US toppled Suharto but learned little

Regime change never works as intended

by Steve Hanke in Baltimore

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Nearly 20 years after the US and the IMF toppled President Suharto of Indonesia during the Asian financial crisis, important lessons have still not been learned.

On 14 August 1997, just after the collapse of the Thai baht, Indonesia floated the rupiah, partly in response to turbulence in the currency markets. The move was welcomed by Stanley Fischer, then deputy managing director of the International Monetary Fund and now vice-chair of the US Federal Reserve. He said: ‘The floating of the rupiah, in combination with Indonesia’s strong fundamentals, supported by prudent fiscal and monetary policies, will allow its economy to continue its impressive performance of the last several years.’

But, caught up in the Asian financial crisis, the rupiah did not flourish. By 1998 it had plunged to nearly Rp16,000 per dollar from Rp2,700. To help find a solution, in February 1998 Suharto appointed me to advise Indonesia’s economic and monetary resilience council. I proposed the establishment of an orthodox currency board – the rupiah would be fully convertible into, and backed by, the dollar at a fixed exchange rate. Currency board systems had been widely used and had an excellent track record. On the day the news was announced, the rupiah soared by 28% against the dollar on both the spot and one-year forward markets.

These developments infuriated the US government and the IMF. Ruthless attacks on the currency board idea ensued. Suharto was firmly told by both Bill Clinton, the US president, and Michel Camdessus, the managing director of the IMF – under the sway of the White House – that he would have to drop the idea or forgo $43bn in foreign assistance.

Economists jumped on the bandwagon, finding every imaginable half-truth and non-truth against the currency board idea. Yet the plan had the support of four Nobel prize-winning economists: Gary Becker, Milton Friedman, Merton Miller and Robert Mundell.

Miller later said that the Clinton administration’s objection to the currency board was ‘not that it wouldn’t work, but that it would, and if it worked, they would be stuck with Suharto’. The late US Secretary of State Lawrence Eagleburger recalled: ‘We were fairly clever in that we supported the IMF as it overthrew [Suharto]. Whether that was a wise way to proceed is another question.’ Even Camdessus did not dispute these assessments. On his retirement, he acknowledged: ‘We created the conditions that obliged President Suharto to leave his job.’

The Asian crisis presented a golden opportunity to the neoconservative regime changers led by Paul Wolfowitz, a former US Ambassador to Indonesia and subsequently deputy secretary of defence, who pushed for the invasion of Iraq and the overthrow of Saddam Hussein. Their agenda was for the US to control the greater Middle East, from Indonesia to Morocco.

To depose Suharto, the IMF had to establish a public position of open hostility to currency boards. This deception was required to convince Suharto that he was acting heretically, and that, if he continued, it would be costly. The IMF’s hostility required a quick about-face: less than a year earlier, Bulgaria as well as Bosnia and Herzegovina had installed currency boards with the endorsement of the IMF. In both cases I had had an advisory role. Shortly after Suharto departed, Camdessus announced that the IMF would support Russia if it chose to adopt a currency board.

Another deception involved the widely circulated story that I had proposed to set the rupiah’s exchange rate at an overvalued level so that Suharto and his cronies could loot the central bank’s reserves at a favourable exchange rate. This fabrication was intended to ‘confirm’ Suharto’s devious intentions and rally international political support against the currency board idea so that Suharto could be ousted. The story was at the heart of the Clinton administration’s campaign to dump Suharto, and continues to be repeated today.

Twenty years on, it seems that the US has not learned its lesson. Regime change never works as intended. In Asia, China has filled the vacuum created by the discredited efforts of the US and the IMF. As for the neoconservatives who embrace regime change and the dream of a US-controlled greater Middle East – in spite of many failures, they continue to embrace their doctrine.

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