group management (even without having explicit managerial position), the role of professional manager is severely limited. This result implies that a newly introduced system of independent commissioners (non-owner members in the Komisaris) would also have the same limitations.[18]

The results of this case study on Indonesia demonstrate that self-governance of an owner-manager-led business group can function well if there is no key stakeholder and no collusion with the government. When this is not the case, however, self-governance does not work and governance by key stakeholders, namely, creditors or professional managers, over the owner-manager also has crucial limitations. As far as the ability of the professional manager to check on the owner-manager is concerned, we can see that as long as the controlling owner is the ultimate decision maker in management, any internal governance mechanism will have a certain limitation. For better corporate governance, there is a need for a combination of measures targeting business groups themselves, measures targeting creditors, and measures for preventing collusion. Firstly, business groups need to be encouraged to publicly list their key holding companies, as opposed to their operating companies, in order to expose a larger part of their activities to market discipline. This measure has to be accompanied by a strengthening of the monitoring function of the capital market in Indonesia, as the case study shows that market exposure alone does not ensure efficacy of governance. A key point here may be to establish institutions which can impose a threat of exit from the market on business groups whose owner-managers do not obey market rules. In parallel, institutions which will impose a potential threat of liquidation are necessary to ensure the efficacy of governance by creditors in case owner-managers behave against the creditors' interest. Secondly, on the creditors' side, one of the possible means for better corporate governance will be the public listing of banks; state-owned banks in particular, so that the creditors are also exposed to market evaluation. Thirdly, to prevent governance failure owing to collusion, it is essential to develop systems of checks and balances within the government to control possible collusion between power and business, and to develop watch-dog systems in society to monitor possible triangular alliances between owner-managers of business groups, domestic creditors and the government. Measures for this purpose may include

Appendix 4.A1a Data of Publicly Listed Companies under 6 Business Groups, 1996

Group	Name of listed company	Business	Financial indicator			Ownership (%)		Management (%)			
								Komisaris		Direksi	
			ROA (%)	ROE (%)	D/E	Major shareholder*	Public	Shareholder	Non-Shareholder	Shareholder	Non-Shareholder
Gudang Garam											
	PT Gudang Garam Tbk.	Cigarettes	15.2	25.7	0.7	79.7	12.6	33.3	66.7	53.8	46.2
Sinar Mas											
	PT Sinar Mas Multiartha Tbk.	Financing	1.0	17.0	15.8	71.2	11.8	100.0	0.0	0.0	100.0
	PT Bank Internasional Indonesia Tbk.	Banking	1.5	20.8	13.3	49.4	50.6	76.9	23.1	30.0	70.0
	PT Indah Kiat Pulp & Paper Corporation Tbk.	Pulp/paper	3.0	8.5	1.8	82.9	16.9	46.7	53.3	33.3	66.7
	PT Pabrik Kertas Tjiwi Kimia Tbk.	Pulp/paper	4.5	15.0	2.4	65.0	35.0	55.6	44.4	44.4	55.6
	PT SM Agro Resources & Technology Corp. Tbk.	Agro	3.7	10.6	1.9	51.0	49.0	42.9	57.1	56.3	43.8
	PT Duta Pertiwi Tbk.	Property	4.6	16.9	2.7	64.9	34.9	73.3	26.7	28.6	71.4
	PT Plaza Indonesia Realty Tbk.	Property	5.5	8.5	0.5	17.2	11.5	62.5	37.5	100.0	0.0
	Average (mean)		3.4	13.9	5.5	57.4	30.0	65.4	34.6	41.8	58.2
	Average (non-financial, mean)				1.9						

Appendix 4.A1a Data of Publicly Listed Companies under 6 Business Groups, 1996 (*continued*)

Group / Name of listed company	Business	Financial indicator			Ownership (%)		Management (%)			
							Komisaris		Direksi	
		ROA (%)	ROE (%)	D/E	Major shareholder*	Public	Shareholder	Non-Shareholder	Shareholder	Non-Shareholder
Astra										
PT Astra International Tbk.	Automotive	2.8	15.6	4.6	10.7	58.3	75.0	25.0	0.0	100.0
PT United Tractor Tbk.	Machinery	4.1	16.3	3.0	57.5	41.6	77.8	22.2	27.3	72.7
PT Astra-Graphia Tbk.	Electronics	1.8	8.4	3.7	79.1	20.9	100.0	0.0	0.0	100.0
PT Komatsu Indonesia Tbk.	Machinery	16.7	23.2	0.4	0.0	20.7	70.0	30.0	61.5	38.5
PT Sumalindo Lestari Jaya Tbk.	Wood-based	0.7	1.1	0.6	39.9	19.8	57.1	42.9	44.4	55.6
Average (non-financial, mean)		5.2	12.9	2.5	46.8	32.3	76.0	24.0	26.7	73.3
Gajah Tunggal										
PT BDNI Capital Corporation Tbk.	Financing	0.4	6.3	15.9	65.5	34.5	37.5	62.5	0.0	100.0
PT Bank Dagang Nasional Indonesia Tbk	Banking	1.1	17.7	14.5	60.1	39.9	0.0	100.0	40.0	60.0
PT Gadjah Tunggal Tbk	Tire	2.7	7.0	1.6	65.0	35.0	42.9	57.1	33.3	66.7
PT GT Petrochem Industries Tbk.	Polyester	2.6	4.1	0.6	75.0	25.0	80.0	20.0	80.0	20.0

Appendix 4.A1a Data of Publicly Listed Companies under 6 Business Groups, 1996 (*continued*)

Group	Name of listed company	Business	Financial indicator			Ownership (%)		Management (%)			
								Komisaris		Direksi	
			ROA (%)	ROE (%)	D/E	Major shareholder*	Public	Shareholder	Non-Shareholder	Shareholder	Non-Shareholder
Gajah Tunggal (*continued*)											
	PT Kabelmetal Indonesia Tbk.	Cables	0.9	2.8	2.2	53.4	45.5	42.9	57.1	50.0	50.0
	PT Indonesia Prima Property Tbk.	Property	1.7	7.6	2.7	75.6	14.3	77.8	22.2	33.3	66.7
	PT Asuransi Dayin Mitra Tbk.	Insurance	15.4	22.7	0.5	73.9	17.9	37.5	62.5	0.0	100.0
	PT BDNI Reksadana Tbk.	Mutual fund	12.6	13.7	0.1	30.0	66.7	-	-	0.0	100.0
	Average (mean)		4.7	10.2	4.7	62.3	34.8	45.5	54.5	29.6	70.4
	Average (non-financial, mean)				1.7						
Texmaco											
	PT Polysindo Eka Perkasa Tbk.	Chemical	4.1	11.1	1.7	67.6	32.4	25.0	75.0	66.7	33.3
	PT Texmaco Jaya Tbk.	Textile	6.6	19.3	1.9	80.0	20.0	60.0	40.0	80.0	20.0
	PT Texmaco Perkasa Engineering Tbk.	Machinery	5.4	14.4	1.7	69.1	31.0	20.0	80.0	83.3	16.7
	Average (non-financial, mean)		5.4	14.9	1.8	72.2	27.8	35.0	65.0	76.7	23.3
100 largest listed companies (mean)			4.8	14.2	4.7	37.7	30.3	56.3	43.7	36.2	63.8
(non-financial, mean)					1.7						

Appendix 4.A1b Data of Publicly Listed Companies under 6 Business Groups, 2000

Group	Name of listed company	Business	Financial indicator			Ownership (%)		Management (%)			
								Komisaris		Direksi	
			ROA (%)	ROE (%)	D/E	Major shareholder*	Public	Shareholder	Non-Shareholder	Shareholder	Non-Shareholder
Gudang Garam											
	PT Gudang Garam Tbk.	Cigarettes	20.7	36.7	0.8	75.7	22.2	80.0	20.0	18.8	81.3
Sinar Mas											
	PT Indah Kiat Pulp & Paper Corporation Tbk.	Pulp/paper	–2.5	–5.6	1.2	52.6	38.7	45.5	54.5	60.0	40.0
	PT Pabrik Kertas Tjiwi Kimia Tbk.	Pulp/paper	–15.5	–59.4	2.8	63.4	36.6	55.6	44.4	33.3	66.7
	PT SM Agro Resources & Technology Corp. Tbk.	Agro	–14.1	4441.9	–317.0	51.0	49.0	20.0	80.0	45.5	54.5
	PT Duta Pertiwi Tbk.	Property	2.5	7.6	2.1	50.8	34.7	55.6	44.4	41.7	58.3
	PT Plaza Indonesia Realty Tbk.	Property	–0.4	–0.9	1.4	17.2	8.5	57.1	42.9	62.5	37.5
	PT Sinar Mas Multiartha Tbk.	Financing	–2.4	–20.7	7.5	34.0	13.4	62.5	37.5	0.0	100.0
	Average (mean)		–5.4	727.1	–50.3	44.8	30.2	46.7	50.6	48.6	59.5
	Average (exclude SM Agro mean)		–5.2	–19.2	2.0						

Appendix 4.A1b Data of Publicly Listed Companies under 6 Business Groups, 2000 (*continued*)

Group	Name of listed company	Business	Financial indicator			Ownership (%)		Management (%)			
								Komisaris		Direksi	
			ROA (%)	ROE (%)	D/E	Major shareholder*	Public	Shareholder	Non-Shareholder	Shareholder	Non-Shareholder
Astra											
	PT Astra International Tbk.	Automotive	–0.9	–14.0	15.1	0.0	32.0	50.0	50.0	0.0	100.0
	PT United Tractor Tbk.	Machinery	0.1	1.1	8.6	50.0	36.1	71.4	28.6	0.0	100.0
	PT Astra Otoparts Tbk.	Automotive	6.0	18.9	2.1	87.3	12.7	50.0	50.0	0.0	100.0
	PT Astra Agro Lestari Tbk.	Agro	3.0	6.6	1.2	75.3	15.4	50.0	50.0	0.0	100.0
	PT Komatsu Indonesia Tbk.	Machinery	25.0	27.3	0.1	0.0	26.6	66.7	33.3	53.8	46.2
	PT Sumalindo Lestari Jaya Tbk.	Wood-based	–17.1	–145.0	7.5	75.9	14.6	60.0	40.0	0.0	100.0
	PT Astra-Graphia Tbk.	Electronics	2.4	9.4	2.9	79.1	20.9	100.0	0.0	0.0	100.0
	Average (non-		2.6	–13.7	5.4	73.5	22.6	64.0	36.0	7.7	92.3
Gajah Tunggal											
	PT Gajah Tunggal Tbk.	Tire	–10.3	259.6	–26.3	67.3	32.5	30.0	70.0	20.0	80.0
	PT GT Petrochem Industries Tbk.	Polyester	–20.0	102.6	–6.1	69.2	30.8	12.5	87.5	37.5	62.5

Appendix 4.A1b Data of Publicly Listed Companies under 6 Business Groups, 2000 (*continued*)

Group Name of listed company	Business	Financial indicator			Ownership (%)		Management (%)			
							Komisaris		Direksi	
		ROA (%)	ROE (%)	D/E	Major shareholder*	Public	Shareholder	Non-Shareholder	Shareholder	Non-Shareholder
Gajah Tunggal (*continued*)										
PT GT Investama Kapital (BDNI Capital Co)	Financing	–19.1	78.2	–5.1	65.5	34.5	0.0	100.0	16.7	83.3
PT GT Kabel Indonesia (Kabelmetal Ind.)	Cables	–34.5	110.4	–4.2	68.9	29.0	37.5	62.5	37.5	62.5
PT Indonesia Prima Property Tbk.	Property	–10.3	91.9	–9.9	65.5	29.7	37.5	62.5	37.5	62.5
PT Asuransi Dayin Mitra Tbk.	Insurance	7.3	14.1	0.9	73.9	26.1	0.0	100.0	0.0	100.0
PT Reksadana Perdana (BDNI Reksadana)	Mutual fund	–77.5	–37.8	0.0	55.9	38.3	60.0	40.0	0.0	100.0
Average (mean)		–23.5	88.4	–7.2	66.5	31.5	25.4	74.6	21.3	78.7

Appendix 4.A1b Data of Publicly Listed Companies under 6 Business Groups, 2000 (*continued*)

Group	Name of listed company	Business	Financial indicator			Ownership (%)		Management (%)			
								Komisaris		Direksi	
			ROA (%)	ROE (%)	D/E	Major shareholder*	Public	Shareholder	Non-Shareholder	Shareholder	Non-Shareholder
Texmaco											
	PT Polysindo Eka Perkasa Tbk.	Chemical	–48.0	57.1	–2.2	64.5	35.5	75.0	25.0	50.0	50.0
	PT Texmaco Jaya Tbk.	Textile	–28.3	91.0	–4.2	92.0	8.0	100.0	0.0	60.0	40.0
	PT Texmaco Perkasa Engineering Tbk.	Machinery	–10.2	264.7	–27.1	62.1	22.1	75.0	25.0	50.0	50.0
	Average (mean)		–28.8	137.6	–11.2	72.9	21.9	83.3	16.7	53.3	46.7
Humpuss											
	PT Humpuss Intermoda Transportasi Tbk.	Transportation	17.0	110.9	5.5	83.6	16.4	0.0	100.0	0.0	100.0
100 largest listed companies (mean)			–3.5	–11.9	–0.8	25.9	25.0	47.5	52.5	33.4	66.6

Source:compiled from ECFIN (various years).
Note: * Shareholding of a central shareholder, his family members, and holding companies owned by the shareholder.

governmental and non-governmental systems of accusation against collusive behaviours, independent governmental institutions for supervising banks, judicial systems that enable fair judgments, and a vigorous and neutral mass media.

Notes

[1] See Claessens, Djankov and Lang (1999a, 1999b), Claessens, Djankov, Fan and Lang (1999a, 1999b) for discussions on high leverage, ultimate control by few families, expropriation, and diversification respectively.

[2] Regarding the contrast between the shareholder-value perspective and the stakeholder-society perspective, Tirole (2001) believes it is because the former originated in Anglo-Saxon countries, while the latter is in non-Anglo Saxon countries including France, Germany and Japan. Aoki (2001, Chap. 11) traces back the origin of the confrontation to refutation by Dodd (1932) against Berle (1931). Dodd argues that a manager should be "a trustee" not only for shareholders but also for all other stakeholders who constitute a community of the corporation.

[3] The Hart and Moore (1990) firm here means a firm "in which the hierarchical decomposition of organizational information processing is combined with centralized ownership of physical assets by the manager", namely, "the classic proprietor's firm" (Aoki 2001, p. 123).

[4] See also Demsetz (1983), Shleifer and Vishny (1986), and Morck (2000). Originally, Berle and Means (1932) showed that almost half of large American firms did not have a single shareholder with more than 20% of the stock. This notion of dispersed ownership was supported by the main stream of American corporate studies, e.g., Baumol (1959), Jensen and Meckling (1976), and Grossman and Hart (1980).

[5] Other than studies mentioned here, see also Khan (1999).

[6] Minority shareholders can be a key stakeholder and the associated problem of expropriation can be an evidence of failure of corporate governance, as indicated in the reviews in the previous section. However, these are not focused on in this chapter for the sake of simplifying the framework for analysis.

[7] Major foreign creditors can be roughly divided into Anglo-American and Japanese. It is generally perceived that their behaviour is different; the former tends to be risk-taking with shorter-term contracts and are ready to cut debts (haircut) in case of insolvency, while the latter tends to have longer-term contracts, sticking to debt rescheduling in case of insolvency. Nevertheless, this chapter does not regard the difference as critical in affecting the results of the analysis, so it deals with foreign creditors as a single group.

[8] Zhuang et al. (2000, p. 43) points out that the unsound lending practices of banks with low coverage of collateral generally prevailed in pre-crisis Indonesia.

[9] For definitions of an established group and a rapid-growth group, see Table 4.1 note a. and b.

[10] Although the Salim Group is the largest in sales (Rp.53.1 trillion) and in foreign debts (US$5.5 billion), it is not selected; the Astra Group and the Sinar Mas Group are selected from the top 3. This is firstly because Astra and Sinar Mas contrast well in ownership/management pattern and investment behaviour, while the three are almost the same in the level of indebtedness. Secondly, Salim Group has a peculiarity in its dismantling process caused by the repayment of a huge amount of domestic debts (central bank liquidity support loans to a group bank), which relates more to political factors rather than to a failure of corporate governance. The Salim case may need to be examined separately; for example, see Sato (2003).

[11] In the general textbooks of financial management in Japan, a firm with the level of liability to sales within 4 months, or less than 0.33, is evaluated as good performing.

[12] All the results in 1985 mentioned in Section 4 are from Sato (1993). For 1996 and 2000, results are calculated from a database of publicly listed companies on the Jakarta Stock Exchange based on ECFIN (annual). For details, see Appendix 1.

[13] Percentages of owner family in the managerial boards are calculated by the number of posts occupied by the owner family weighted by 3 for Chairman/President, 2 for Vice Chairman/Vice President, and 1 for other board members, and divided by the total weighted value of the posts.

[14] In 2003 the workers of PT Gudang Garam went on the first large-scale strike, in line with a rise of labour movements in Indonesia after the fall of the Soeharto regime in 1998. This event shows that workers are no longer a dormant stakeholder but appear as a crucial stakeholder especially in this group that carries out labour-intensive industry. The conclusion here is true only within the framework of this paper; we have to reexamine whether the Gudang Garam's governance is still effective in governing relations with workers.

[15] Although the foreign creditors were major creditors of the Sinar Mas Group, there was also a domestic creditor, namely, IBRA (the Indonesian Bank Restructuring Agency), an Indonesian governmental agency. BII, the group's bank, which received capital injection from the government, had as much as Rp.12 trillion in non-performing loans owing to APP. In order to complete the bank restructuring, the IBRA ordered BII to transfer the non-performing

loans to IBRA. As APP's creditor, the IBRA then ordered the owners of APP, the Widjaja family, to place their group assets equivalent to the loan amount under the IBRA's control for sale.

[16] Lang (2001a) shows that APP's intra-group lending and the pushing of its debt burden down the pyramid of the group played a crucial role in deceiving creditors.

[17] Based on the author's interview (October 2002) with the then deputy chairman in charge of the IBRA.

[18] For the limitations of outside commissioners, see Fitzpatrick (2000).

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