

Implementation Of Indonesia's Defence Economy Through The Defence Budget Sector

Ledy Seftiana¹⁾, Guntur Eko Saputro²⁾, Suwito Suwito³⁾

^{1,2,3)}Defence Economy / Defence Management, Indonesia Defence University

*Corresponding Author

Email: ledyseftiana@gmail.com

Abstract

The implementation of military spending through the Indonesian defense industry has shown gradual positive development, driven by efforts to establish an independent defense sector. This study examines the role of Indonesia's defense budget in supporting national security and fostering economic growth, focusing on the collaboration between state-owned enterprises (BUMN) and private companies (BUMS). The defense budget is applied progressively to balance the country's limited resources and the relatively low level of external threats. Using a qualitative research method, this study analyzes data from relevant literature, reports, and policies to evaluate the impact of the defense budget on the Indonesian economy. The research explores key aspects such as the gradual development of defense equipment, the role of research and development (R&D) in driving innovation, and the partnership between public and private sectors to strengthen the local defense industry. The results indicate that Indonesia's defense budget has steadily increased over the past decade, contributing to economic growth, particularly in the manufacturing and technology sectors. However, the overall impact on the economy remains mixed due to challenges such as bureaucratic inefficiencies and dependence on imported materials. The discussion highlights the potential for defense R&D investments to generate spillover effects into civilian industries and recommends strategies to enhance the efficiency of defense spending. In conclusion, the implementation of defense economic policies has laid a strong foundation for the development of an independent defense industry in Indonesia. The study suggests that a gradual increase in defense spending, combined with strategic partnerships and innovation, can support both national security and economic stability in the long term.

Keywords: Defense Economy, Defense Budget, Defense Industry, Military Spending, Economic Growth

INTRODUCTION

The role of military spending in national development, particularly through the defence industry, is an important topic for developing countries such as Indonesia. Military spending is not only related to national security, but is also an integral part of the country's economy, affecting resource allocation and overall economic performance. In the Indonesian context, the defence industry has experienced gradual development, and understanding the impact of military spending on the economy is important to ensure economic stability and national security. (Stroup & Heckelman, 2001).

Various studies have examined the relationship between military spending and economic growth. This relationship may vary depending on a country's economic structure, budgetary policies, and political stability. Some studies suggest that military spending can promote economic growth by fuelling technological advancement, creating jobs, and supporting industrial development. This view is in line with the concept of 'military Keynesianism', which states that defence spending can be an economic stimulus, especially in situations of economic recession. This theory is relevant for Indonesia, where defence spending has been utilised to boost economic activity in sectors such as manufacturing and technology (Hartley & Belin, 2020; Paul Dunne, 2013).

On the other hand, there is a view that emphasises the 'guns versus butter' dilemma, where increased military spending could potentially reduce allocations to civilian sectors such as education, health and infrastructure (Kaplinsky, 1985; Stroup & Heckelman, 2001). This is

particularly important for developing countries like Indonesia, where resources are often limited, so prioritising military spending may reduce investment in social programmes that are crucial for long-term growth (Dikici, 2015; Mintz & Huang, 1991).

Indonesia's defence budget has seen a consistent increase in recent years, driven by the government's commitment to modernising its military capabilities as well as developing an independent defence industry (Karim, 2014). However, the challenge is how to maintain a balance between this budget increase and the needs of the wider economy. Research by Eko Saputro et al. (2022) shows that while Indonesia's defence budget contributes to economic growth, particularly in the manufacturing and technology sectors, its impact on the overall economy is mixed. This is consistent with the findings of Dunne (2013), who state that in developing countries, the relationship between military spending and growth is highly dependent on context and how effectively resources are allocated (Eko Saputro & Yudho Prakoso, 2022).

One of the keys to optimising military spending is to increase domestic production capabilities in the defence sector. Through defence economic policy, the Indonesian government seeks to reduce dependence on foreign imports and encourage domestic innovation. The revision of the Defence Industry Law and partnerships between state-owned enterprises (SOEs) and private companies (BUMS) have created the foundation for a more independent defence industry (Arhan et al., 2022). By encouraging collaboration between the public and private sectors, the government not only hopes to strengthen military capabilities, but also improve economic resilience by stimulating domestic industries.

Moreover, the role of the defence industry in the economy goes beyond direct military applications. Innovations resulting from research and development (R&D) in defence can spill over into civilian sectors of the economy, increasing productivity and competitiveness in manufacturing, aerospace and telecommunications (Hartley & Belin, 2020). These potential spillover effects demonstrate the importance of investing in R&D as part of the defence budget. However, to maximise these benefits, the allocation of defence funds must be carefully managed to ensure that spending is efficient and in line with national economic objectives (Solehah et al., 2020).

This research focuses on how Indonesia can implement a defence economy through the defence budget by balancing national security needs and economic growth. The study explores how military spending can be optimised to support the defence industry as well as the wider economy, without overburdening the state budget or compromising social welfare. Building on the defence economics literature, this study will analyse the relationship between defence spending and economic growth, focusing on the Indonesian context and identify strategies for sustainable defence spending.

Given Indonesia's unique geopolitical position and economic structure, the implementation of a defence economy should be strategic and gradual. By slowly modernising the military and developing an independent defence industry, Indonesia has the opportunity to strengthen national security while boosting domestic economic growth. This research seeks to provide insights into how the government can achieve these goals through wise and efficient defence budget allocation.

RESEARCH METHODS

In this section, we will discuss the research stage or research method which is a scientific way to obtain data to use it in science, namely by scientific means of data, objectives, and uses (Sugiyono, 2013). So that the data will be observed and implemented logically. This research uses a qualitative method in which the data that has been sought will be collected and analysed

into the main procedure and will be explored with the application of the defence budget and the implementation of the defence economy to be analysed. as mentioned that qualitative research is an activity of revealing a state and object into a context where the activity aims to find meaning or a deep understanding of the problem at hand (Yusuf, 2013).

The qualitative research approach will involve collecting data from relevant literature, including reports, policies and academic studies. This data will be carefully analyzed to provide insights into the defense industry and its role in resource allocation. The primary study, which is the activity of collecting and synthesizing previous research, which can serve as a foundation to facilitate theory development and scientific advancement (Snyder, 2019). In this study, the literature review will feature three conceptualizations to examine the defense industry, defense budget, and defense economy, with the following studies:

The defence industry is a major user of scarce resources but very little is known about this industry. This industry contains a list of companies as well as all countries listed in the arms manufacturing companies contained in the SIPRI database covering both private and government companies. In this industry the activities review the National Defence expenditure with annual defence R&D and procurement data, defence equipment imports and defence equipment exports trend measures both sales and employment data collected year by year will be briefly reviewed to assess the changes of the industry activities where in the national industry is competitive, oligopolistic or national Monopoly, including long-term structural trends and competitive opportunities (Hartley & Belin, 2019).

State expenditure is an important matter for the benefit of the people of the state, so the application of the budget must be carried out quickly, effectively, efficiently, transparently and accountably. So is the application in the field of defence spending. When viewed from the defence sector, there are several defence expenditures handled by the Ministry of Defence, namely: personnel expenditure for financing military salaries and personnel goods expenditure for care and maintenance and model expenditure for modernisation or purchase of defence equipment this budget point will be allocated for various purposes related to national defence, the aim is to provide a strong military defence for a country and maintain the security of the country (Pandia et al., 2022).

From several explanations of the defence industry budget, it cannot be separated from the economic and defence references of a country. Because the science of defence economics can be a reference for the implementation of the defence industry budget to be more efficient and wise, it is necessary to apply several applications in the concept of defence economics to make the defence industry budget more efficient. Based on Adam and gold's theory of military budget expenditure, there are four applications of budget and expenditure decision making in the defence sector, namely: Close interaction or working relationship in policy between the government and the private sector; close interpretation between private and government interests where each moves freely forward or backward, interacts formally and informally, and tends to develop shared values, interests, and perceptions about future defence industry policy and design; gradual development of the defence industry over time, fostering continuous interaction between the government and the private sector where each seeks to maintain the state of the structure and framework of the defence budget as the defence budget cannot be released all at once due to the impact on the economic recession; and the tendency to protect defence industry activities externally and seek alternative policies if both the defence industry and the defence budget are threatened (Schmidt & Blackaby, 1987).

The reason for applying Schmidt & Blackaby's concept of Defence Economics implementation is because this research is a source that applies the implementation of defence economic policies to the defence industry budget that can be applied and is suitable for Indonesia,

and recent researchers, their research is not much different and leads to the research of Christian Schmidt & Frank Blackaby

RESULT AND DISCUSSION

This section will discuss the overall picture of the national defence industry budget. The determination of the amount of the defence budget from year to year is based on the factors of financial capability and the state economy in each national development plan.

The defence budget allocation can support the development of national defence in accordance with the national development strategic plan. This budget will be used to finance operational activities, maintenance of defence equipment and development of defence forces that are below the needs. in order to support domestic defence to overcome conflicts both externally and internally and protect islands and border areas and assist the government in dealing with the impact of natural disasters (*BUKU-PUTIH*, 2015).

Furthermore, the budget projection, which is the planning of the defence section that needs to be prioritised on building strength and improving the professionalism of soldiers with the availability of defence equipment and realised to realize preparedness and mobility. The process of importing Alutsista greatly affects the results of Indonesia's military budget. It can be seen that the defence budget experiences fluctuations but tends to rise, the need for a defence budget will continue to increase along with the quality of the threat so that budget allocations and the independence of the defence industry in developing weapons are needed with the improvement of the national economy (*BUKU-PUTIH*, 2015).

Budget Allocation Trends (2012-2022)

The analysis of SIPRI (Stockholm International Peace Research Institute) data from 2012 to 2022 indicates a steady rise in Indonesia's defense budget. In this period, military expenditure saw consistent increments, driven primarily by modernization efforts, increased regional security concerns, and a desire for Indonesia to establish a more autonomous defense industry. In 2022, the defense budget increased substantially compared to previous years, reflecting a strong commitment to modernizing Indonesia's military capabilities.

Figure 1 illustrates the year-by-year fluctuations and increases in the defense budget. While increases were consistent, they were gradual, avoiding large, abrupt allocations that could destabilize other areas of the national budget. This approach also reflects Indonesia's strategy of maintaining minimal reliance on foreign military suppliers while developing indigenous capabilities through BUMN and BUMS partnerships.

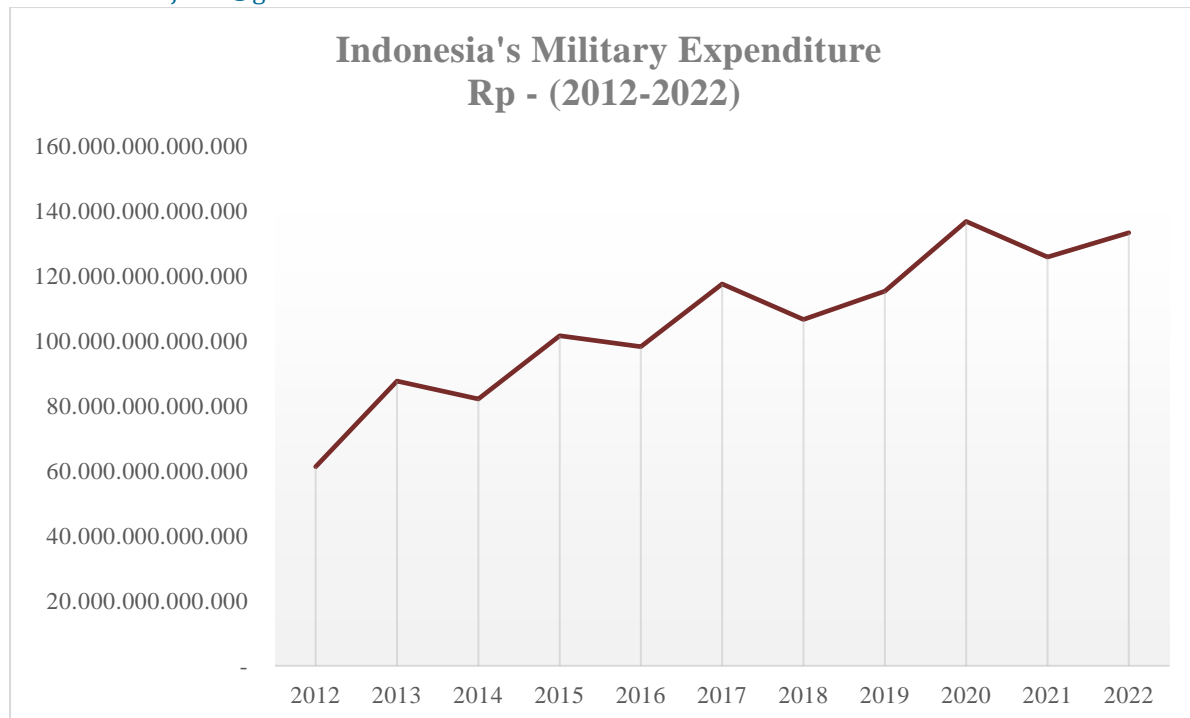


Figure 1. Indonesia's Defence Expenditure Budget

Source: Processed by the author using SIPRI data Indonesian Military Expenditure 2012-2022 (2023)

The government's budget implementation in the Government in increasing the defence industry expenditure budget are:

1. improving the state budget by reducing the budget deficit through increased budget discipline by gradually reducing subsidies and foreign loans, increasing fair and honest progressive tax revenues and saving spending.
2. developing fiscal policy by taking into account the principles of transparency, discipline, efficiency, fairness and effectiveness to increase state revenues and by emphasising on increasing tax revenues.
3. optimising tax revenue so that it is reviewed per GDP increasingly.
4. efforts to keep the deficit within safe limits and control the primary balance. as well as maintaining the budget deficit target with closer conditions between revenue, expenditure and debt management.
5. increase the efficiency and effectiveness of state spending through a structure that becomes more productive and efficient, which in aggregate is in line with the macroeconomic framework.
6. revenue is sought from domestic sources because it is highly influenced by external factors and reduces the independence of development financing.
7. efforts to reduce the provision of subsidies both in energy and non-energy to reduce state expenditure compared to other (Pandia et al., 2022).

The research results present an in-depth analysis of Indonesia's national defense budget, including year-to-year trends, allocation of resources, and key factors driving these changes. The defense budget allocation is influenced by various internal and external factors, including financial capability, national security requirements, and the global economic situation. The defense budget has been allocated to support the strategic plans of national defense, which include operational activities, the maintenance of military equipment, and the overall development of the defense forces.

Defense Equipment and R&D

A significant portion of the budget has been dedicated to purchasing and developing defense equipment, primarily Alutsista (main defense systems), including aircraft, naval vessels, and armored vehicles. Furthermore, investments in research and development (R&D) have focused on producing advanced military technology locally. This focus on R&D is essential not only for reducing reliance on imported defense systems but also for fostering innovation in related civilian industries such as telecommunications and aerospace (Moretti et al., 2019; Palve, 2024).

Budget Challenges and Efficiency Measures

Despite the rise in budget, there have been challenges in ensuring that these resources are allocated efficiently. Issues such as bureaucracy, procurement delays, and reliance on foreign technology have slowed the process of defense modernization. However, Indonesia has begun implementing policies to overcome these inefficiencies, such as streamlining procurement processes and enhancing collaboration between the public and private sectors. These measures, as outlined in the government's fiscal policy framework, aim to increase the efficiency and effectiveness of defense spending while ensuring that resources are used in line with national security priorities ("Alutsista Procurement Program Should Strengthen Technology for State Defense: President Jokowi ,” 2020; Ng, 2024; Surahman et al., 2024).

Discussion

Based on **Christian Schmidt & Frank Blackaby's Implementation of the Defence Economy**, similar that Indonesia could implement:

1. Increasing Independence through Defense Budget Implementation

Indonesia's strategic efforts to modernize its military through defense budget allocations are aligned with its broader goal of building an independent defense industry. The collaboration between state-owned enterprises (BUMN) and private entities (BUMS) in the production of medium tanks and other equipment is a notable achievement. This partnership strengthens the defense sector's ability to meet local needs while promoting healthy competition that drives innovation (Arhan et al., 2022).

Furthermore, the steady budget increases reflect Indonesia's gradual approach to avoiding a sudden economic burden. This incremental rise ensures that the state's fiscal capacity is not overwhelmed, avoiding situations where critical social sectors such as education and healthcare would need to be sacrificed. The collaboration between BUMN and BUMS has also contributed to the economic impact of the defense budget, with domestic companies benefiting from defense contracts, thus stimulating growth in the industrial sector.

2. Defense Spending and Economic Growth: Mixed Outcomes

While there is evidence of the defense budget contributing to economic growth, particularly in the manufacturing and technology sectors (Eko Saputro & Yudho Prakoso, 2022), the overall impact on Indonesia's economy remains complex. The defense industry continues to face challenges such as limited economies of scale and high dependency on imported raw materials for manufacturing advanced systems. These factors reduce the potential multiplier effect of defense spending on the broader economy. This finding aligns with Dunne (2013), who argue that the relationship between military spending and growth is highly dependent on the context, including a country's economic structure and the efficiency of resource allocation (Paul Dunne, 2013).

In this context, the need for Indonesia to develop local supply chains and enhance the capacity of domestic industries to meet defense needs is clear. As more funds are directed toward indigenous defense production, it is expected that the positive spillover effects on the economy will increase. These include not only job creation in defense manufacturing

but also technological advancements that could be applied to civilian industries such as transportation and communication.

3. Spillover Effects from Defense R&D to Civilian Sectors

The role of defense R&D in generating spillover benefits to civilian industries is crucial. Investments in military research have led to technological innovations that can be applied beyond defense, particularly in industries such as aerospace and telecommunications (Hartley & Belin, 2020). In Indonesia, there are early signs that defense R&D investments have stimulated broader technological advancements, with defense innovations being adapted for use in the civilian sector. However, more investment and focus are needed in this area to fully realize the potential of these spillover effects.

4. External Factors and National Security Strategy

Indonesia's geopolitical position in Southeast Asia necessitates a robust defense strategy, particularly given the growing security concerns in the region. The defense budget reflects the country's need to protect its territorial integrity, secure maritime borders, and respond to external threats. The consistent rise in defense spending has also been influenced by regional arms races and the need to counterbalance the military capabilities of neighboring countries. As noted in the "guns versus butter" trade-off (Kaplinsky, 1985; Stroup & Heckelman, 2001), the challenge for Indonesia is to balance its defense needs with the broader socio-economic requirements of its population.

Policy Recommendations for Sustainable Defense Spending

Based on the research findings, several policy recommendations emerge for ensuring sustainable defense spending:

1. **Efficient Budget Allocation:** The defense budget should continue to increase gradually to avoid economic strain, with a focus on reducing bureaucratic inefficiencies in procurement and spending.
2. **Strengthening Domestic Production:** Continued investment in domestic production capabilities through partnerships between BUMN and BUMS is vital. Incentives should be provided for local industries to innovate and develop advanced defense technologies.
3. **Spillover Promotion:** Defense R&D investments should be strategically designed to maximize spillover benefits to the civilian sector, particularly in technology-heavy industries like telecommunications and aerospace.

Regional Cooperation: As regional security concerns grow, Indonesia should strengthen its defense partnerships with neighboring countries through joint exercises and technology-sharing initiatives to enhance regional stability.

CONCLUSION

The study concludes that the implementation of the defence economy in Indonesia through planned defence budget management has achieved significant progress in building a more independent and robust defence industry. Cooperation between state-owned enterprises (SOEs) and privately-owned enterprises (SOEs) plays an important role in driving innovation and increasing domestic production capacity, thereby reducing dependence on imports. The gradual increase in the defence budget has helped Indonesia's military modernisation process and had a positive impact on economic growth, especially in the manufacturing and technology sectors.

However, there are still some bottlenecks, such as inefficient bureaucracy, dependence on imported raw materials and delays in the procurement process, which limit the optimisation of defence spending to spur broader economic growth. Hence, the study stresses the importance

of improving the efficiency of defence spending, strengthening domestic supply chains and focusing on enhancing domestic production capabilities.

Overall, this study shows that sustainable growth in the defence sector can be achieved through consistent public-private collaboration, strategic investment in research and development (R&D), and effective budget management. These measures will not only strengthen national security, but also enhance economic stability and technological advancement, making Indonesia more competitive in regional defence and economic development.

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