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Regulatory Challenges and Shifting Domestic Investment Behaviour in Indonesia: A Legal and Economic Analysis Towards Golden Indonesia 2045

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Abstract: Indonesia's economic transformation toward Golden Indonesia 2045 demands a robust and sustainable investment climate supported by regulatory and institutional resilience. While foreign direct investment has expanded significantly, domestic investment behaviour remains shaped by macroeconomic and legal constraints. This study employs a normative legal and qualitative analysis, supported by doctrinal and comparative approaches. It examines primary legal sources—including Law No. 25 of 2007 on Investment and Law No. 37 of 2004 on Bankruptcy—alongside secondary literature and empirical data on domestic investment determinants. Findings reveal that domestic investor behaviour is increasingly influenced by human development, labour quality, infrastructure, and inflation stability. However, Indonesia's legal framework does not adequately support business continuity. The absence of insolvency testing and overly creditor-centric bankruptcy procedures create high investment risks. Strengthening regulatory mechanisms through insolvency reform, going concern protection, and better alignment with international best practices is essential for promoting sustainable domestic investment. Legal reforms would foster resilience, encourage long-term capital flows, and strengthen Indonesia's economic position toward 2045.

Keywords: investment behaviour, regulatory framework, insolvency, going concern, Indonesia 2045.

INTRODUCTION

In the last two decades, globalisation has significantly reconfigured the landscape of international trade and investment, compelling nations to adapt their regulatory environments to an increasingly complex global economy. Indonesia, as one of the largest emerging economies in Southeast Asia, finds itself at the intersection of domestic development goals and external economic pressures. The acceleration of foreign direct investment (FDI), accompanied by the rapid influx of global products and multinational corporate activities, has placed significant strain on local industries that often lack the financial and structural resilience to compete effectively. As such, the dynamics of Indonesia's investment climate have shifted, creating both new opportunities and substantial challenges for domestic investors.

The increasing penetration of foreign products—particularly in sectors such as food, electronics, telecommunications, and automotive—demonstrates the power of global corporations to adapt to and dominate local markets. These firms leverage advanced global marketing strategies, economies of scale, and strong capital positions, enabling them to sustain profitability despite fluctuating margins (Suharini, 2023). In contrast, many Indonesian companies operate with limited capital, outdated technology, and insufficient regulatory protection, making it difficult for them to compete on equal footing. This imbalance not only exacerbates economic disparities but also threatens the sustainability of domestic enterprises in a liberalised market environment.

Indonesia's unique political, legal, socio-cultural, geographical, and technological characteristics further complicate its investment climate. The legal system, in particular, plays a central role in either facilitating or hindering investment flows. While the enactment of Law No. 25 of 2007 on Investment was a significant step toward liberalising the investment framework, it has not adequately addressed the institutional and structural disadvantages faced by domestic investors. Article 1(3) of the law permits foreign investment to be carried out independently or in partnership with domestic capital. However, in practice, joint ventures between local and foreign investors remain rare due to the substantial financial disparities and risk aversion among domestic players (Untung, 2020).

Moreover, empirical evidence from other Asian economies such as China, South Korea, and Pakistan shows that foreign aid and investment can contribute to economic growth, particularly in lower and middle-income countries (Dowling & Hiemenz, 1982). These investments often supplement domestic savings and promote capital formation. Nonetheless, without proper legal safeguards and an equitable regulatory framework, FDI can lead to overdependence, crowding out local businesses, and exacerbating existing inequalities. Hence, the regulatory environment must be carefully calibrated to ensure that investment—both foreign and domestic—supports sustainable and inclusive development.

Indonesia is currently preparing for a pivotal moment in its national trajectory: the vision of "Golden Indonesia 2045", which marks the centennial of the country's independence. This vision positions Indonesia as a top-five global economy in terms of purchasing power parity (PPP) and among the top ten in real gross domestic product (GDP) rankings (KADIN, 2024). Achieving this ambitious goal requires a strong and competitive domestic investment base supported by legal and institutional frameworks that promote fairness, certainty, and long-term business continuity.

Central to this endeavour is the role of law in development. Indonesian legal scholar Mochtar Kusumaatmadja's theory of developmental law offers a critical lens through which to understand the transformative potential of law in guiding economic change. According to Kusumaatmadja, law must not merely function as a mechanism for maintaining order, but as an instrument of deliberate social transformation (Aulia, 2018). Thus, law becomes a tool for directing economic and institutional change in ways that are aligned with national development objectives.

Despite this normative ideal, the current Indonesian legal framework often falls short in supporting the continuity and sustainability of domestic enterprises. This shortfall is particularly evident in insolvency and bankruptcy law. Indonesia's bankruptcy regime, as it stands, tends to focus on the liquidation and distribution of assets, with limited mechanisms for business recovery or restructuring. The dominant legal culture does not yet embrace the principle of "fresh start" or business rehabilitation, which are crucial for maintaining economic dynamism and encouraging entrepreneurial risk-taking.

By contrast, the United States provides an alternative model through Chapter 11 of the Bankruptcy Code, which allows for corporate reorganisation and temporary protection from creditors while the firm restructures its obligations. This legal framework not only protects jobs and creditors' interests but also sustains economic value by enabling distressed firms to recover and continue contributing to the economy (Irianto, 2018). Indonesia's failure to integrate such mechanisms limits the capacity of domestic enterprises—especially small and medium-sized enterprises (SMEs)—to survive financial distress and undermines their long-term contributions to national development.

Given these conditions, a clear gap emerges in the academic and policy discourse on Indonesia's investment climate: there is insufficient exploration of how regulatory frameworks, particularly those related to business continuity and legal certainty, affect the sustainability of domestic investment in the face of global competition. Existing research has largely focused on macroeconomic indicators of investment or the attractiveness of Indonesia to foreign investors. Few studies examine how the legal and regulatory system can be reformed to better support local enterprises in a competitive global environment.

Furthermore, there is a critical need to investigate how domestic investor behaviour is evolving in response to global market pressures and whether current regulations provide adequate support for such adaptation. Questions regarding legal certainty, regulatory flexibility, access to financial restructuring mechanisms, and protection from arbitrary enforcement actions are particularly relevant. Without addressing these concerns, Indonesia risks entering 2045 with a structurally imbalanced economy, overly reliant on foreign capital, and lacking a resilient domestic investment class. This study seeks to fill that gap by offering a comprehensive analysis of Indonesia's investment regulatory framework in the context of global economic shifts and the national development vision of Golden Indonesia 2045. It aims to investigate the extent to which current regulations align with the needs of domestic investors and how legal reforms can foster a more equitable, competitive, and sustainable investment climate.

Two key research questions guide this inquiry: (1) How are domestic investors in Indonesia adapting their investment behaviour in response to global market challenges and increasing foreign competition? (2) To what extent does Indonesia's current regulatory framework support long-term business continuity and the development of a sustainable domestic investment climate? Answering these questions is essential for designing a legal and policy framework that not only attracts foreign capital but also empowers local enterprises. Legal reform must be guided by principles of fairness, sustainability, and inclusivity, ensuring that domestic investors are not merely participants in the market but central agents in national economic development.

Ultimately, the goal of this research is to contribute to the scholarly discourse on law and economic development in Indonesia, while offering practical recommendations for policymakers to align investment regulations with the strategic objectives of Golden Indonesia 2045. By highlighting the regulatory gaps and proposing a pathway toward reform, this study aspires to support the creation of an investment climate where domestic and foreign investors can coexist and thrive, driving inclusive and resilient economic growth.

METHOD

This study employs a qualitative normative legal research approach to examine the alignment of Indonesia's investment regulations with the objectives of sustainable domestic investment and the vision of Golden Indonesia 2045. The research focuses on the analysis of primary legal materials, including statutory laws such as Law No. 25 of 2007 on Investment, the Bankruptcy Law, and relevant government regulations, as well as secondary legal materials comprising legal commentaries, scholarly articles, and policy reports. A doctrinal method is utilised to interpret legal norms and principles, particularly those related to business continuity, regulatory certainty, and legal protection for domestic investors.

In addition, a comparative analysis is conducted by referencing legal practices from jurisdictions such as the United States and South Korea, which implement reorganisation mechanisms to support business survival. The research also integrates a conceptual approach to explore the theoretical underpinnings of developmental law as proposed by Mochtar Kusumaatmadja. Data are collected through literature review and document analysis, with a focus on regulatory conformity and legal reform. The findings aim to provide recommendations for strengthening Indonesia's legal infrastructure in support of a balanced and resilient investment climate.

RESULTS AND DISCUSSION

Changes in Domestic Investor Behaviour in Responding to the Global Market

The behaviour of domestic investors in Indonesia has evolved substantially in recent years, driven largely by the pressures of globalisation and the shifting contours of regional development. Unlike in the past, when domestic investment decisions were often based on short-term profit motives or resource-driven opportunities, contemporary domestic investors exhibit a more data-informed and strategic orientation. This transformation is particularly evident in how they evaluate regional development indicators, macroeconomic stability, and socio-institutional conditions as factors shaping their investment choices.

One of the most influential determinants of domestic investment is the Human Development Index (HDI), which reflects the combined performance of education, health, and income in a given area. Empirical data suggest that domestic investors in Indonesia are increasingly directing capital toward regions with higher HDI scores. Areas categorised as fast-growing and rapidly developing demonstrate investment probabilities that are 1.346 times higher than underdeveloped regions, while advanced but pressured regions and emerging regions record investment probabilities of 1.289 and 1.099 respectively (Prayitno & Yustie, 2020). This pattern reveals a growing preference for stability, governance, and the presence of human capital as crucial indicators of investment readiness. Investors interpret HDI as a signal of not only current economic capability but also long-term development potential.

In parallel with the focus on human development, the role of labour in influencing investment decisions has also undergone a fundamental shift. It is no longer merely the quantity of available workers that matters; rather, the quality, skills, and productivity of labour have become critical considerations. The increasing integration of Indonesia into global value chains and the rise of technology-based sectors require a labour force that is educated, adaptable, and equipped with both digital and technical skills. Labour, therefore, is no longer viewed as a cost factor alone but as a driver of competitive advantage. The quality of human resources, especially in urban and semi-urban centres, has become a strong pull factor for domestic capital, especially among firms seeking long-term operational efficiency and sustainable returns.

Infrastructure also plays a decisive role in this transformation of investment behaviour. Investors are now highly sensitive to the quality of logistical and digital infrastructure in the regions they consider. Roads, transport networks, internet connectivity, and electricity availability are treated as indicators of operational feasibility. Infrastructure not only reduces transaction costs but also provides confidence that public policy supports long-term regional development. Hutauruk (2021) asserts that infrastructure access is often a deal-maker or deal-breaker in investment decisions, particularly for domestic investors who typically operate with tighter margins than their foreign counterparts.

Macroeconomic stability, particularly in terms of inflation management, adds another layer of complexity to investor behaviour. Domestic investors are acutely responsive to inflation trends. While moderate inflation (below 10%) can stimulate growth and encourage expansion, excessive inflation undermines planning, erodes real returns, and signals policy instability. Simanungkalit (2020) argues that moderate inflation is even welcomed by some domestic investors, as it encourages production and business expansion due to the prospect of rising profits. However, once inflation crosses into double digits, it reduces consumer purchasing power and deters new investment, particularly in sectors like retail, food production, and construction.

Collectively, these four factors—HDI, labour quality, infrastructure, and inflation—have fundamentally reshaped how domestic investors in Indonesia assess risks and opportunities. There is a discernible shift from speculative, short-term investing to behaviour characterised by due diligence, long-term outlooks, and alignment with development indicators. This evolution is an encouraging sign of maturity in Indonesia's domestic investment ecosystem. However, it also reveals critical dependencies on the state's ability to sustain human development, improve infrastructure, and maintain macroeconomic stability. If left unaddressed, regional disparities and policy inconsistency could stifle this positive transformation.

Regulatory Standards for Business Continuity in Supporting Sustainable Domestic Investment

As Indonesia positions itself toward achieving the national vision of Golden Indonesia 2045, the sustainability of its domestic investment climate is increasingly tied to the presence of supportive regulatory structures. One critical element of this investment ecosystem is the principle of going concern, which denotes the ability of a business to continue its operations without the immediate threat of liquidation. This principle is not merely an accounting assumption but a foundational economic expectation that affects investor sentiment, credit allocation, and capital formation.

In theory, a legal environment that recognises and protects the going concern status of businesses contributes significantly to investor confidence. When businesses operate in a regulatory setting that offers legal recourse, restructuring opportunities, and protection against predatory creditor behaviour, investors are more likely to commit resources with a long-term perspective. In Indonesia, however, the current legal and regulatory framework does not sufficiently embody this principle. The primary legislation governing insolvency, namely Law No. 37 of 2004, remains largely liquidation-oriented. Rather than facilitating business recovery, it often enables creditors to seek bankruptcy declarations even when a business retains the capacity for financial recovery.

According to Laili and Canggih (2021), this legal framework presents a high-risk environment for businesses that rely on credit, particularly SMEs and start-ups. The ease with which bankruptcy petitions can be filed—and approved—without thorough financial evaluation creates systemic vulnerabilities. Many viable businesses face premature closure not due to insolvency in the substantive sense but due to procedural technicalities and creditor pressures. The law does not adequately consider whether a debtor is genuinely unable to fulfil obligations or merely facing temporary liquidity issues.

This regulatory gap is exacerbated by the absence of an insolvency test in the Indonesian legal context. In more advanced jurisdictions, such as the United States, courts apply a series of financial assessments to determine whether a firm is insolvent. These include the balance sheet test, cash flow test, and transactional analysis. The absence of similar mechanisms in Indonesia means that legal decisions often rely on narrow and sometimes misleading interpretations of solvency. As a result, businesses that could recover with restructuring are pushed into liquidation, eliminating jobs, destroying capital, and sending adverse signals to investors.

Moreover, the principle of business continuity is undermined by the law's failure to differentiate between temporary financial distress and structural insolvency. This blurring of categories creates a chilling effect on entrepreneurial risk-taking. Investors become cautious not just about market risks but about the potential legal consequences of temporary downturns. Consequently, a regulatory environment that should ideally support resilience ends up encouraging premature exit.

The implications for Indonesia's investment climate are significant. Regulatory support for going concern status is a key determinant of whether businesses are viewed as stable and creditworthy. Without such legal assurances, domestic investors are less likely to inject capital into long-term projects, and external investors may question the institutional quality of Indonesia's financial ecosystem. The net effect is a suboptimal investment climate marked by short-termism and risk aversion.

It is therefore essential that Indonesia's legal framework be recalibrated to reflect the realities of business life cycles. Legal protection for business continuity does not mean shielding failing businesses indefinitely, but rather ensuring that potentially viable firms are not arbitrarily dissolved. Implementing reforms that include structured insolvency tests, mandatory reorganisation periods, and clearer definitions of financial distress will go a long way in fostering a healthy, sustainable investment environment.

Legal Framework Weaknesses in Bankruptcy and the Absence of Insolvency Tests

The Indonesian bankruptcy system, while well-intentioned in its aim to regulate financial failure, is critically flawed due to its structural bias toward liquidation and its failure to incorporate objective insolvency testing. These weaknesses not only affect the firms involved but have broader consequences for the domestic investment climate, especially as Indonesia aspires to transition into a high-income economy by 2045.

One of the most striking deficiencies of Law No. 37 of 2004 is the lack of codified financial tests to determine insolvency. Unlike jurisdictions such as the United States and United Kingdom, which utilise detailed frameworks including the balance sheet test, the cash flow test, and transactional risk analysis, Indonesian law does not mandate such assessments before declaring a company bankrupt (Mait et al., 2023). As a result, the process is vulnerable to abuse. Creditors can initiate bankruptcy proceedings against solvent firms based merely on payment delays, regardless of the firm's broader financial condition.

This legal gap presents a distorted picture of financial distress. The balance sheet test, commonly used in other systems, examines whether a firm's liabilities exceed its assets, providing a snapshot of overall solvency. The cash flow test looks at whether the firm can meet obligations as they fall due. Without applying these lenses, courts risk declaring firms insolvent based on incomplete or short-term data. The result is the unnecessary destruction of economic value and investor confidence.

In addition, the transactional analysis, which assesses whether a firm has made irrational financial decisions that undermine its capital structure, is also absent from Indonesian legal procedures. This omission means that systemic financial mismanagement may go unchecked, while temporary liquidity issues are treated as grounds for liquidation. Such asymmetries in legal reasoning exacerbate market instability and increase the perceived risk of doing business.

Moreover, the legal culture surrounding bankruptcy in Indonesia often lacks nuance. Rather than viewing bankruptcy as a rehabilitative tool—as is common in more investor-friendly jurisdictions—it is frequently perceived as punitive. This perception discourages innovation and entrepreneurship, especially in sectors where business cycles are volatile. Start-ups and new ventures, which are vital to Indonesia's future economy, are most at risk under such a system.

If Indonesia intends to create a resilient and inclusive investment environment, legal reform is indispensable. Introducing insolvency tests would allow courts to distinguish between firms that are structurally unsound and those that can recover. Reforming the law to include reorganisation pathways, much like Chapter 11 of the U.S. Bankruptcy Code, would enable firms to restructure, protect jobs, and maintain investor confidence (Peterman & Morissette, 2004). Such reforms would also align Indonesia's legal framework with international standards and signal a serious commitment to improving its investment climate.

The integration of objective financial criteria and the adoption of principles such as "commercial exit from financial distress" would mark a transformative shift in Indonesia's legal system. By doing so, Indonesia could better protect domestic capital, encourage responsible risk-taking, and ultimately enhance the sustainability of its economic development.

CONCLUSION

The findings of this study highlight a significant gap between evolving domestic investment behaviour and Indonesia's current legal framework. Domestic investors are becoming more strategic and data-driven, prioritising regions with higher human development indicators, skilled labour, adequate infrastructure, and stable inflation. However, this behavioural shift is not adequately supported by the legal system. Law No. 37 of 2004 remains heavily liquidation-oriented, lacks structured insolvency testing, and undermines the principle of going concern. These weaknesses increase uncertainty and discourage long-term domestic investment, especially for SMEs and start-ups.

A regulatory transformation is therefore necessary. Introducing insolvency tests, formalising restructuring mechanisms, and ensuring legal protection for viable businesses would align Indonesia's regulatory system with international best practices. Such reforms are vital to achieve the economic vision of Golden Indonesia 2045. This study has certain limitations. It relies primarily on legal and secondary economic data, without incorporating primary field research or econometric modelling. Future studies should expand to empirical analyses involving investor perceptions, financial performance data, and comparative jurisdictional outcomes to provide a more granular policy framework.

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