INDONESIA'S MISSING MULTINATIONALS:
BUSINESS GROUPS AND OUTWARD DIRECT INVESTMENT

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Michael Carney* | Marleen Dieleman*

Concordia University, Montreal | *National University of Singapore*

Some countries produce more multinational enterprises (MNEs) than others. India and China, in particular, have produced a number of dynamic MNEs whose success abroad generates important economic benefits for the home economy. Motivated by this observation, we describe the internationalisation record of Indonesia's major business groups. Using an archival analysis method we find that, with a few exceptions, Indonesia's largest business groupings focus predominantly upon the domestic market. We advance two explanations for this investment pattern. The first suggests that the apparent absence of Indonesian MNEs is an accounting error, because firms' outward investment is under-reported in official statistics. The second suggests that Indonesian outward foreign direct investment is impeded by a combination of institutional and firm-level factors that arrest the internationalisation of all but the largest firms. We discuss the policy implications of these findings and reflect on their theoretical implications.

INTRODUCTION

Multinational enterprises (MNEs) from Asian countries such as India and China are becoming major players in the globalised world economy, and their recent dynamism has attracted much attention from scholars (for example, Buckley et al. 2007). Economists and management scholars agree that outward direct investment (ODI) by emerging market MNEs strengthens their competitive advantage and provides their countries of origin with a number of economic benefits, including improved export performance and access to foreign technology (UNCTAD 2006). Low ODI may signal lagging international competitiveness, and is therefore of potential concern to policy makers. Research to date has focused almost exclusively on emerging markets that produce successful MNEs; scant attention has been given to explaining why some emerging markets engender relatively few multinational firms.

Indonesia's record is somewhat unclear in this regard. Research suggests that some Indonesian firms have successfully internationalised (Lecraw 1993), especially those owned and controlled by

* mcarney@jmsb.concordia.ca; marleen@nus.edu.sg. We thank the editor and two anonymous reviewers for their constructive and insightful comments on an earlier version of this manuscript. Michael Carney acknowledges the financial support of the Canadian Social Science and Humanities Research Council, and Marleen Dieleman that of the Singapore Ministry of Education's Tier 1 Grant R-313-000-079-112.

Chinese Indonesians (Liu 2001; Sato 1993). Yet official statistics show that Indonesia has produced few substantial MNEs. In the past five years, Indonesia did not have a single firm in the top 100 non-financial transnational corporations from developing countries, according to an annual ranking published by UNCTAD. The latest list, released in 2010, shows Singapore as having seven representatives, Malaysia six and both Thailand and the Philippines one firm each. In firm-level data on the number of new overseas greenfield investments undertaken in the past five years, Indonesia almost fails to register, its score dwarfed by those of the big players in the region – India, China and Malaysia – and well below those of Thailand, Vietnam and the Philippines (figure 1).[1] In short, these metrics point to a relatively modest international investment record on Indonesia's part.

----FIGURE 1 ABOUT HERE----

Opinion is divided on how to interpret Indonesian ODI statistics. Indonesian officials often point to the idiosyncrasies of their economy and stress disadvantages of ODI such as capital flight and tax evasion. Officials also assume that ODI metrics under-estimate actual outward investment because Indonesian firms may misreport or under-state their foreign investments. Consequently, the international performance of Indonesian firms is difficult to measure, and the appropriate stance of the Indonesian government on ODI policy remains unresolved. Improved understanding of Indonesian firms' ODI performance can inform the policy debate on whether the governments of Indonesia and other emerging market countries should implement policies to accelerate or otherwise influence their ODI.

We contribute to this debate by documenting the internationalisation patterns of Indonesia's largest business groupings and developing plausible explanations for them. To do so we use an archival analysis method that identifies ODI activities (hereafter 'events') undertaken by Indonesia's largest business groups over a 13-year period. Whereas official statistics give an aggregated overview of ODI, the contribution of our methodology is to provide fine-grained insight into the international investment record of specific firms. We focus upon the ODI of firms affiliated with 25 of Indonesia's largest business groups, because we expect them to be the best endowed with the resources necessary for international expansion. We begin with a brief review of evidence and theory on emerging economy ODI. We then outline some shortcomings of ODI accounting in Asia's emerging markets. We report our internationalisation findings on Indonesian business groups and suggest two explanations. Our conclusion discusses implications for policy and theory.

[1] The city-states of Singapore and Hong Kong are excluded from figure 1 (and figure 2, below) because their ODI data are inflated by pass-through investments that originate in other countries.

FDI AND ODI IN ASIA

In recent decades Asia's industrialising states have embraced inward foreign direct investment (FDI) as part of their industrial policy programs. States such as China, Korea, Malaysia, Thailand and Singapore have offered generous investment incentives to foreign MNEs to boost economic development. Since the early 1970s Indonesia too has made its foreign investment rules more accommodating, albeit with occasional back-tracking (Hofman, Zhao and Ishihara 2007). On the other hand, industrialising states have been more circumspect about the promotion of *outward* direct investment by domestic firms, because of concerns about capital flight and tax evasion, and the fear that ODI 'hollows out' domestic industry by transferring jobs to other countries.

ODI can benefit the originating country's economy only if it has a positive impact on the performance of the parent firm undertaking a foreign project. There are both risks and benefits associated with ODI. The risks include unfavourable movements in exchange rates, failure to understand foreign business practice and cultures, and additional managerial costs associated with coordinating geographically dispersed operations. Realisation of ODI's potential benefits will depend upon the parent firm's objectives and its organisational capabilities. Scholars and policy analysts typically distinguish three distinct motives for undertaking ODI: efficiency-, asset- and market-seeking motives. Efficiency-seeking ODI is directed at accessing low-cost inputs such as cheap labour and materials. Asset-seeking ODI is directed at the acquisition of technology, marketing skills, research and development (R&D) laboratories and distribution facilities that are unavailable in the home market but can improve the parent firm's competitive capabilities. Market-seeking ODI is aimed at generating revenues in foreign markets; its occurrence assumes that the parent firm possesses a proprietary capability that gives it an advantage over local firms in those markets. Each type of ODI can improve the firm's performance by lowering its costs, increasing its competitiveness or providing additional revenues.

There has been something of a sea change in the importance states attach to having their own MNEs. Recent statistics report a surge in ODI from emerging economies, most of it originating in Asia (UNCTAD 2006). States increasingly recognise ODI's potential to enhance the international competitiveness of domestic firms. They also perceive that accelerating the development of local MNEs can improve competitiveness within the domestic market, because knowledge of international best practice and technological know-how can spill over and be diffused through linkages with local suppliers and competitive imitation by rivals. Foreign technology and practice are often more valuable in the hands of domestic firms, whose superior local knowledge allows modification to fit domestic conditions (Szulanski 1996). Market-seeking ODI is critical to consolidating export sales and market expansion. It helps firms to develop international networks and relationships through which they can initiate activities rather than serving merely as dependent sub-contractors at the periphery of international value chains.

Lecraw (1993) suggests that Indonesian firms engaging in ODI improved both their management expertise and their export performance to a greater extent than firms that did not make such investments.

Concern that ODI results in the loss of domestic employment may be over-stated. Evidence from emerging markets in fact suggests that ODI has a marginally positive impact upon aggregate employment levels (UNCTAD 2006: 189). Lost jobs are more closely associated with efficiency-seeking ODI, such as occurs when parent firms seek cheaper labour abroad. Emerging market MNEs are unlikely to undertake efficiency-seeking ODI because of the continuing availability of low-cost domestic labour. They are more likely to undertake asset-seeking ODI projects, which generally have a positive impact on employment levels at home.

While Indonesia's inward FDI performance has recently been quite strong –its ODI record appears less so from the data presented above. Nevertheless, if we look at aggregate ODI scaled by GDP, Indonesia seems to be on a par with other emerging Asian economies (figure 2). When ODI is measured relative to economy size, Malaysia emerges as a clear front-runner during the years 2005–09. There is little to differentiate India, Indonesia, Thailand and China, although this group is well in front of the Philippines and Vietnam.

----FIGURE 2 ABOUT HERE----

THEORETICAL APPROACHES TO ODI FROM EMERGING MARKETS

Research on emerging market MNEs has been under way for several decades. More recently, the emergence of Chinese and Indian multinational enterprises has given new impetus to this research stream. One point of consensus in the research is that the international activity of MNEs from advanced countries is attributable to the creation and leverage of proprietary technological and organisational capabilities that drive their market-seeking ODI. By contrast, scholars believe that firms from emerging markets typically lack the firm-specific advantages required to compete successfully in international markets. This is because economic and competitive conditions in the host country provide few country-specific advantages conducive to the development of world-class organisational and technological competence.

The consensus of research on emerging market MNEs is that many firms internationalise for asset-seeking reasons – that is, to acquire resources and competencies that are unavailable locally (Luo and Tung 2007). Child and Rodrigues (2005) suggest, for example, that Chinese firms' international strategies seek to address competitive *dis*advantage. To bring their skills up to par, firms must invest considerable resources in learning, either through the formation of strategic partnerships or the gradual accumulation of skills, information and technologies (Hobday 1995). To the extent that emerging market firms can leverage their competencies in foreign markets, scholars think that these skills are derived from the

capacity to manage in harsh or corrupt environments (Cuervo-Cazzura and Genc 2008), but such capacities are of less value in more advanced markets.

Aside from firm-specific factors, external factors such as home-country institutions also influence ODI (Peng, Wang and Jiang 2008). Advanced economies typically benefit from a functioning matrix of institutions, comprising enforceable contracts, government regulation and efficient capital markets. They also possess a diverse array of specialised institutions such as standards committees, accreditation agencies, consumer watchdogs, market research firms, executive recruitment agencies, business schools and vocational training institutes that facilitate market transactions. Niskanen (1991: 223) has described these institutions as the 'soft infrastructure of the market economy'. In contrast, many emerging markets are characterised by extensive institutional and market failure – a condition that management and finance scholars term an 'institutional void' (Khanna and Palepu 1997).

However, scholars disagree about whether institutional voids are an asset or a liability for the internationalisation of firms. On the one hand, institutional voids such as weak regulations or unenforced product safety standards can create negative perceptions of a country's enterprises that inhibit their foreign expansion, while institutional voids in capital markets can deprive firms of the resources needed to pursue international opportunities.

On the other hand, institutional voids can stimulate the formation of MNEs if they facilitate the emergence of large diversified business groups. Diversified business groups can arise and thrive in emerging markets because of their capacity to span institutional voids by internalising market failures. Business groups that attain sufficient scale can do this by substituting for missing soft market infrastructure, and can provide their affiliates with resources such as capital, experienced management, finance, technology, and marketing and political lobbying services (Khanna and Palepu 1997). Compared with free-standing firms, the affiliates of large business groups enjoy considerable advantages in assembling the resources needed to pursue international opportunities. Institutional voids can also stimulate foreign expansion if they cause domestic firms to flee home-country conditions. For instance, weak intellectual property protection and a lack of venture capital may drive small high-technology firms to internationalise in order to gain access to foreign capital markets and better legal protection for their intellectual property (Yamakawa, Peng and Deeds 2008). Similarly, political risks and the threat of expropriation in volatile emerging markets may drive firms to invest abroad (Witt and Lewin 2007). In summary, much existing research suggests that emerging market firms internationalise both because of and in spite of home-country conditions.

Both institutional voids and business groups are a feature of Indonesia's business environment, and there are incentives for Indonesian firms to engage in 'institutional escape'. World Bank indicators of

government effectiveness, regulatory quality, rule of law and ability to control corruption reveal Indonesia to have significantly negative coefficients of state governance capacity (Kaufmann, Kraay and Mastruzzi 2007). World Economic Forum indices show that Indonesia ranks low on factors such as goods market efficiency, financial market sophistication, technological readiness and protection of property rights. For instance, on a measure of intellectual property protection, Indonesia ranks 102nd in a survey of 134 countries (Schwab and Porter 2008). In both Indonesia and Malaysia, government discrimination against business people of Chinese descent may also spur internationalisation.

In view of the rise in ODI from emerging markets in the last decade, the literature tends to focus primarily on why firms internationalise (drivers) rather than on what obstacles might prevent them from competing in global markets (inhibitors). Our contribution is to complement existing literature by looking at the interplay between institutional and organisational factors that enable and inhibit internationalisation, and at how these factors affect different firms. In doing this we help to explain why some firms fail to internationalise. In combination, theories of institutional drivers and obstacles promise to offer a more balanced account of globalisation of firms from emerging markets.

ACCOUNTING FOR ODI IN EMERGING MARKETS

Scholars typically use aggregate statistics such as the volume of annual inward and outward FDI flows to assess a country's international investment performance. Business scholars also use firm-level indicators such as the percentage of sales derived from overseas or the percentage of assets located outside the home country. However, official statistics on ODI collected by organisations such as the OECD and the United Nations, and used to construct country-level and firm-level indices of internationalisation, do not necessarily provide an accurate picture of ODI from emerging markets. These statistics may significantly over- or under-estimate the true level of ODI, because they fail to take account of institutional factors and firm practices in such markets.

One indication of over-estimation is that a small number of emerging economies are responsible for a very high share of ODI outflows. For example, in 2005 just four economies (Hong Kong, the British Virgin Islands, Russia and Singapore) accounted for 60% of the stock of ODI from developing and transition economies (UNCTAD 2006). Much of this presumed investment may be statistically inflated by the phenomenon of 'round tripping' – a term that refers to capital outflows channelled offshore into special-purpose entities that subsequently return the funds to the economy of origin, usually to take advantage of inward foreign investment incentives.

Official statistics may also under-state the extent of emerging economy ODI. Official statistics on ODI are founded on the assumption of direct or indirect ownership of subsidiaries, associate companies and branches by a common parent (OECD 1999). This assumption may be invalid if firms display

fragmented ownership or if they achieve control over foreign firms by non-ownership means. Firms in emerging markets are often organised as business groups whose inter-organisational linkages are not necessarily characterised by legal ownership, but whose members are integrated through a variety of other social and informal mechanisms (Khanna and Palepu 1997). Business group affiliates located in different national jurisdictions may transfer resources to other affiliates through devices such as related-party transactions (Cheung, Rau and Stouraitis 2006). In addition, investment and trade are often conducted through ethnic and family networks in a manner that blurs the origin and destination of capital flows (Rauch 2001). To the extent that ODI statistics reflect ownership assumptions that are not apposite in Asia, they may under-estimate the true extent of firms' international activities.

In much of Asia a substantial proportion of a country's largest publicly listed firms are affiliated with a business group (La Porta, Lopez-de-Silanes and Shleifer 1999). In Indonesia the figure is almost 70% (Claessens, Djankov and Lang 2000). This fact poses a considerable empirical challenge, because capital flows among affiliates are often non-transparent. In emerging markets, institutional voids such as weak property rights and inefficient contract enforcement result in little support for transactions, and firms come to rely on informal arrangements such as family ties, government connections and business group structures to support transactions with their business partners. As in other emerging markets, many Indonesian firms have become affiliated with business groups with pyramidal and opaque corporate governance structures that are believed to facilitate and obscure inter-firm resource exchanges (Morck and Yeung 2003). Pyramidal structures and weak disclosure standards suggest that the financial data disclosed by individual companies may paint a misleading picture of the disposition of their assets. This means that firm-based measures of internationalisation, such as those created in the the UNCTAD Transnational Index (which identifies the world's largest multinational firms based upon their foreign' assets, sales, employment is derived from annual reports) may not accurately reflect the true international scopeof firms affiliated with Indonesian business groups. Moreover, many Indonesian outward foreign investments might not be initiated by publicly listed companies, because families have an incentive to maximise control over foreign currency management within the group, which would be subject to restrictions if a listed company were involved.

It is generally believed that official statistics on Indonesia's FDI and ODI suffer several shortcomings (Hattari and Rajan 2008). Most experts consider official ODI figures to be under-stated. Indeed, our interviews suggest that Indonesia's large business groups face incentives to 'hide' their foreign investments. Because the owners of most of the large business groups are of Chinese descent, ODI carries the stigma of disloyalty to Indonesia, and is often portrayed negatively in the Indonesian press. To avoid problems, large business group owners often set up platforms in Hong Kong or Singapore from

which internationalisation is pursued. Such activities prevent the foreign investments from being reported in official Indonesian statistics.

ARCHIVAL ANALYSIS METHODOLOGY

We use a qualitative archival analysis method to complement official macro-level and firm-level statistics – namely, systematic collection and coding of published news sources. We focus on business groups because most Indonesian firms operate as part of a group. In addition, the UNCTAD list of the world's largest transnational companies from developing countries shows that many of the emerging market MNEs are business groups. We began by identifying the largest business groups in Indonesia, and then documented cases of their internationalisation using a database of worldwide news articles. To contextualise our results and facilitate explanation, we conducted background interviews with several bankers and executives from the Jakarta business community.

First, we identified Indonesia's top 25 domestic privately owned business groups. Because most such groups are owned by families, we were able to estimate the approximate size of the business groups from reports of family wealth. We constructed a list of the largest groups in the country using the following four sources: a report on Indonesia's largest business groups developed by the global financial services firm UBS; a report on Indonesia's 40 richest families in the *Forbes* international business magazine; the September 2007 issue of the Indonesian business magazine *Globe Asia*), which included a list of the top business groups (pp. 32–128); and the August 2007 issue of *Globe Asia*, which contained a list of Indonesia's richest individuals (pp. 29–136). We limited ourselves to the top 40 from each source. (In the UBS report there was no ranking.) The sources agreed on the 15–20 main groups, diverging more in relation to the smaller groups. On the basis of size and inclusion in multiple sources, we selected 25 business groups. An overview of the four lists, together with our combined list, can be found in table 1.

----TABLE 1 ABOUT HERE----

Second, we conducted a structured search of each group's foreign business activities in the LexisNexis news media database. Substantial foreign investments are typically reported in the business news media in Indonesia and/or in the country receiving the investment. The use of each group's name as a keyword elicited a considerable number of articles for each of the top 25 groups (table 2). To deepen the pool of articles on each group's activities, we performed complementary searches using the names of group owners and of prominent group-affiliated companies.

Third, we conducted a content analysis and coding procedure recommended by Boyatzis (1998) and used in an Indonesian context by Dieleman and Sachs (2008). We first condensed the raw data into 'business events' – discrete strategic decisions taken by a focal company. Examples of such events include starting a new line of business, forming a strategic alliance, exiting a business, initiating a merger, and

expanding production capacity (either in Indonesia or abroad). Events that were a continuation of an already existing line of business, such as the introduction of a new brand or the upgrading of an existing manufacturing plant, were not taken into account. Between 1994 and 2006 – a period of some 13 years – we identified a total of 958 business events (n = 958) for our sample. We selected 1994 as a starting point because before that year our database contained too few events for most of the top 25 companies in the list.

Fourth, to determine a business group's international activities we employed a simple count of occurrences of ODI in the reported business events, using presence/non-presence coding (Boyatzis 1998), and identified 197 (n = 197) unique ODI cases and their destinations. In this way we created a 13-year inventory of foreign investments by large Indonesian business groups. The use of presence/non-presence coding does not enable us to assess the importance of any specific ODI occurrence, but this can be done by going back to the original rich data about each event and interpreting a series of separate events as an emergent pattern. The richer underlying data were used to formulate explanations for our results, which now follow.

In concluding this section we note some shortcomings in our archival analysis methodology. Not all foreign investments are reported in news media articles, which typically show a bias toward the reporting of large investments. As with all sources, news articles can only partially resolve the problem of non-disclosure of foreign investments. For example, conversations with members of the Jakarta business community suggest the existence of substantial foreign investments that have gone unreported in the news media. Consequently, we expect that our data could be biased, because some groups have adopted non-disclosure policies in their corporate communications. Despite these evident shortcomings, we propose that our data, in combination with existing macro-level and firm-level statistics, provide a fuller and more accurate depiction of Indonesian business groups' ODI activities than has existed hitherto.

RESULTS

Table 2 contains the sample of 25 business groups; the keywords used in the LexisNexis search; the number of news articles retrieved for each business group; the number of business events abstracted; and the number of ODI occurrences. One group (Wings) was discarded because there was too much 'noise': there were too many companies and products named 'Wings' worldwide, and it was not easy to distinguish when the Indonesian company was being referred to. We found foreign investments in our database for 16 of the remaining 24 groups.

-----TABLE 2 ABOUT HERE----

Limited internationalisation

The data in table 2 suggest that Indonesian business groups have little appetite for international activity. Of the 24 largest groups, most have hardly ventured abroad in the past 13 years. Our results show that eight groups (33%) display no internationalisation at all – at least in a manner that is captured by our methodology. An even larger proportion display only a very limited degree of international activity. In general, groups with no foreign investments tend to be smaller.

We labelled groups with more than 30 ODI events over the 13 years 'emerging market giants'; those with 6–30 ODI events 'intermediate' (intermediately internationalised) groups; and those with five ODI events or fewer 'domestic' groups. This classification is arbitrary, but table 2 shows that two groups are clearly outliers, with over 60 ODI occurrences each; there is a small cluster of intermediately internationalised companies, and a large group of companies with hardly any ODI occurrences. Based on this classification, only two groups (Salim and Lippo) can be considered as emerging market MNEs, and these two groups are in fact closely related (historically, at least): the founder of the Lippo Group (Mochtar Riady) worked for the founder of the Salim Group (Liem Sioe Liong) before striking out on his own. Only seven groups had more than five ODI occurrences over the 13-year period. This low level of internationalisation is in marked contrast with what is revealed by the literature on ethnic Chinese firms from Southeast Asia: they are typically portrayed as transnational empires that invest extensively in the region and in China (Yeung 2004). Given that all but three groups in our sample are controlled by families of Chinese descent, with two notable exceptions our research does not support the notion of these families running 'transnational' enterprises in the Indonesian case. Rather, table 2 suggests that a substantial category of large Indonesian business groups is focused almost exclusively on the domestic market.

If we compare our results to ODI statistics on Indonesia, there are evident discrepancies. In 2006 alone we recorded 18 foreign investments for the Lippo group. Returning to the original news articles to assess the significance of these investments, we found that Lippo's media-reported investments summed to almost $2 billion, whereas Indonesia posted total official ODI of $2.7 billion in 2006. While Lippo is a large group, it seems unlikely that it alone accounted for almost all of Indonesia's ODI in that year. This example suggests that errors in either or both figures are likely, because official statistics under-estimate ODI and because reported investments may not match actual investments. Notwithstanding these discrepancies, our data appear to point in the same direction as the official statistics, in the sense that we found relatively limited ODI among Indonesia's largest business groups.

Distribution of ODI occurrences

Figure 3 shows the distribution of the 197 foreign investments by company. Salim and Lippo account for almost 70% of the reported ODI events, suggesting that these are by far the most internationally active of the Indonesian business groups (with the caveat that we are focusing on events, and not money amounts). The news reports show that these groups have established footholds in Hong Kong and Singapore, diversifying internationally from there. In fact, one Salim Group firm, First Pacific Company, even made it into the UNCTAD top 100 non-financial transnational companies from developing countries, listed as a firm from Hong Kong. A third group, Sinar Mas, displays a similar pattern, albeit on a much smaller scale. All three groups control listed companies in Singapore, and have appointed second-generation family members as executives responsible for directing the internationalisation of their group's activities. By locating their international activities in a foreign jurisdiction these groups can to some extent disguise their ODI activities so as to avoid charges of taking capital out of Indonesia. Consequently, their foreign investments are unlikely to turn up in official ODI figures for Indonesia. In this respect, our database is more complete than the official data.

ODI destination

Figure 4 provides the destinations of Indonesian business groups' ODI. The pattern of investments shows that most Indonesian business groups are primarily regional rather than global players – a phenomenon that has been documented for other Asian firms (Collinson and Rugman 2007). The primary destinations of Indonesian ODI are China, Singapore, Australia, India, the Philippines, Malaysia and Vietnam – Australia being the only developed country destination of any importance. The high levels of investment in China and India are not surprising, given the size of these economies and their rapid rates of growth. The literature on ethnic Chinese family groups suggests that Chinese Indonesians may be inclined to invest in their ancestral country – another factor that may also play a role.

While much of Indonesian ODI is destined for other emerging markets, including those in East and Southeast Asia, some firms have invested in more distant emerging markets in Latin America (Raja Garuda Mas), Africa (Kalbe Farma), the Middle East (Bakrie, Salim) and Central Asia (Bakrie, Salim). These trends are consistent with the suggestion that emerging market firms are more likely to invest in other emerging markets, because these markets share institutional characteristics that are similar to those in the country of origin (cf. Cuervo-Cazurra and Genc 2008). For example, Buckley et al. (2007) find that Chinese firms invest heavily in countries characterised by high political risk, suggesting that Chinese MNEs may enjoy an advantage in managing difficult institutional contexts.

Time trends

Our data show that significant fluctuations in ODI are likely to be related to the business cycle (figure 5). The decline in 1996 may have been a harbinger of the AFC, during which ODI fell to very low levels. More recently, ODI has shown a strong positive trend. However, given the results discussed above, this may be driven primarily by a small number of increasingly global firms. It obscures the prevailing reality that ODI is limited in the majority of Indonesia's large business groups.

----FIGURE 3 ABOUT HERE----

----FIGURE 4 ABOUT HERE----

----FIGURE 5 ABOUT HERE----

EXPLAINING INDONESIA'S MISSING MNEs

Relative to its regional neighbours Indonesia generates a limited number of prominent multinational firms. Our analysis finds that ODI is driven by a very small number of internationally active business groups, and that the majority of Indonesian business groups are focused on domestic activities. To the extent that ODI is directed at seeking strategic assets, Indonesia's economic development may be impeded by the absence of a larger number of home-grown MNEs. Given the accounting ambiguity about international capital outflows from emerging markets, we now consider whether both official statistics and our methodology have under-estimated the true extent of Indonesian firms' international activities. In addition, we consider whether our methodology accurately depicts the limited internationalisation of Indonesia's business groups, and discuss the extent to which institutional voids explain the patterns documented above.

Hidden dragons?

The first explanation for the apparently limited internationalisation of Indonesian firms is a 'hidden dragons' explanation. It suggests that domestic factors cause firms to internationalise in a manner that is not readily identified by our methods. This explanation suggests that Indonesia's missing MNEs represent a 'type two error' or false negative: their ODI is significant but not readily apparent. Possible sources of a type two error are of two kinds.

It may be that our sample of Indonesia's largest 24 business groups is biased. If the large business groups in the sample are more locally oriented than the population of free-standing firms or the affiliates of smaller groups, then the missing MNEs might be found among the latter. Our method is unlikely to capture ODI in smaller firms, because their international activities do not draw the attention of the international media.

A second possibility is that domestic considerations may encourage business groups to conceal their ODI activities in an informal international economy. The informal economy consists of a range of activities that are *unreported, unrecorded or informally organised* (Portes and Haller 2005). We cannot say with certainty that the groups in our sample are engaged in any or all three forms of informal activity, but we enumerate them as a guide to further research.

First, it is well established that high tax rates can stimulate an increase in visible ODI as firms seek to shift activities to lower tax jurisdictions offshore. Equally, high tax rates can stimulate tax evasion through invisible intra-firm transfers such as the use of special purpose entities registered in tax havens (OECD 1999). More generally, opaque business group governance structures allow cash to flow upwards into privately held family firms that may seek to preserve family wealth and evade home-country taxes by channelling resources into *unreported* foreign investments. While our archival data cannot detect such activity, our interviews with analysts and bankers suggest that it is widespread among Indonesian groups. One source with experience of Indonesian business groups explained in an interview that, in his view, tax reduction was the main rationale for the complex legal structure of Indonesian business groups, which tend to span multiple jurisdictions.

Second, it is well known that ethnic diasporas constitute important networks that facilitate international trade (Tung and Chung 2010). Chinese Indonesian business groups may participate in ventures with fellow ethnic Chinese through minority investments, but if investments in such projects constitute less than 10% of the share capital they are recorded as portfolio investments. Morck, Wolfenzon and Yeung (2005) document how family business groups exercise *de facto* control over great swathes of the corporate sector through pyramidal structures with equity ownership stakes of less than 10%. Similarly, other capital arrangements, such as loans made through a group's in-house private bank, may not be recorded as direct investment, even though a core firm may exercise *de facto* control of the invested firm. To the extent that these investments cross borders they constitute an important source of ODI, but they go *unrecorded*. If Indonesian business groups make extensive use of such financial instruments, then their participation in ODI may be under-stated.

Third, foreign direct investment may go undetected because it occurs within an *informal* setting. Productive foreign investment may be informally organised in an intra-family wealth transfer (Tung and Chung 2010). Saxenian (2002) describes the importance of this phenomenon for foreign-born Silicon Valley entrepreneurs who raise funds through family networks. In other cases, trading companies affiliated with business groups facilitate the operation of global commodity chains (Gereffi 1994), in which firms engaged in recurrent relational contracting may control a network of foreign assets without actually owning them. Large segments of these chains are organised into informal sub-contract networks so as to avoid burdensome regulations. Each of these cross-border capital flows represents significant

activity, but is unreported as ODI. This contributes to the under-stating of the scope of international activity.

The above discussion suggests that processes of globalisation have engendered ethnic and relational communities that straddle geographic boundaries and are 'neither here nor there'. Entrepreneurs embedded in these communities adopt a form of transnational organisation in which foreign direct investment has little meaning, because firms cannot easily be identified with a specific national home base (Yeung 2004).

Missing dragons?

The second explanation is a 'missing dragons' explanation, suggesting that a complex interplay of family ownership and management and institutional voids may leave firms with structural characteristics that impede ODI. First, family-owned and family-controlled firms typically prefer domestic rather than international diversification (Gomez-Mejia, Makri and Kintana 2010). Risk aversion and a desire among family management to retain close control constrain family firms' international opportunities because of the high costs associated with coordinating geographically dispersed operations. Sometimes family firms limit participation in the senior management team to a small cadre of trusted insiders and are not inclined to recruit professional managers with detailed knowledge of international markets. Moreover, the firms' most important social and political networks are based on local connections. Such networks are unlikely to help when the firm ventures across international borders.

. Many large Southeast Asian business groups attained prominence before the widespread implementation of liberal market policies and growing globalisation (Yoshihara 1988). These groups became especially attuned to the conditions of a pre-liberalisation phase of economic growth and aligned their structures and business practices with them. With liberalisation and globalisation these firms became increasingly out of tune with emerging business conditions, because they continued to rely on their connections instead of developing organisational capabilities that may have facilitated their international growth (Carney and Gedajlovic 2002; Dieleman and Sachs 2008).

This is especially evident in Indonesia, where many business groups emerged in the late 1960s and early 1970s, when Indonesia relied heavily on import-substitution policies. Consequently, most groups developed business models focusing on the local market. The Soeharto era (1966–98) was one of growth, but also one of corruption and cronyism, in which ample opportunities were available inside the country for the well connected. Entrepreneurs often formed alliances with politicians to secure sector monopolies, permissions and licences (Robison 1986), and effectively organised their diversified business groups in response to the abundance of local opportunities. In so doing, these groups learned to mobilise resources for repeated entry into multiple domestic industrial and commercial projects, but they developed little

international experience. instead, these large enterprises were able to convert their economic power into political power influencing policy and entrenching both market and political power ( )

Refernce is Morck, R., Wolfenzon, D., & Yeung, B. 2005. Corporate governance, economic entrenchment, and growth Journal of Economic Literature, 43: 655-720.

In subsequent decades the ASEAN economies grew rapidly, and business groups were seemingly well positioned to expand beyond their domestic strongholds (McVey 1992). However, global capital flows created incentives to remain domestically focused. Established business groups mediated, and benefited from, the entry of foreign firms into the region (Yoshihara 1988), and served as a major conduit for a flood of portfolio investment during the 'emerging economy fever' of the early 1990s. These continuities illustrate the way dominant organisational forms and the institutional arrangements that engender them evolve along path-dependent trajectories. After working so well for so long, the strategies became 'locked in', creating an administrative heritage (Carney and Gedajlovic 2003) that may have left all but the largest groups ill equipped to engage in internationalisation. Management structures that were efficiently aligned with the domestic challenges of early-stage industrialisation are now misaligned with the tasks of developing firm-specific capabilities that could fuel the firms' internationalisation. In this path-dependent explanation, very few domestically focused business groups are able to abandon their deeply rooted business practices and acquire the capabilities needed to succeed in global competition.

Policy implications

Should Indonesian governments pursue policies to accelerate or otherwise influence their ODI? While we have been unable to furnish definitive evidence in support of either a 'hidden dragons' or a 'missing dragons' hypothesis, we speculate that both concepts play some part in the explanation of Indonesian ODI patterns. First, we suspect that at least some ODI goes unreported. However, unreported ODI is unlikely to be associated with asset-seeking investments that could contribute to the development of domestic firms' competitive capabilities. Rather, we suspect that most unreported ODI represents a form of institutional escape, perhaps to avoid taxation or to shelter accumulated family wealth from the risks of political instability and expropriation. Second, apart from the very largest, we suspect that Indonesia's business groups are too small to compensate effectively for institutional voids. Because of their relatively small scale they may lack the managerial, organisational and financial resources for effective pursuit of asset-seeking international opportunities that might strengthen their competitive capabilities. The firms affiliated with smaller groups may prefer instead to avoid the risks associated with ODI, or may see the domestic environment as continuing to provide plentiful lucrative opportunities.

If business groups are too small to assemble the resources needed for asset-seeking ODI, a more active role for the state may be justified. Many of Indonesia's neighbours have adopted pro-active ODI

strategies for this purpose. For example, China initiated a ‘go global’ campaign in the 1990s as part of a comprehensive industrial strategy aimed at producing internationally competitive firms. While many Singaporean firms are engaging in ODI for efficiency-seeking purposes, Singapore’s sovereign wealth funds are engaged in ODI to secure access to strategic technologies. Malaysia too has recently become more active in promoting ODI, by offering tax exemptions on income derived from foreign earnings. It has also attempted to streamline a range of agencies involved in promoting national industrial competitiveness, and gives particular emphasis to investment in other developing countries. This may explain why Malaysia’s ODI levels are higher than those of other ASEAN countries.

A significant constraint for the development of Indonesian MNEs is a shortage of professional management and technical personnel. World Economic Forum data show that Indonesia is a middle-ranking country with respect to ‘reliance on professional management’. It is ranked 54th among 134 countries, close to China (ranked 53rd), but significantly below Malaysia (22nd) and Singapore (8th). Similarly, Indonesia ranks 43rd in the local availability of research and training services, well below Singapore (13th) and Malaysia (27th) (Schwab and Porter 2008). The development of high-quality executive and technical talent is often the product of experience and first-hand learning through exposure to international projects. For example, research on Japanese and South Korean business groups suggests that their successful international performance was aided by the systematic development of management talent that could be deployed across a range of industries (Ungson, Steers and Park 1997). Researchers observe that family-controlled business groups are sometimes reluctant to make comparable investments in human resources, and often rely upon family members for senior executive talent (Carney 1998). The existence of a corporate elite dominated by family firms, combined with an absence of opportunities for managers to learn on the job, may create a self-reinforcing dynamic in which a supply of high-quality professional management fails to materialise. Consequently, in addition to pro-active and direct ODI policies, states such as Indonesia may also wish to consider indirect policies aimed at developing skilled professional managers.

Theoretical implications

We believe that our results also have more general theoretical implications for the study of internationalisation in emerging-market firms. As our literature review showed, existing research emphasises drivers rather than inhibitors of globalisation. This is not surprising, given that UNCTAD statistics show a surge in ODI from emerging economies, and that newspapers report frequently on high-profile cases. However, these indicators alone do not necessarily suggest a general trend in a wider population. Instead, our limited study of Indonesian groups suggests that they could reflect a Pareto-type (rather than a normal) distribution, with a few ‘extreme’ cases of internationalisation and a long tail of firms focusing on the domestic market. Pareto-science is being applied to an expanding set of social

phenomena, and is thought to be more appropriate in a context of interdependent actors, complex tensions and self-organising effects. Such a setting is common in international management research (Andriani and McKelvey 2007).

The internationalisation of Indonesian groups may similarly be characterised by processes of interdependence and self-organisation. Our database contains various events in which a medium-sized group (for example, the Ciputra Group) teamed up with a larger group (such as the Salim Group) when investing abroad, because the latter was better endowed with resources and foreign contacts. The Lippo Group frequently teamed up with business groups from other emerging economies (Malaysia, China), which presumably were drawn into the partnership because of Lippo's international capabilities. In this manner, the most international groups perceive more business opportunities than other groups and become increasingly experienced and successful, so a 'positive feedback mechanism' produces an accelerated internationalisation pattern in these firms. In other words, a few first-mover firms can overcome obstacles to internationalisation and become 'extremes' (Baum and McKelvey 2006) that tend to skew aggregate statistics on ODI. If the pattern of internationalisation found among Indonesia's largest firms is representative of other emerging economies, this suggests that a promising new approach lies in re-directing research away from assumptions of normal distribution towards a focus on the differential dynamics that generate both extreme cases of emerging economy giants and a long tail of firms focused on domestic markets.

CONCLUSION

We find that very few large Indonesian business groups can be characterised as MNEs, and that most either are active only in the domestic market or display limited internationalisation. We suggest two explanations for our findings, which we call 'hidden dragons' and 'missing dragons'. The first explanation suggests that more Indonesian MNEs exist than have been identified to date, but that some go unnoticed in official statistics and in our data. The second suggests that few Indonesian MNEs have emerged because, with a very small number of exceptions, Indonesia's business groups are too small to span institutional voids and internalise market failures. Which of our explanations is the more persuasive? At present we do not know how much ODI goes undetected, and we assume that we have overlooked some ODI events. Yet our understanding of business groups accumulated from past research tells us that while our data and official statistics may not be very accurate, they do reflect a general pattern of limited internationalisation in Indonesian firms. We contend that both the small size of most Indonesian business groups and the familial structure of Indonesia's corporate sector play a role in inhibiting Indonesian ODI, with possibly worrying consequences for Indonesia's economic development.

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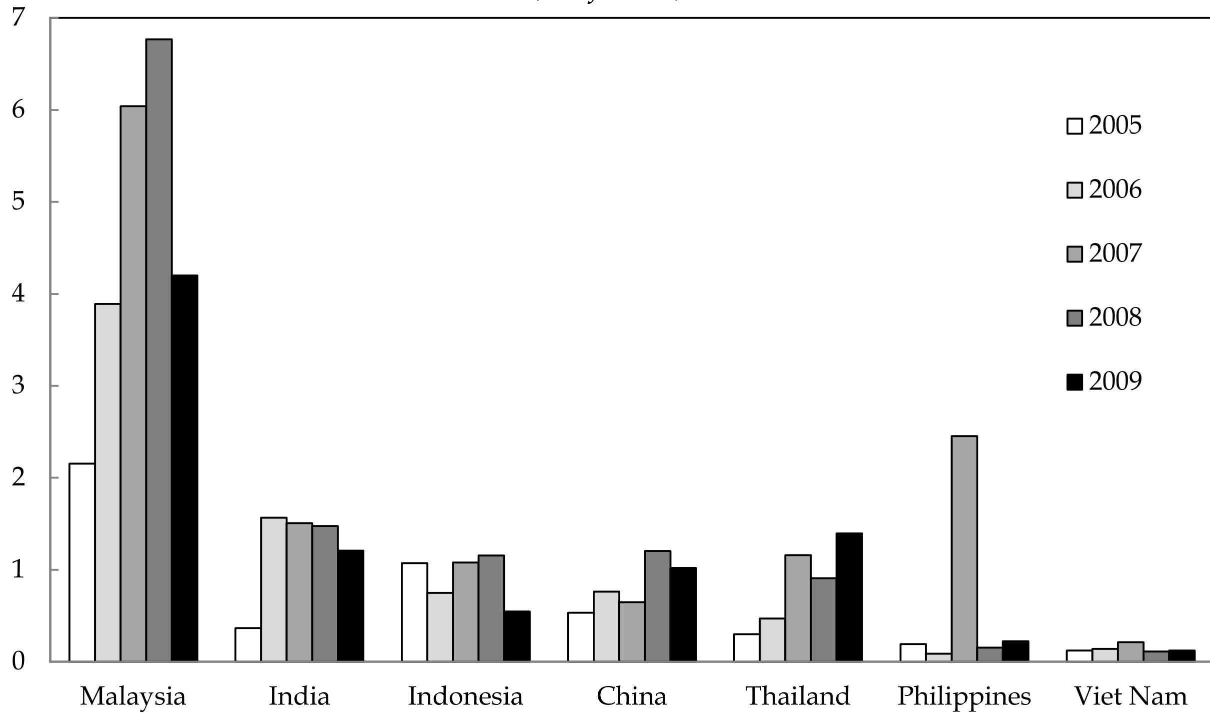
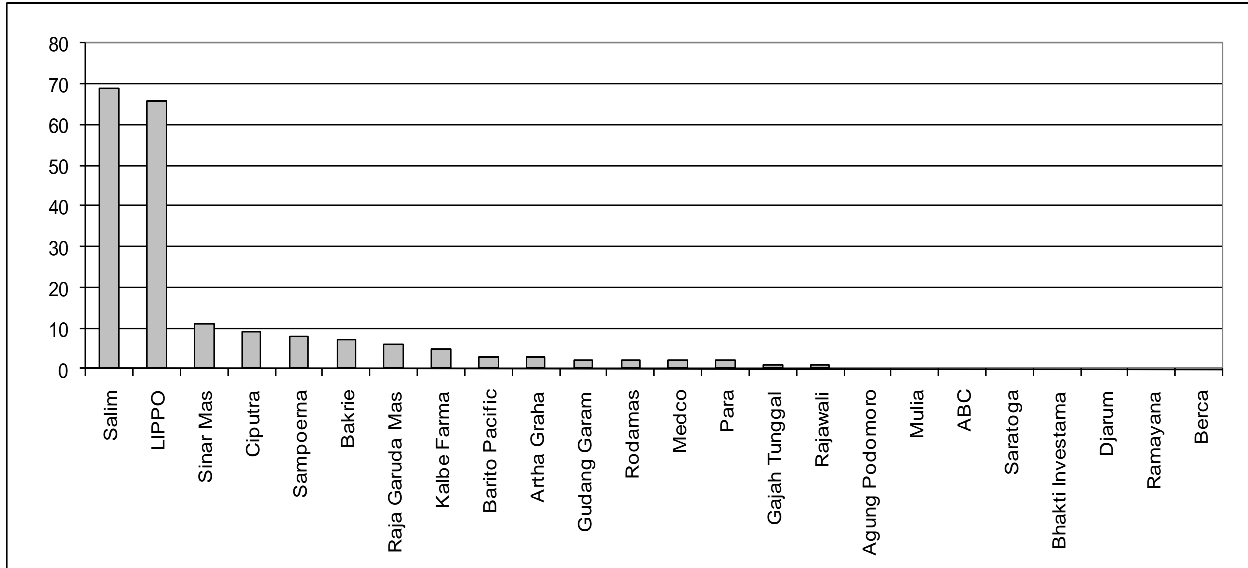
Figure 1: Outward Direct Investment, selected countries



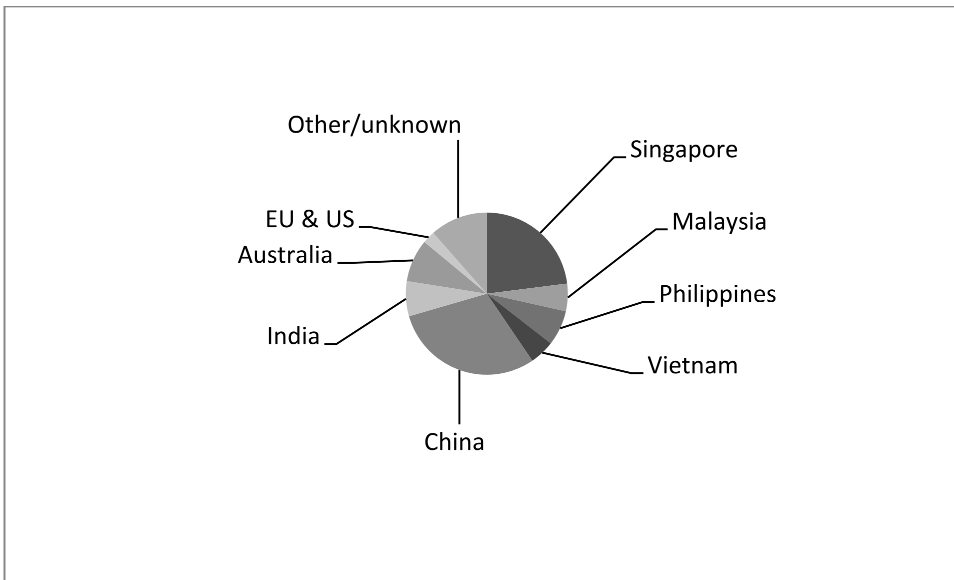
Source: UNCTAD World Investment Report 2010 available at
http://unctadstat.unctad.org/ReportFolders/reportFolders.aspx?sRF_ActivePath=P,5,27&sRF_Expanded=,P,5,27

FIGURE 2 *Number of Indonesian ODI occurrences by business group (cumulative 1994–2006)*



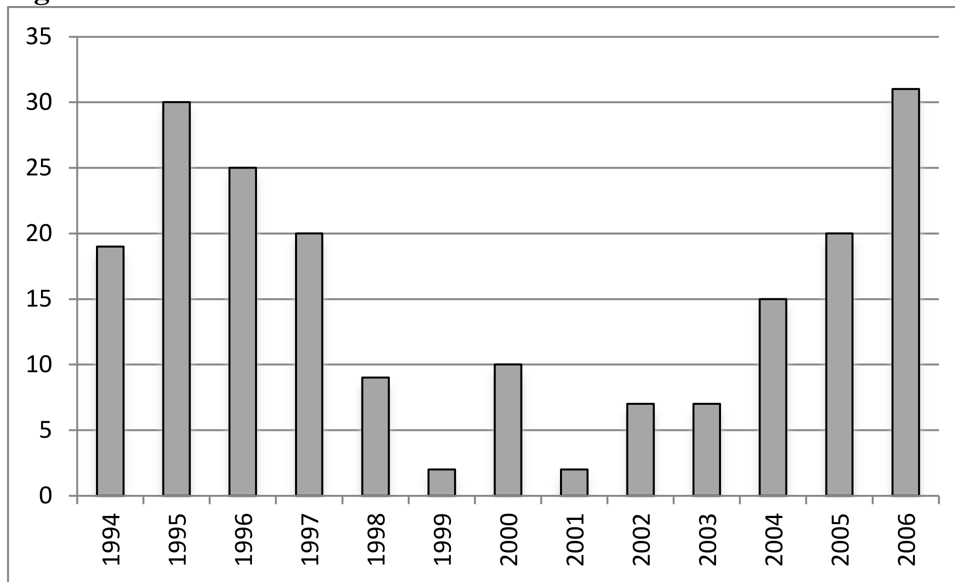
Source: authors' database

FIGURE 3 *Indonesia's ODI Destinations (cumulative 1994–2006)*



Source: authors' database

Figure 4: ODI Occurrences



Source: authors' database

TABLE 1 *Indonesia's Largest Business Groups*

Group*	Family/CEO Name	Globe				Forbes	
		People rank	Group rank	Annual turnover $ billion	Family worth $ billion	Family worth $ billion	People rank
Raja Garuda Mas	Sukanto Tanoto and family	6	11	2.00	1.30	2.80	1
Sampoerna	Putera Sampoerna and sons	5	6	3.30	2.20	2.10	2
Sinar Mas	Widjaja family	3	3	4.50	3.10	2.00	3
Gudang Garam	Wonowidjojo family	2	7	2.90	3.50	1.80	4
Djarum	Hartono family	1	5	3.50	4.20	1.40	5
Wings	Kattuari family/Sutanto family	7	14	1.40	1.10	1.00/0.22	7/25
Bakrie[a]	Bakrie family	8	8	2.80	1.05	1.20	6
Agung Podomoro	Haliman family	20	27	0.60	0.51	0.90	8
Medco[a]	Arifin Panigoro	9	22	0.81	0.90	0.82	9
Salim	Salim family	4	2	6.95	2.80	0.80	10
Lippo	Riady family	14	9	2.50	0.59	0.57	11
Rajawali	Peter Sondakh	19	25	0.72	0.51	0.53	12
Barito Pacific	Prajogo Pangestu and family	17	20	1.10	0.53	0.51	13
Ramayana[b]	Tumewu family	24	34	0.50	0.40	0.44	14
Berca[b]	Murdaya Po and family	27	na	na	0.35	0.43	16
ABC	Djojonegoro family	16	12	1.90	0.56	0.36	17
Para[a]	Chairul Tanjung and family	15	31	0.53	0.57	0.31	18
Gajah Tunggal	Sjamsul Nursalim and family	21	21	1.10	0.45	0.30	21
Saratoga Capital[b]	Edwin Soeryadjaja	18	13	1.60	0.52	0.23	23
Rodamas	Tan family	25	39	0.42	0.38	0.20	27
Ciputra	Ciputra family	30	57	0.24	0.34	0.15	30
Kalbe Farma	Benjamin Setiawan/F.B. Aryanto	11	24	0.73	0.65	0.12	34
Artha Graha	Tomy Winata (F)/Sugianto Kusuma (G)	38	70	0.18	0.28	0.11	35
Mulia	Gunawan Tjandra	37	48	0.31	0.28	0.08	40
Bhakti Investama	Harry Tanoesoedibyo	10	29	0.57	0.82	na	na

*Groups are ranked based on Forbes family worth. List excludes state-owned groups, foreign multinationals, domestic groups majority owned by foreign firms
[a] Non-ethnic Chinese ownership.
[b] Not on UBS list.
F: Forbes People Ranking; G: Globe People Ranking

Sources:

UBS list: UBS (2006). Indonesian Connections, UBS, Jakarta. (note: no ranking)
Globe groups ranking: Globe (2007) 100 Top Groups, September. (without state/foreign-owned companies)
Globe people ranking: Globe (2007) 150 richest individuals, August.
Forbes ranking: www.forbes.com; accessed December 15 2007.

TABLE 2 *Sources and Results*

Group Name	Search terms	Lexis Articles	Events in database	FDI occurrences	Type
Salim Group	Salim	129,964	210	69	Emerging Market Giant
Lippo	Lippo	14,735	153	66	Emerging Market Giant
Sinar Mas	Sinar Mas	3,730	133	11	Intermediate
Ciputra	Ciputra	2,012	37	9	Intermediate
Sampoerna	Sampoerna	8,932	47	8	Intermediate
Bakrie	Bakrie Group	1,282	88	7	Intermediate
Raja Garuda Mas	Raja Garuda Mas	196	28	6	Intermediate
Kalbe Farma	Kalbe Farma	2,111	17	5	Domestic
Artha Graha	Artha Graha	1,583	35	3	Domestic
Barito Pacific	Barito Pacific	2,049	49	3	Domestic
Gudang Garam	Gudang Garam	7,884	14	2	Domestic
Medco	Medco Group	209	23	2	Domestic
Para	Chairul Tanjung	146	13	2	Domestic
Rodamas	Rodamas	74	11	2	Domestic
Gajah Tunggal	Gajah Tunggal	1,942	15	1	Domestic
Rajawali	Rajawali	2,960	23	1	Domestic
ABC	??	1,728	3	0	Domestic
Agung Podomoro	Agung Podomoro	32	5	0	Domestic
Berca	Berca	163	20	0	Domestic
Bhakti Investama	Bhakti Investama	1,449	30	0	Domestic
Djarum	Djarum	491	4	0	Domestic
Mulia	Mulia	119	0	0	Domestic
Ramayana	Ramayana	1	0	0	Domestic
Saratoga Capital	Saratoga	291	0	0	Domestic
Wings	Wings	24,039	discarded	discarded	na
Total		**208,122**	**958**	**197**	