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This report is part of the Bertelsmann Stiftung’s Transformation Index (BTI) 2016. It covers the period from 1 February 2013 to 31 January 2015. The BTI assesses the transformation toward democracy and a market economy as well as the quality of political management in 129 countries. More on the BTI at [http://www.bti-project.org](http://www.bti-project.org).


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Executive Summary

During the period under review, Indonesia’s democracy underwent a serious populist challenge. During the campaign to the run-up of the 2014 presidential elections, Prabowo Subianto – the former son-in-law of ex-dictator Suharto – proposed to reintroduce Indonesia’s pre-democratic constitution. A success of his would have annulled all major democratic reforms achieved since 1998, and arguably led to some form of neo-authoritarian regime under Prabowo’s leadership. Ultimately, Prabowo lost the election to Joko Widodo, the pragmatic governor of Jakarta. The fact that an openly anti-democratic presidential nominee should gather 47% of the votes however highlighted the vulnerability of Indonesian democracy. Moreover, Joko Widodo paid a high price for his victory – he had to form alliances with a number of oligarchs, retired military figures and party patrons who demanded – and received – rewards after Widodo’s inauguration in October 2014. As a result, Widodo’s ability to pursue the reforms he promised during the campaign has been severely constrained.

The 2014 elections also witnessed three other negative trends: first, the legislative elections in April saw the highest-ever levels of vote-buying in Indonesian history; second, the country’s television stations were remarkably biased during the presidential campaign, exclusively promoting the candidate championed by their various tycoon owners; and third, the presidential ballot was marked by an unprecedented extent of slander and belligerent rhetoric.

Nevertheless, the overall parameters of Indonesian democracy continue to be relatively sound. The competitiveness of elections remains high, as do voter turnout and the wider population’s declared support for democracy - somewhat ironically, even the majority of Prabowo’s voters did so. After a highly divisive 2014 election campaign, the levels of political conflict returned to the stability Indonesia has become used to since the mid-2000s. Similarly, there has been no outbreak of large-scale ethnic, religious or other grassroots violence. Given that more than 10,000 people were killed during communal clashes in the transitional period between 1998 and 2003, the absence of any comparable conflict should not be taken for granted. Moreover, the Indonesian state has continued
to strengthen its hold over remote territories, establishing more local government structures and institutions in regions previously untouched by the state apparatus. Finally, while human rights abuse persists, it is now mostly of a nonpolitical nature, with the exception of violations in the province of Papua, where the state continues to fight a poorly organized separatist movement.

Indonesia’s economy showed signs of increasing volatility between 2013 and 2015. The end of the global commodity boom has hit the country hard, and in late 2014 GDP growth fell below 5% for the first time since 2009. The current account deficit has increased significantly, and the local currency, the Rupiah, depreciated by 25% between early 2013 and early 2015. Inequality has also reached record levels. In addition, the government – and the elite in general – strengthened their protectionist posture. In a series of policy decisions heavily criticized by foreign investors, the government issued regulations that imposed new import and export taxes, limited economic freedoms, and strengthened the role of the state in key areas of the economy. On the positive side, unemployment and poverty continued to decline, although almost half of the population still live on less than $2 a day. Overall, Indonesian democracy has become more volatile in the period between 2013 and 2015, and the economy struggles to adjust to the end of the natural resource boom.

History and Characteristics of Transformation

Indonesia’s democratic transition began in May 1998, when longtime autocrat Suharto resigned from the presidency after 32 years in office. Supported by the military, the bureaucracy and his Golkar party electoral machine, Suharto had ruled the archipelago with an iron fist after bloodily putting down a communist coup attempt in October 1965. For much of his tenure, Suharto governed with a mixture of repression, patronage and performance legitimacy – the latter drawing on the high levels of economic growth under his watch. But the Asian financial crisis of 1997 – 1998 led to the collapse of the Indonesian economy, destroying Suharto’s power base and sending poor Indonesians to the streets. As a result, cracks in the regime emerged, which in turn emboldened street protests and encouraged Western capitals to reconsider their support for their former anti-communist ally. When the armed forces deserted him as well, Suharto had no other option but to resign.

While Suharto’s resignation occurred amid significant mass mobilization, the regime change itself took place as a pact-based transition. Opposition forces allowed Suharto’s vice president, the hugely unpopular B.J. Habibie, to take power in exchange for assurances of substantial political reform. Indeed, Habibie’s reforms – most of which he began implementing only a week after Suharto’s fall – far exceeded the opposition’s expectations: He scheduled free and fair elections, lifted restrictions on the press, released political prisoners and even launched a decentralization process that turned the heavily centralized state into one of the most decentralized polities of the developing world. The June 1999 parliamentary elections were globally praised as free, fair and competitive, and Habibie handed over power to his successor Abdurrahman Wahid in October.
1999. However, Wahid was elected by the partially appointed People’s Consultative Assembly, tainting the democratic quality of Indonesia’s first non-autocratic power transfer and making political conflict unavoidable. Backed only by a small faction in the legislature, Wahid was soon locked in a hostile conflict with all other political forces. Following his attempt to dissolve parliament in an unconstitutional manner in July 2001, the legislature impeached him. He was replaced by Vice President Megawati Sukarnoputri, who governed between 2001 and 2004.

While Megawati’s presidency has often been described as visionless, it was during her term that the most important reforms of the post-1999 era were launched. Direct presidential elections were introduced; a Constitutional Court was established; an Anti-Corruption Commission was founded; and direct local elections for governors, mayors and district chiefs were enshrined in the decentralization laws. When these reforms became fully operational in 2004 and 2005, Indonesia finally completed its democratic transition and moved into an early phase of democratic consolidation. The main beneficiary of this trend was Susilo Bambang Yudhoyono, who won the first direct presidential elections in 2004 and was re-elected in 2009. While he further stabilized the polity, he was often accused of inactivity. At the end of Yudhoyono’s term, two populist challengers emerged who competed for his succession: the ultranationalist Prabowo Subianto, Suharto’s former son-in-law, who proposed a return to stronger centralist government and moderation of some of the democratic reforms achieved since 1998; and Joko Widodo (“Jokowi”), the pragmatic governor of Jakarta, who stood for the continuation of the democratic status quo while promising improvements to public service delivery. Jokowi eventually won the elections in July 2014. It remains to be seen whether Jokowi will be able to lead a more effective government than Yudhoyono did, but early indications are that he is regularly forced to make compromises with established elites in order to fend off challenges to his rule.
The BTI combines text analysis and numerical assessments. The score for each question is provided below its respective title. The scale ranges from 1 (worst) to 10 (best).

Transformation Status

I. Political Transformation

1 | Stateness

The Indonesian state’s monopoly on the use of force is generally accepted. Decentralization dynamics have increased the number of districts, sub-districts and villages significantly, leading to the highest level of state penetration in remote areas since the country’s independence. In the province of Aceh, where separatist rebels challenged the state’s authority between the 1970s and mid-2000s, a 2005 peace agreement is in place. Papuan guerilla fighters continue to fight the Indonesian state, but their forces are relatively few and do not exercise any effective territorial control. In most Indonesian provinces and districts, there are ethnic or religious groups (such as the Betawi Brotherhood Forum or the Islamic Defenders Front) that lay claim to some law enforcement functions. However, they often do so in cooperation with the police, who view them as fulfilling a useful political purpose. Wherever terrorist Islamist groups have tried to gain or re-gain a foothold in a particular locality (as in the district of Poso in South Sulawesi in 2014), the Indonesian state immediately suppresses insurgencies. As a result, terrorist Islamist groups have increasingly targeted police officers in their attacks.

The vast majority of Indonesians have a strong sense of nationalism and enthusiastically support the nation-state as the final and exclusive form of state organization. The only exceptions are Papua, where many citizens demand their own state, and a number of marginal Islamist groups, which advocate for a Muslim caliphate in Southeast Asia and beyond. In late 2014, the Islamic State in Iraq and the Levante (IS) attracted some support in Indonesia, but its influence remains limited. Similarly, while decentralization has led to the revival of local identities, languages, customs and local strongmen, this pattern has not undermined the strength of national identity. Rather, it has strengthened it. Unlike the authoritarian regime, the current democratic regime does not deny any particular groups access to citizenship. From the founding of the nation in the 1940s until the early phase of democratic transition in the late 1990s, ethnic Chinese had found it difficult to gain citizenship. In the last
decade, however, Indonesia has made remarkable progress in this regard, reducing discrimination against ethnic Chinese people and opening up opportunities for them in terms of cultural, political and social participation.

As a state with around 87% Muslim inhabitants, Indonesia has traditionally struggled to maintain a balance between promoting Islamic values and the rights of non-Muslim minorities. While the Indonesian constitution guarantees the freedom of religion, this right has not been consistently upheld in recent years. Under President Yudhoyono, orthodox Islamic views had a strong influence on political attitudes and law enforcement practices. Yudhoyono refused to take tough action against Islamist groups that attacked non-Muslim constituencies and Muslim sects viewed by the Islamic mainstream as heretic (such as the Ahmadis and the Shi’ites). The Jokowi government, by contrast, has promised to provide better protection for these minorities. For example, The Minister of Home Affairs announced that the administration plans to no longer force Indonesians to state their religion in their identity cards, if they belong to a minority group. In Aceh province, however, Shari’ah law has been enforced with increasing strictness, even against foreigners. On 1 January 2015, a group of foreigners celebrating New Year on a beach in Aceh were attacked by civilians claiming to uphold Shari’ah law. Similarly, other districts and provinces have issued bylaws that enforce Islamic dress codes or require civil servants to be able to recite the Quran. These bylaws threaten women’s rights and the ability of religious minorities to practice their faith, and the acquisition of licenses for non-Muslim places of worship continues to be difficult.

The Indonesian state has a functioning administration that reaches into all levels of state organization. Indeed, the expansion of the state apparatus that accompanied the post-decentralization explosion in the number of districts, sub-districts and villages has vastly increased the reach of the Indonesian bureaucracy. However, the quality of the public services delivered by the administration is often low. About 41% of Indonesians still lack access to sanitation and clean water. The health and education systems are poor, with Indonesia spending less in these two sectors than most of its regional competitors (3.0% on health and 3.6% on education, compared to Thailand’s 7.9% and 3.9% respectively). On the other hand, democratic elections have forced local incumbents to improve infrastructure, health, and education services. Many now introduce the development of traffic infrastructure and free schooling and health care programs; this has led to a qualitative improvement in such services in some – but by no means all – areas.

2 | Political Participation

Every five years, Indonesians go the polls to elect the president, members of the House of Representatives and Regional Representative Council, and members of provincial and district-level parliaments. They also vote for governors, mayors, and
district and village heads. The direct ballots for president, governors, mayors and district heads include the possibility of run-offs. Most Indonesians, as well as outside observers, believe that these elections are generally free, fair and competitive. However, the 2014 elections have seen trends that warrant an overall downgrading of such an estimation. First, the legislative elections saw an unprecedented level of vote-buying, including payments to local electoral commissions to mark-up the results of individual candidates (Indonesia uses an open party list system). Second, the presidential election experienced a growing number of black campaigning from both candidates, especially on the social media. Third, the media was politically biased to an extent never seen before. Almost every TV station delivered around-the-clock propaganda for the nominee the media tycoon owner of the station would favor. While the presidential elections also recorded positive trends (such as a successful social media project to monitor the vote count and high levels of public satisfaction with the electoral process), increased corruption and media bias have had a significant impact on the general quality of elections.

While democratically elected politicians can generally govern without outside intervention, some veto powers continue to interfere in policymaking processes. The military, however, is no longer the most important veto power. Rather, oligarchs and business groups exert the greatest pressure on parties and politicians today, both with respect to the executive and the legislature. This was particularly visible in the 2014 elections, when a number of oligarchs either tried to run for presidency themselves, or sponsored candidates to represent their interests. Given the absence of a functioning party and campaign financing system, many politicians have become highly dependent on such oligarchic sponsors. In return, they pass regulations or approve projects that benefit their donors. In 2013 and 2014, large-scale corruption scandals involving senior party leaders (one sitting party chairman was imprisoned, another indicted) revealed the extent of this collusion with oligarchic interests. Partly because of this special-interest meddling, the legislative branch has been unable to implement its legislative and budgeting functions properly. The veto power held by oligarchs has also been visible in the first few months of the Joko Widodo administration, with many cabinet appointments and policy decisions made under the pressure of selected magnates who supported Widodo in his 2014 campaign.

In most parts of the archipelago, the freedom of association and assembly is upheld. Indeed, Indonesia now has one of the most vibrant civil societies in Asia, with labor unions, grassroots advocacy groups, women’s rights associations and other bodies mushrooming and making their voices heard. Demonstrations in front of government buildings are a common sight and are usually not restricted by the police. However, this freedom still does not extend to groups that promote separatism, radical leftist ideologies or nonmainstream religious views. Supporters of Papuan independence are not allowed to organize freely, and some have been sentenced to long prison terms because they participated in peaceful flag-raising ceremonies. In many cases,
however, it is not the state, but other societal groups that restrict the freedom of assembly of their fellow citizens. For instance, violent mobs have often dispersed meetings of religious minorities or sects, with the state failing to offer protection. In December 2014, a group of thugs also stopped a meeting of activists in the cities of Yogyakarta, Malang, Surakarta, Semarang, Surabaya, and Manado, where a film critical of Indonesia’s handling of the 1965 massacres was supposed to be screened.

Developments in the area of the freedom of expression were mixed between 2013 and 2015. On the one hand, Indonesia continues to have one of the most pluralist and diverse press in the region (despite its overall oligarchic ownership structure). Media reports on government policy and other key issues are often highly critical. On the other hand, the level of violence against journalists has increased in recent years, with several journalists killed or kidnapped. One controversial case surrounded accusations of blasphemy to the Jakarta Post editor-in-chief for printing a cartoon which mocked the IS (Islamic State) terror group. As a result, Indonesia was ranked 132th out of 180 countries in the Reporters Without Borders’ Press Freedom Index in 2014. While this is an improvement over 2012 and 2013, it still places Indonesia among countries such as Oman and Zimbabwe. Furthermore, the government has limited public access to the Internet. By the end of 2014, it had blocked more than one million websites – mostly pornographic sites, but also the video and image-sharing fora Vimeo, Reddit and Imgur. The new Jokowi administration has announced that it will maintain this restrictive policy introduced under Yudhoyono. Furthermore, freedom of expression has been increasingly limited for members of nonmainstream religious groups, who fear social and legal sanctions if they publicly speak about their faith.

3 | Rule of Law

Following wide-ranging political reforms implemented after Suharto’s fall, Indonesia now has a very effective system of checks and balances. Minor concerns emerged during the review period following corruption charges against supreme judges at the constitution court, though these did not result in undermining the system of checks and balance. While officially a presidential system, the Indonesian polity features a legislature with extensive budgetary, oversight and appointment powers. Indeed, the government cannot engage in any major policy initiative without the parliament’s explicit approval. The election of President Joko Widodo, who shortly after his inauguration in October 2014 did not hold a majority in parliamentary support, is likely to deepen this pattern. Meanwhile, the judiciary has developed into a politically independent branch of state organization, a stark contrast to the authoritarian era when judges openly served the political interests of the incumbent regime.
While the judiciary is now largely autonomous from political influences, it is by no means independent of corruption and its perpetrators. Bribes can influence judicial procedures at all levels, from police investigations to indictments by the Attorney General’s Office to court verdicts and appeals. The Anti-Corruption Commission arrested several judges in 2013 and 2014, including a judge at Bandung’s Anti-Corruption court in August 2014. As a result of its corrupt nature, the judiciary has been unable to develop a differentiated and professional organization, despite the existence of a large network of formal institutions and channels. Indonesia’s score in the area of judicial independence warrants a downgrade in the period under review because the Constitutional Court – previously the only legal body thought to be immune to corruption – has too experienced a major corruption scandal. Its chairman was arrested in October 2013 and later sentenced to life in prison after he received money from local politicians for declaring them winners in electoral disputes. With this, he jeopardized not only the credibility of the judiciary, but of the electoral process as well. While the Constitutional Court has since then tried to rehabilitate itself and issued a number of well-received verdicts (such as the rejection of Prabowo Subianto’s challenge of the 2014 election results), the stain on its reputation is likely to remain for some time.

Corruption and abuse of power remain endemic in Indonesia. However, in contrast to the early post-Suharto period, many officeholders are now prosecuted for their actions. Between 2004 and early 2013, a total of 2,976 members of local parliaments have been investigated for abuses ranging from corruption (40% of cases), physical and sexual harassment, document forgery and fraud. By November 2013, 309 local government heads had been subject to legal investigations. Many of these prosecutions have resulted in prison terms for the accused, especially in those cases handled by special corruption courts in the capital Jakarta. Most successfully prosecuted cases against officials were initiated by the highly popular Anti-Corruption Commission, which has indicted a host of politicians and businesspeople in the highest echelons of power. In addition to pushing for tough prison terms, the Commission has also increasingly asked courts to seize possessions of convicts. A party chairman was not only sentenced to 16 years in prison in December 2013, but also had significant possessions confiscated. Such successes have encouraged some political elites to propose reforms that would curtail the powers of the Commission. So far, these attempts have been unsuccessful, but anti-corruption activists have expressed concern that President Widodo could be forced by his allies to support initiatives that would weaken the Commission.

Protection of civil rights remained volatile between 2013 and 2015. Most importantly, civil rights in Papua continue to be under assault, with the police and military taking harsh measures against peaceful pro-independence activists and ordinary citizens suspected of assisting them. On 8 December 2014, at least four protesters were killed and over a dozen injured when police and military forces
allegedly fired on protesters at the Paniai District Military Command. The crowd had protested against soldiers who had reportedly beaten a child the night before. Papuans were particularly disappointed because newly inaugurated President Joko Widodo did not immediately condemn the incident. Similarly, the civil rights of nonmainstream religious group followers remain weakly protected. Ahmadis, Shi’ites and other groups viewed by the Muslim mainstream as heretic cannot count on the state to guarantee their basic rights as citizens. An Ahmadiyah mosque and several houses were attacked in West Java in April and May 2013. In some areas, Ahmadis have been living in refugee camps for 9 years, and are still waiting to be granted return. While The Wahid Institute reported a decline in religiously motivated attacks from 243 cases in 2013 to 158 incidents in 2014, most observers explained this drop with a shift in focus by radical groups during an election year rather than increased state protection. Indonesia has also been slow to take steps against former human rights abusers. After years of debate, Indonesia confirmed in 2013 and 2014 that, for the time being, it would not ratify the Rome Statute of the International Criminal Court.

4 | Stability of Democratic Institutions

Overall, Indonesia’s democratic institutions are functional and operate in an effective manner. While the inauguration of President Joko Widodo in October 2014 was followed by a period of conflict between the government and parliament (in which the opposition held a majority at that time), these problems did not cause a serious, long-term crisis in executive-legislative relations. Similarly, the executive has honored the decisions made by the Constitutional Court, although many of its verdicts have openly contradicted government policies. Problems with the performance of democratic institutions usually do not arise as a result of interactions between state bodies, but rather have their roots in dynamics within them. For instance, ministries have a high level of autonomy and are controlled by different parties or technocrats, impeding the government to act as a coherent entity. In parliament, decisions are rarely made by majority vote along party lines, but are mostly the result of consensus-oriented negotiations that involve individual legislators and commissions as much as parties and caucuses. This leads to highly protracted policy-making processes and in some cases low-quality legislation. In 2013 and 2014, the Constitutional Court overturned 51 unconstitutional measures that had been enshrined in national law, pointing to serious problems in the legislative process. At the local level, the effectiveness of executive and legislative institutions varies widely. While some areas have moderately stable and accountable institutions, in others (such as Papua) these are handicapped by nepotism, corruption, mismanagement and incapacity.
While most major social and political forces rhetorically accept Indonesia’s democratic institutions as legitimate, the years 2013 and 2014 have seen a revival of anti-democratic discourses in Indonesia. For the first time since the regime change in 1998, a leading presidential candidate, Prabowo Subianto, suggested that the country should return to its pre-democratic constitution of 1945, which had served as the legal foundation of Sukarno’s and Suharto’s authoritarian regimes. Prabowo lost the election, but some of his supporters have continued their demands for a democratic rollback. So far, however, the democratic institutions have maintained their authority, and even Prabowo ultimately accepted his proclaimed defeat at the ballot box through the Electoral Commission and the Constitutional Court. Importantly, the armed forces have been successfully subordinated to the civilian democratic leadership, and Nahdlatul Ulama and Muhammadiyah, the two biggest mainstream Islamic organizations, have also endorsed the democratic system. Thus, the most vocal opponents of the democratic system – besides conservative supporters of Prabowo – are Islamist groups such as Hizbut Tahrir Indonesia and the Indonesian branch of IS. Although not irrelevant in terms of their social significance, these organizations’ following is not large enough to pose a serious threat to the democratic polity.

5 | Political and Social Integration

Indonesia’s party system is fairly stable and socially rooted. Voter volatility is considerably lower than in many other new democracies in Eastern Europe, Latin America or East Asia. In the 2014 legislative elections, all nine parliamentary parties of the previous period re-entered the legislature, and only one new party gained seats. The level of polarization is also low. The stability of the current Indonesian party system contrasts sharply with the excessive polarization and volatility of the party system in the 1950s, the only other democratic period in the country’s history before the 1998 regime change. For the 2014 elections, the parliamentary threshold (i.e., the vote percentage a party needs to achieve nationally in order to enter parliament) was raised to 3.5%, a move which further consolidated the party system. Indonesia’s political parties tend to be anchored in specific religio-political constituencies, although the switch to a more candidate-centered electoral system after 2004 has also led to the emergence of catch-all presidentialist parties such as Yudhoyono’s Democratic Party or Prabowo’s Great Indonesia Movement.

Indonesia has a wide variety of interest groups that reflect competing societal interests. There are Islamic organizations such as Nahdlatul Ulama and Muhammadiyah, which are among the largest Muslim groups in the world; there are hundreds of labor unions that – although not centrally organized – were highly effective in achieving large increases in the minimum wage in 2013 and 2014; there are grassroots groups, women’s rights associations, church networks, human rights NGOs, agrarian organizations, think tanks, mass media organizations, and many
more associations that mediate between society and political parties. In combination, these groups have formed a powerful counterweight to the rising influence of oligarchic business interests. Of course, some societal interest groups have pursued an anti-democratic agenda: while numerically small, violent organizations such as the Islamic Defenders Front have successfully used the mushrooming of NGOs throughout the country to masquerade their attacks on nonmainstream religious groups as legitimate expressions of civil society activism.

Most Indonesian citizens strongly support democracy, both as a principle and as the basis of the current political system. In July 2014, 75% of respondents in a poll run by Saiful Mujani Research & Consulting (SMRC) stated that they wanted democracy to be practiced in Indonesia. Moreover, a majority of Indonesians regularly express satisfaction with the way democracy functions (in July 2014, this figure - in the same SMRC poll - stood at 69 percent). Interestingly, even the vast majority of Prabowo Subianto voters supported democracy, suggesting that they did not believe he would go ahead with his anti-democratic agenda if elected president. There are two caveats to this general pattern, however. First, there is no joint understanding among Indonesians of what democracy means. In some surveys, many respondents have defined democracy as the state’s satisfactory provision of welfare. Second, some key democratic institutions, most notably parties and parliament, have invariably received bad marks from Indonesian citizens. Given that these two entities often suffer from low levels of popularity in advanced democracies as well, this should not come as a surprise. Many other institutions, including the presidency, the armed forces, the Anti-Corruption Commission, the Constitutional Court and various levels of local government enjoy generally high approval ratings.

Indonesia has a large number of autonomous self-organized groups, associations and organizations. A recent study found that 84% of Indonesians belong to at least one such organization, as compared to a world average of 63% (as a regional comparison, this figure is 61% in Malaysia and 51% in Thailand). The number of people belonging to three organizations or more is nine times higher in Indonesia than in the Philippines or Singapore, and three times higher than in Thailand. In the study’s sociability index (which measures the degree of intragroup loyalty and incidence of activities such as joining religious organizations), Indonesia has a score of 0.79, significantly above the world average of 0.49, the Philippines’ score of 0.54 and Singapore’s score of 0.49. However, the level of trust between citizens is not always as high. In the 2012 – 2015 period, there have been numerous incidents of rural clashes and ethnic tensions over relatively small issues, sometimes resulting in deaths and serious injuries. One such clash occurred in the province of East Nusa Tenggara in August 2014, leaving one person dead and five injured.
II. Economic Transformation

**6 | Level of Socioeconomic Development**

Despite significant economic growth in the last 10 years, Indonesia continues to face serious development problems that effectively exclude large sections of the population from socioeconomic participation. In the 2014 Human Development Index, Indonesia ranked at 108th out of 187 countries surveyed. Moreover, its index score has increased only slowly, from 0.681 in 2014 to 0.684 in 2013. Poverty remains the country’s biggest socioeconomic challenge. While the official poverty rate declined from 11.46% in September 2013 to 11.25% in March 2014, these figures are based on a national poverty line of $0.80 per day (US$ 24 a month), significantly below the $1.25 a day threshold used by the Asian Development Bank and the now widely recommended poverty line of $2 a day. If the later formula were to be applied to Indonesia, about 43% of the population could be considered poor or near-poor. While in absolute numbers most of the poor live on Java, eastern Indonesia has the highest concentration of poverty in percentage terms. The concurrent economic boom and persistence of poverty has led to increasing levels of inequality. Indonesia’s Gini index has risen significantly, from 0.38 in 2010 to 0.41 in 2013/14. By the same token, the household consumption share of the upper 20% of income earners rose from 42.1% in 2004 to 49% in 2013-14, while the share of the lowest 40% of income earners fell from 20.8% to 16.8%. Women are particularly affected by this increasing level inequality. Indonesia ranked only 103rd in the 2013 Gender Inequality Index, down from 100th in 2011.

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<td>Unemployment (%)</td>
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### Economic indicators

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<td>0.8</td>
<td>1.1</td>
<td>1.2</td>
</tr>
<tr>
<td>R&amp;D expenditure</td>
<td>% of GDP</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>Military expenditure</td>
<td>% of GDP</td>
<td>0.8</td>
<td>0.6</td>
<td>0.9</td>
</tr>
</tbody>
</table>

Sources (as of October 2015): The World Bank, World Development Indicators 2015 | International Monetary Fund (IMF), World Economic Outlook, October 2015 | Stockholm International Peace Research Institute (SIPRI), Military Expenditure Database 2015.

### 7 | Organization of the Market and Competition

In generally, market competition enjoys a sound institutional framework in Indonesia. However, there are two (important) major constraints: rules for market competition are not always uniform for all market participants; and Indonesia has a significant informal sector (which is true for all countries in Asia, Latin America, Africa, and most post-communist countries).

While Indonesia’s economy is generally based on free market principles, the period between 2013 and 2015 recorded some contradictory evidence in this regard. On the one hand, Indonesia has increasingly turned to protectionist measures. In 2013 and 2014, four new laws were passed that allow the government to increase tariffs and regulate new import and export quotas: Law 19/2013 on the Protection and Empowerment of Farmers, Law 3/2014 on Industry, Law 7/2014 on Trade, and Law 39/2014 on Plantations. This increased state control of trade policies followed significant public criticism of ASEAN’s 2010 Free Trade Agreement with China, which particularly threatened Indonesia’s continuously large informal sector (59% of Indonesians work in that sector). Indonesia has also forced a number of foreign oil and mining firms to agree to renegotiate their long-term contracts with the government. This has led to complaints among investors about the legal certainty of their contracts. Moreover, an export ban on unprocessed minerals was declared in January 2014, trying to force investors to build in-country processing facilities. At the same time, entry barriers for foreign investment were retained and even expanded.
- in early 2015, a court ruled that water supply must be managed by the state, effectively canceling a number of foreign investment projects in that area. On the other hand, however, Indonesia removed one of the biggest market distortions that had challenged the country’s economy for decades: in January 2015, President Joko Widodo abolished subsidies for premium petrol, declaring that its price would now be determined by the world market. Indonesia also maintained full currency convertibility, despite public demands for more state efforts to stabilize the Rupiah. In the 2014/2015 World Competitiveness Report, Indonesia was thus ranked a very respectable 34th out of 144 countries.

Indonesia’s anti-monopoly measures are relatively effective. The state no longer grants monopolies to politically connected entrepreneurs, as was the case under Suharto’s authoritarian regime. Many business fields previously monopolized by state-owned enterprises are now also open to competitive private investment. In the 2014/2015 World Competitiveness Report, Indonesia was ranked 37th out of 144 nations in terms of the effectiveness of anti-monopoly policy. To some extent, Indonesia’s success in controlling monopolization trends is due to the work of the Commission for the Supervision of Business Competition (KPPU), established in 2000 under Indonesia’s Anti-Monopoly and Unfair Competition Law. However, the law is still ambiguous. Also, some of the KPPU’s recent decisions have been overturned by the Supreme Court. In September 2013, the Supreme Court rejected an appeal by the KPPU against a decision by a lower court that had annulled a KPPU verdict against a number of companies in the gas processing sector. The companies had been accused of conspiring not only amongst each other to avoid competition, but also of manipulating state tender processes. Thus, while anti-monopoly policies are stronger than in the past, the weak Indonesian court system continues to undermine the KPPU’s effectiveness. In addition, there have been significant concentration trends in the media sector, with a handful of tycoons controlling virtually all of Indonesia’s television stations.

As a country whose growth is driven largely by domestic consumption rather than foreign trade, Indonesia has had fewer incentives to liberalize its foreign trade regime than have many of its neighbors in Southeast Asia. In 2014, Indonesia’s export volume to GDP ratio was 23.6%, while the percentage of imports in total GDP was just 25.4%, indicating a very low rate of foreign trade and ranking it 129th in the World Competitiveness Report in that category. In other indicators of the openness of its trade regime, Indonesia ranked slightly better, but still exhibited a tendency toward protectionism and cumbersome trade procedures. For instance, it was ranked 103rd with respect to the prevalence of trade barriers, 68th for the burden presented by customs procedures, 64th for the extent of trade tariffs, and 59th for the business impact of foreign direct investment rules. A number of new laws and regulations passed in 2013 and 2014 have restricted trade liberalization and privileged local companies over foreign investors. For instance, parliament passed a law in September
2014 that gave the government instruments to limit foreign ownership in plantations. While an initially proposed 30% ownership cap was rejected, the new law will give the incumbent government opportunities to set such limitations if it wishes to do so. Equivalent laws on trade and industry also enable the executive to set tariffs and quotas for imports and exports. Such protectionist measures enjoyed widespread public and elite support.

After collapsing in 1997–1998, Indonesia’s banking system has made a remarkable recovery. Its current indicators point to overall stability. Indonesia’s bank-capital-to-asset ratio was 12.5% in 2013, its capital adequacy ratio (CAR) was 18.1% in July 2013, and the banks’ share of nonperforming loans was 2.1% in 2014. All of these figures are better than the Basel III requirements for a healthy banking sector. However, conflicts have emerged between the Central Bank (BI) and the newly established Financial Services Authority (OJK), with the former handing over authority of bank supervision to the latter on 31 December 2013. In early 2014, a case was brought to the Constitutional Court that sought to cancel this transfer of power, and the BI expressed implicit support for this petition by pointing to examples of overlapping authority between the two institutions. Moreover, many banks are critical of the fees they have to pay to the OJK to fund its operations. The unclear demarcation lines between BI and OJK are likely to lead to further tensions in the years ahead. In terms of the accessibility of the Indonesian banking sector for foreign investors and banks, there have been calls by populist politicians to impose tighter restrictions.

After the 1997–1998 crisis, Indonesia allowed foreign banks to hold up to 99% of shares in Indonesian banks. A new draft law on regulating the banking sector was discussed in parliament in the 2009-2014 term, but did not pass. In this draft bill, foreign ownership in Indonesian banks was limited to 40 percent, with additional share purchases allowed if certain conditions were met. In its new, 2014-2019 term, parliament is likely to revisit this draft, and discussions on limiting foreign ownership in banks are likely to be a dominant theme once again.

8 | Currency and Price Stability

While Indonesia was widely praised for its prudent anti-inflation and monetary policies in the past, the period between 2013 and 2015 has seen significant problems emerge in both fields. In December 2014, year-on-year inflation stood at 8.36%, much higher than the Central Bank’s target of 4.5% (plus/minus 1%). This was largely the result of cuts to fuel subsidies in November 2014, but even before that, inflation had been at 8.22% in January 2014. Similarly, the national currency, the Rupiah, experienced a sharp depreciation between early 2013 and early 2015, from IDR 9,500 to IDR 12,600 per US dollar – a drop of 25%. In addition to global currency trends (i.e., the strengthening of the US dollar towards most other currencies), the depreciation of the Rupiah was primarily the result of Indonesia’s
worsening account deficit. The independence of the Central Bank (BI) in controlling all aspects of monetary policies has been diminished by its loss of bank supervision powers to the newly formed OJK.

One of the biggest successes of the Yudhoyono presidency has been the reduction of the government-debt-to-GDP ratio from 60.5% in 2004 to 26.1% in 2014. While external debt increased from $132.6 billion in 2006 to more than $294 billion in October 2014, the rapid expansion of the broader economy has made this rise easy to manage. In the same vein, Indonesia increased its foreign reserves from below $40 billion in 2004 to $111.8 billion in December 2014. However, the populist spending on fuel subsidies – which was only drastically reduced in November 2014 - has led to the highest budget deficit in a decade, reaching 2.3% in 2014. At the same time, Indonesia recorded current account deficits throughout 2012, reaching a high of $10.1 billion in mid-2013 (in 2006, it had still registered record surpluses of $3.8 billion). While these deficits point to Indonesia’s increasing need for imports to fuel its expanding economy, they also highlight a reduced demand for Indonesian exports as a result of the stagnant world economy. Thus, these deficits will become a source of concern if sustained over the long term.

9 | Private Property

Private property rights are generally upheld, but remain vulnerable to the uncertainties inherent with a corrupt judiciary. Especially in the area of land rights, courts often side with the party that offers the largest bribe to the judges handling the case. Thus, in the 2014 International Property Rights Index, Indonesia ranked only 59th out of 97 surveyed countries. Within this index, Indonesia has recorded a particularly poor result in the protection of intellectual property rights, where it ranked 83rd and witnessed a slight decline of its score compared to the 2013 index. This reflected the open availability of pirated software, movies and music DVDs across Indonesia, against which the government and law enforcement agencies have taken no serious measures. For example, in a 2014 survey by the Business Software Alliance, the Unlicensed Software Installation Rate of Indonesia was 83%, virtually unchanged from previous years. In the Asia-Pacific region, the average percentage was 62%, and globally it was 43%.

The Indonesian state views private enterprises as primary engines of economic production. Indeed, much of the government’s long-term economic planning relies on investment by and the role of private businesses, especially with respect to developing infrastructure and fueling growth. Private business organizations such as the Chamber of Commerce (Kadin) and the Association of Indonesian Entrepreneurs (Apindo) have become increasingly powerful. Since 1998, the government has privatized many state-owned enterprises (SOEs) in an attempt to reduce its debt, and has pledged to make the remaining ones operate more professionally. Initially,
privatization processes were handled by a government-run debt restructuring team, but since the late 2000s, international financial firms have been hired to manage initial public offerings (IPOs). However, this privatization drive has slowed down in recent years. After the national airline Garuda was successfully listed on the stock market in 2011, the government prepared IPOs for several other companies. However, only two plantation companies were approved for IPOs in early 2014, and they had still not been realized by early 2015. In addition to a general stagnation of IPOs at the stock market due to the sluggish investment environment, the increasing economic nationalism has also been responsible for the stalling of new privatization initiatives. In early 2015, the government injected $3.1 billion into the remaining SOEs, suggesting that it intends to not only retain, but to strengthen them.

10 | Welfare Regime

While Indonesia’s social safety nets remains underdeveloped compared to the Western world, there have been significant improvements in the 2013-2015 period. In January 2014, the health component of a new social security agency (BPJS) became operational, providing health insurance to all Indonesians. Those with a regular income pay monthly premiums, while these are provided for the poor or unemployed by government. In July 2015, the second BPJS component will be launched, offering accident and life insurance as well as pension programs. President Joko Widodo also announced additional initiatives after his election, most of which constitute expansions of existing programs. There have been reports of already exhausted budgets because so many people make use of the new services. But the country has made progress beyond simply initiating a national social security scheme. More and more districts and municipalities have introduced their own systems, offering free health care and schooling to their citizens. In addition, there is a wide variety of national and local programs for the poor, ranging from cash hand-outs to distribution of free food and provision of heavily subsidized oil for home cookers.

While equal opportunities to access education, public office or employment are generally available to citizens regardless of ethnicity or religion, there are significant hurdles for women, the poor, citizens in rural areas and persons with non-conformist sexual orientations. Women are underrepresented in the workforce, with 51% of them obtaining some form of employment as opposed to 84% of men. In the 2014 parliament, only 17% of members are women (down from 18% in the last legislature), and just a handful of governors, district heads or mayors are female. The poor face equally significant challenges in obtaining high-quality education or employment. While literacy and gross primary school enrollment levels are high in Indonesia (93% and 109% respectively), the quality of public schools is sub-standard to a point where private school graduates are often preferred over regular school graduates when seeking employment. Rural Indonesians also face harder living conditions than those
who live in the city. In September 2014, 8.2% of urban citizens were poor, versus 13.8% of the rural population. Finally, citizens with non-conformist sexual orientations are confronted with various forms of discrimination, both on a state as well as societal level.

11 | Economic Performance

Indonesia’s economy has been deteriorating despite an overall solid performance. GDP growth was at 4.9% in the last quarter of 2014, the lowest rate since 2009. While still recording one of the strongest growth rates among G20 nations, the decline points to the end of the commodity boom, which had fueled Indonesia’s economic expansion for more than a decade. Nominal GDP per capita was $3,475 in 2013, only a slight increase from its 2011 level of $3,470. In purchasing power parity (PPP) terms, GDP per capita was above $9,500 in 2013. The official unemployment rate stood at 5.94% in October 2014, down from 11.24% in October 2005 – but unrecorded underemployment remains very high. Foreign direct investment (FDI) inflows hit a record $23.3 billion in 2013, but its growth has slowed down significantly in 2014: third quarter growth was only 0.4 percent over the second quarter of 2014. As noted in earlier sections, inflation reached the 8-percent-mark in 2014, and Indonesia’s current account and budget deficits have increased in 2013 and 2014. In the same vein, the tax-revenue-to-GDP ratio remained stagnant at an unsatisfactory 12% in 2014. Although other macroeconomic indicators continue to be sound (such as the debt-to-GDP ratio of 26%), the output strength of the Indonesian economy was weaker between 2013 and 2015 than during the previous 2011-2013 review period.

12 | Sustainability

Former Indonesian President Susilo Bambang Yudhoyono had tried to present Indonesia as a pioneer in environmental protection among the developing world. He promised to reduce carbon emissions by 26% by 2020, signed several agreements with foreign nations about cooperating in the prevention of deforestation, and - in November 2014 – was awarded the Champion of the Earth Award by the United Nations Environment Program (UNEP). After his retirement, Yudhoyono became the chairman of the Global Green Growth Institute, a South Korea-based body committed to promoting environmental sustainability, particularly in the developing world. Thus, on a rhetorical level, Indonesia paid attention to environmental issues throughout Yudhoyono’s ten-year rule. The reality, however, looked much less impressive. In the 2014 Environmental Performance Index, Indonesia ranked 112th out of 178 surveyed countries – in the 2012 index, it had been ranked 74th out of 132 nations. While that figure has shown a slight upwards trend in the last ten years, the rise was minimal. Indeed, Indonesia has done little to implement its ambitious announcements. It continues to build coal-fueled power plants, to expand its
plantations and to offer subsidies for the consumption of some fuels rather than limiting it through tax incentives. Thus, on the 2014 PricewaterhouseCoopers Low Economy Carbon Index, Indonesia had one of the lowest declines in carbon intensity (the amount of carbon emissions per unit of GDP) of all G20 countries between 2012 and 2013. While Indonesia’s carbon intensity fell by 0.1%, China’s declined by 4.0%, and the world average saw a decline by 1.2%. Meanwhile, the implementation of the Reducing Emissions from Deforestation and Forest Degradation (REDD+) does little to nothing to curtail drivers of deforestation and forest degradation. The new government of Joko Widodo has given no indication that environmental protection is high on its priority list.

Indonesia’s education and research facilities are generally of poor quality. While primary education enrollment is satisfactory, Indonesia’s secondary education enrollment levels are low (82.5% in 2014), as is its tertiary education enrollment (31.5%). At 3.6% (in 2012), the ratio of education spending to GDP is also below average. As a result, in the most recent PISA (Programme for International Student Assessment) tests released in 2013, Indonesia ranked 60th in reading skills and 64th in maths and science (out of 65 participating nations). Similarly, the levels of R&D spending are substandard. Based on the latest available data from 2012, Indonesia spent only 0.2% of GDP on research and development. In the 2014/2015 World Competitiveness Report, Indonesia was ranked 106th out of 144 surveyed countries in the number of patents per 1 million of a country’s inhabitants (0.1). However, not all of Indonesia’s indicators in the field of education and R&D are discouraging. According to the 2014-2015 World Competitiveness Report, Indonesia was ranked 22nd with respect to the capacity for innovation, and 25th in company spending on R&D. The number of scholarship programs for students, state university lecturers and public servants provided by the central and local governments has also increased. In April 2014, the government launched a new Presidential Scholarships scheme, through which at least 100 Indonesians will be placed at top-ranked international universities each year. The new Joko Widodo government has also announced that it plans massive new investments in the education sector, and has appointed a popular former university rector as minister of education to oversee the reforms.
Transformation Management

I. Level of Difficulty

As in previous review periods, the major constraints on the Indonesian leadership’s governance capacity remain widespread poverty, low education levels, severely limited public infrastructures especially in the regions outside Java, endemic corruption and geographical factors. With just below half of the population living on less than $2 a day, Indonesia’s political leaders have to focus much of their attention on fulfilling the population’s basic needs. This in turn often contributes to short-term policies rather than long-term solutions. Similarly, the lack of an educated workforce makes Indonesia’s transformation into an industrial, modern and sophisticated society difficult. Particularly serious is the low percentage of Indonesians with a tertiary education – 31.5% as compared to Thailand’s 51%, for example. In the same vein, the rampant corruption and weak rule of law continue to sabotage the development of a modern economy and of public infrastructure such as roads, bridges, electricity generation and transmission facilities and clean water. Finally, Indonesia’s geographic conditions also constrain governance capacity. As an archipelago stretching about 5,000 kilometers and encompassing three time zones from its western to its eastern end, the country faces considerable transportation, communication and infrastructure challenges. This vulnerability to geographic factors is due to the high likelihood of natural disasters, especially volcanic eruptions, earthquakes, tsunamis, floods and landslides. A July 2013 earthquake in Aceh, which killed 35 people, demonstrated that a disaster like the 2004 Boxing Day tsunami, which caused around 170,000 deaths and billions of dollars in damage, could strike again at any time.

While Suharto’s authoritarian regime sought to control and suppress civil society activism, the regime change led to an explosion in the number of NGOs and other societal organizations. In July 2013, the Home Ministry reported that there were at least 139,507 NGOs in Indonesia. A new civil society organization law, passed in 2013, tightened regulations for NGOs, but their number keeps rising. When the law was passed, 300 NGOs registered in the city of South Tangerang alone. Most of these civil society groups have scrutinized government policies, demanded more popular participation in budgeting, protested against corruption, and have represented the poor vis-à-vis bureaucrats, employers and law enforcement institutions. Indeed, civil
society is at the moment the strongest bulwark of Indonesian democracy: NGO-based volunteers were the most vocal opponents of Prabowo Subianto’s neo-authoritarian candidacy in the 2014 elections. While civil society activism is stronger in the urban centers than at the local levels, decentralization has strengthened NGO operations in the districts as well. Despite the strength of civil society activism, it is vital to recall that not all civil society groups are supportive of principles of good governance, the development of social capital and popular participation. Some groups (Hizbut Tahrir Indonesia, for example) openly pursue nondemocratic goals, such as limiting the rights of religious minority groups. Some others are under control of politicians, and are used to support their sponsor’s interests. Dealing with these groups is a constant policy challenge for incumbent governments at both the national and local level. In November 2014, for example, Islamist civil society groups protested against the inauguration of Basuki Tjahaja Purnama as the new governor of Jakarta because he is both Christian and ethnic Chinese.

After high levels of religious, ethnic and separatist conflict in the early phase of the post-authoritarian transition, the extent of communal violence is now relatively low. To be sure, clashes between religious, ethnic and local groups still occur, but on a much smaller scale than in the late 1990s and early 2000s. The period between 2013 and 2015 has seen a number of land conflicts, particularly in Lampung, Sumatra. In September 2014, one person was killed in the latest installment of the conflict, during which thousands of farmers occupied a plantation in Mesuji district, and security forces tried to remove them. Political conflicts resulting from local elections also still occur in some regions, especially in Papua. At the national level, the nature of political competition is largely non-combative, despite a period of strong polarization during the 2014 electoral campaign. During this campaign, Indonesia’s religio-political cleavages (between more secular and Islamist forces) became visible, but were de-escalated after the outcome of the election was confirmed. Indeed, these cleavages are crucial for the maintenance of an effective party system, which requires a certain degree of partisanship in order to survive. One indication of the sustainability of Indonesia’s cleavage structure is that it has not triggered significant mass mobilization. The only instances of large-scale mass protests in recent years have involved labor unions demanding higher wages. While some of these actions have interrupted industrial production, they have also led to considerably higher minimum wages for Indonesian workers. Overall, the level of societal and political violence is moderate to low.
II. Management Performance

14 | Steering Capability

In general, the government has the capacity to prioritize and organize strategic policy measures but it is constrained by three major institutional factors: the post-1999 decentralization, through which significant policy authorities were transferred from central to district levels; the fragmented nature of post-Suharto “rainbow coalition” governments; and third, the time-consuming bargaining processes within the legislature, especially the DPR’s committees.

While the Yudhoyono government had often been criticized for failing to set clear priorities, the administration of Joko Widodo has defined a strong set of priorities under the so-called Nawa Cita (nine priorities agendas). These include health, education, infrastructure, and vision of a maritime nation. In order to mobilize the funds needed to improve public service delivery in these three areas, Widodo also announced that he would drastically reduce fuel subsidies – something Yudhoyono had been unable to do during his ten years in power. Widodo delivered on his promise in November 2014 and January 2015, when he first reduced subsidies and then set the price of premium petrol based on its market value. It remains to be seen if his government can withstand potential public pressure, should international oil prices increase again. In areas of health, education and infrastructure, Widodo also initiated quick reforms, such as new health insurance cards and new education scholarship programs. Indeed, Widodo has been so focused on his main priorities that he has neglected other important policy areas, such as defense, human rights or broader issues of political reform. In all of these areas, he has surrendered authority to conservative elements in his cabinet, who use their powers to set and pursue personal interests. These conservative elements include oligarchs and retired military officers who supported Widodo during his 2014 campaign, and have subsequently been rewarded for their support. Thus, while Widodo has set stronger priorities for Indonesia than Yudhoyono, he has done so at the expense of other policy fields that are of great significance.

Policy implementation has been obstructed by a range of problems. To begin with, parliament has often blocked executive policies. In September 2014, it voted down a government draft bill on local direct elections – although parties supporting the government held the majority in the chamber. President Yudhoyono, then in his final days, had to resort to a rare emergency measure to have his draft released. Moreover, individual legislators often have locally defined and/or material interests that drive them to seek amendments to the executive’s budget proposals. Similarly, government
policies are often overturned by the Constitutional Court. In January 2013, for example, the court disbanded a government-sponsored system of privileged schools, in which the main language of instruction was English. Furthermore, national governments have found it much more difficult to implement national policies in the wake of the decentralization that became fully operational in the mid-2000s. More than 40% of the national budget is now spent by local governments, up from 17% in 2000. Other hindrances to effective policy implementation include corruption, noncompliance and ineffective bureaucracies. For instance, the bureaucracy protested against a draft bill that would have modernized its internal selection and promotion process – in response, Yudhoyono changed the most controversial sections of the bill in December 2013. It should not be suggested that government policies are only rarely implemented. In fact, given the myriad problems in day-to-day governance, a surprising number of policy initiatives do get put in place by national and local executives.

In the early post-authoritarian transition, Indonesian governments were highly innovative. Learning from the mistakes of previous autocratic regimes, post-Suharto rulers introduced effective democratic institutions and the basic structures of a market economy. Since the mid- to late 2000s, the pace of innovation has slowed down. The current government’s track record in learning and innovation is ambiguous. One the one hand, the Widodo administration has dramatically reformed the fuel subsidies regime, after a succession of governments had previously failed to do so. In this case, Widodo showed a significant ability to learn from, and correct, errors made by his predecessors. On the other hand, however, Widodo has put the defense forces under a minister widely known for his outdated ideas, and unsurprisingly, he has proposed to reinstate some military practices abolished during the reform era, such as an army program aimed at the organization of student regiments on campuses. At the same time, some sections of the elite – both within and outside of government – are openly propagating the return to a more centralist, executive-heavy system of government, despite the negative experiences Indonesia made in this regard under Sukarno and Suharto.

15 | Resource Efficiency

Indonesia faces significant problems in using its available human, financial and organizational resources effectively. For example, national and local executives spend more on administration and salaries than is usual in most other countries (in some districts, nearly 70% of the total budget is allocated for the management of the bureaucracy), but there has been no dramatic improvement of public services that could justify such expenditure. Similarly, the recruitment of civil servants is often not based on merit – in some cases, positions are “sold” to applicants, whereas in others they are given to associates and relatives of senior bureaucrats. A new law on
the civil service, passed in 2013, is not expected to drastically change this constellation. While the overall budget deficit is manageable and government debt is low, there are inefficiencies in budget management as well. Indeed, these inefficiencies often result in a situation in which governments struggle to spend the available money. For instance, in December 2014, the Jakarta city government had spent only 36% of its 2014 budget. In more general terms, the government does not make effective use of its unique human and natural resources. While Indonesia’s workforce is Asia’s third largest, it is also one of the region’s most unproductive – labor productivity stood at 10.7% of the 2013 levels in the U.S. (Malaysia’s was 32.4%), and productivity growth had slowed down compared to 2012. The country’s abundant natural resources are often not professionally managed. Illegal logging, mining and fishing cost the state billions of dollars each year, and it has fallen behind in developing new gas, oil and mining concessions that could be of substantial budgetary benefit.

Post-Suharto governments have found it difficult to coordinate conflicting objectives into a coherent policy. Ministers have traditionally enjoyed a high level of autonomy in running their departments, and the level of coordination between them is low. Before his inauguration, Joko Widodo had promised to improve the coordination of ministers, but early indications are that little has changed. Widodo has a tight grip over the ministries that deal with his policy priorities (health, education, infrastructure), but has allowed other ministers to run their departments without much intervention. Even if cabinet was coordinated more effectively, it would still face the problem of amalgamating the interests of the executive, the parliament, the Constitutional Court, several levels of local government and public opinion into a coherent set of government policies. The degree of power diffusion in post-authoritarian Indonesia is extremely high, and while this has prevented the return of authoritarianism, it has also complicated policy-making. For instance, between October and December 2014, internal divisions in parliament prevented any executive-legislative interactions. Despite such complications, the government has been mostly able to deliver satisfactory macroeconomic policies, not least thanks to a long tradition in Indonesian politics of entrusting the actual implementation of economic and monetary policies to a small circle of Western-educated technocrats – a tradition continued by Widodo. Problems of the policy coordination also occurred between the central and local governments in developmental policies.

Between 2013 and 2015, an unprecedented number of ministers, legislators, judges, bureaucrats and senior party officials have been indicted, arrested or sentenced. In the last months of Yudhoyono’s presidency, both the minister of religion and the minister of mines and energy were charged with corruption. The Anti-Corruption Agency (KPK) also achieved a life sentence against the chief justice of the Constitutional Court, and indicted the head of the State Auditing Agency (BPK) on the day of his retirement. This signifies that many officials are now being held...
accountable for their transgressions, but it also demonstrates that corruption is still endemic. Moreover, there are signs that President Widodo may not be able (or willing) to withstand the pressure by some elite groups to reduce the KPK’s powers (Widodo showed little determination in early 2015 to defend the agency in a serious conflict with the police). At the same time, the auditing of state spending remains weak. In the second half of 2013, the BPK found 10,996 cases of financial irregularities involving $1.1 billion of state funds, but there have been few legal consequences for the agencies accused of the violations. Similarly, party financing regulations are not enforced. Since the state provides only minuscule state subsidies to parties (covering far less than 1% of their operational costs), the parties’ illicit fundraising activities are widely tolerated. During the 2014 elections, parties and candidates spent significantly more than they reported (including on vote-buying), but the Election Commission (KPU) declared that no violations of campaign financing rules took place. While office holders have to submit regular wealth reports that are widely publicized in the media, unusual increases in wealth over time only rarely lead to legal investigations. For instance, most candidates for the post of police chief in January 2015 had a personal wealth in excess of $500,000, despite receiving a salary of only $2,000 a month.

16 | Consensus-Building

The consensus among the political elite about maintaining the democratic system has weakened significantly in the 2013-2015 period. Prabowo Subianto, one of the two presidential nominees in 2014, openly supported Indonesia’s return to its pre-democratic constitution, and gained 47% of the vote. He was supported by Abdurizal Bakrie, the chairman of Suharto’s former electoral machine, Golkar. Bakrie suggested that Indonesia revive Suharto’s “Pancasila Democracy”, a tightly controlled system guided by the state’s consensus-oriented philosophy. In September 2014, Prabowo and Bakrie led a coalition of parties that achieved the abolition of direct local elections, a measure that was eventually overturned by Yudhoyono. All this indicates that the anti-democratic discourse has gone mainstream. The only factor that mitigates this rise of anti-democratic rhetoric is the continued strong support for democracy in society itself.

The consensus on the need for a market economy has also eroded. The 2014 election campaign was marked by strongly protectionist and nationalist rhetoric, and Widodo stuck with this position after the ballot. That said, Indonesia is unlikely to return to the economic isolationism of the 1960s. It is probable that Indonesia will be forced to rescind some of its protectionist policies if and when they begin to hurt the overall economy – that is, if they have an impact on FDI and GDP growth.
In general, the Indonesian polity has co-opted rather than excluded anti-democratic actors. The armed forces, oligarchic interests and Islamist groups have all been offered a place in the post-authoritarian system. This tradition has been continued by President Widodo, himself a moderate reformer. Dependent on party support in the legislature (he does not control a party as his own powerbase), Widodo has been forced to include a wide range of military, oligarchic and conservative party interests in his government. On the one hand, this inclusiveness has guaranteed the stability of the polity, giving spoilers few incentives to derail the democratization process. On the other hand, the integration of anti-democratic actors has slowed down reforms. Oligarchic interests, for instance, have been increasingly powerful. Indeed, oligarchs have taken over a number of key parties, exploiting the latter’s financial weakness by offering to fund their operations. In 2015, five of the ten main parties were led by financially powerful patrons, who in turn have received access to policy-making processes. Local strongmen and bossism have gained a foothold as well. The armed forces, while politically emasculated, have enjoyed continued legal impunity for past (and more recent) human rights violations in exchange for their acceptance of democratic rule. By 2015, not a single high-ranking general had gone to prison for any of the systematic and gross human rights violations committed under Suharto. Finally, Islamist parties and forces have a significant stake in the post-Suharto polity, which constrains their anti-democratic activism but also gives them political leverage to gain influence over important policy decisions. While their candidate, Prabowo Subianto, lost in the 2014 elections, Islamist parties maintain a powerful presence in local governments.

The 2014 elections re-opened a national cleavage between secular nationalists and supporters of a stronger role for Islam in state organization, which Indonesia had managed well for much of the post-Suharto democratization process. While the cleavage lost some of its intensity after the elections, it is likely to be more pronounced under President Widodo, a nationalist, than it was under Yudhoyono. At the grassroots, this cleavage has remained significant too, with attacks against nonmainstream Muslim groups and other religious minorities (mostly evangelical Christians) continuing in 2013 and 2014. The government has also faced a widening class cleavage, with Indonesia recording the fastest growth of millionaires in Asia and underpaid workers now demanding better pay. Accordingly, massive labor strikes continued in 2013 and 2014. In order to calm the protests, the political leadership agreed to large increases in minimum wages, despite knowing that such a short-term, unsystematic response was unlikely to solve the problem. However, there is one divide that Indonesia has routinely managed well in recent years, including in the 2013-2015 period: regional and urban-rural conflicts have been addressed effectively through inequality-mitigating mechanisms built into the decentralization policies. Poorer areas receive more central government subsidies than affluent ones.
Thus, there have been very few center-periphery conflicts, or serious conflicts between territories.

Indonesian civil society has a significant but ambivalent influence on the political process. On the one hand, there has been a notable influx of civil society activists into political parties and parliament since the mid-2000s. Women’s activists, labor leaders, journalists and other civil society figures have since that time occupied critical positions in the political infrastructure. President Joko Widodo’s election campaign in 2014 was strongly supported by pro-democracy civil society groups, and he appointed the activist son of a former migrant worker as labor minister. Not only because of this appointment, labor unions have found it relatively easy to exert pressure on incumbent officials at both the national and local levels – no minister, governor, district head or mayor can today issue labor-related regulations without taking the demands of the unions into account. The 2013 and 2014 increase in minimum wage across the archipelago are examples of this. The media has also had a tremendous influence on policymaking, with government plans often faltering after attacks by newspapers and television stations. On the other hand, the strength of civil society has a downside: nondemocratic segments of civil society also have a say in the political process. Conservative religious organizations have influence legislation that touches on issues of religion, and they have even claimed a role in their implementation. In May 2014, members of the Front of the Defenders of Islam (FPI) attacked the house of a Catholic activist in Yogyakarta in order to stop a prayer meeting there, insisting that government regulations did not allow for such meetings in private residences.

Indonesian governments have traditionally shown little interest in truth and reconciliation processes, and the current administration of Joko Widodo is no exception. His predecessor, Yudhoyono, had systematically blocked attempts to deal with the anti-communist massacres of 1965 – 1966. The National Commission on Human Rights had recommended to Yudhoyono to issue an official apology for these crimes. Despite a promise to take this into consideration, Yudhoyono didn’t act on it until his term expired. He equally lacked in proaction on the establishment of the Truth and Reconciliation Commission. This commission was first created in 2004 but was annulled by the Constitutional Court in 2006, with the judges asking the government to draft a new law. In 2015, the government has not yet followed up on the court’s order. The failure to convene a national Truth and Reconciliation Commission has also hampered the creation of an equivalent commission for Aceh, as was mandated by the 2005 Helsinki peace accord between the Indonesian government and Acehnese rebel leaders. At the same time, the government has refused to establish human rights tribunals dealing with the involuntary disappearances of 1998, which involved high-ranking military officers. This refusal comes despite the fact that parliament requested just such a move in 2009, usually the first step in the establishment of tribunals. Overall, the Indonesian leadership’s
efforts to achieve reconciliation between victims and perpetrators of past injustice are poor, and there are so far no indications that President Widodo plans to substantially improve them. Indeed, some former military officers accused of human rights violations are now part of his government.

17 | International Cooperation

In the first decade of the post-Suharto transition, Indonesian governments made extensive use of international democracy and economic assistance. In fact, the key reforms undertaken by post-1998 governments – the electoral system, decentralization, the creation of the Anti-Corruption Commission, the establishment of the Constitutional Court and international trade policies, to cite just a few examples – were mostly designed along international models. But after Indonesia repaid its debt to the IMF in 2006, and after its economy grew stronger, the country adopted a more nationalist attitude toward foreign assistance and advice. Foreign donors were asked to have all their programs vetted by the Indonesian government, and a 2013 law on civil society organizations required all foreign NGOs to register with authorities and submit to control by government “partners”. More generally, Indonesia has also showed less interest in international best practices, especially under the government of Joko Widodo. For instance, the Widodo government started a campaign against food imports, claiming that the country can achieve self-sufficiency in the food sector by 2018. International experience shows that such efforts lead to an increase of prices, inefficiencies and corruption. But the government is responding to a rising nationalist and protectionist mood in society at large, suggesting the acceptance of international advice to be a politically risky matter. In line with this, Widodo also announced a foreign policy more focused on Indonesia’s national interest than on international engagement.

Politically, the international community considers Indonesia a credible and reliable partner. Indeed, many Western leaders (including U.S. President Obama and British Prime Minister Cameron) have been criticized in activist circles for excessively praising Indonesia’s progress and ignoring its shortcomings. For most Western countries, Indonesia is a tremendously successful example of a democratized Muslim nation. As a member of the G-20, Indonesia is no longer seen as an economic and political basket case, as was common in the late 1990s and early 2000s. That said, Indonesia’s new economic protectionism and nationalism have reduced its reliability as an investment destination. Investment firms and chambers of commerce, such as the American Chamber of Commerce in Indonesia, have regularly expressed their concern about the increasing legal and financial uncertainty associated with the rise of economic protectionism. The two biggest mining companies in Indonesia, Freeport-McMoRan, which mines copper and gold, and Newmont Mining Corp, another copper producer, temporarily stopped production because the government
imposed an export ban on unprocessed mineral ores in January 2014, causing both companies – and the Indonesian state – a damage in the tens of millions of dollars. Such cases have reduced Indonesia’s credibility and attractiveness as an economic partner, and given that the current government insists on continuing on its protectionist course, this credibility deficit is likely to persist for some time.

While Indonesia remains a driver of regional cooperation and integration in Southeast Asia, its relationship with its neighbors has deteriorated in recent years. When President Joko Widodo came to power in October 2014, he decided to initiate a new campaign against illegal fishing by scuppering a number of fishing boats from Thailand, Vietnam and Malaysia. This move has led to tensions in the relationship with all three nations, especially with Malaysia. Indonesia’s ties with Malaysia have been historically difficult because the high number of Indonesian migrants working in the country often complain about mistreatment, abuse and low pay. In September 2013, a demonstration by migrant workers took place in front of the Malaysian embassy in Jakarta to protest against the death sentence imposed on a migrant worker in Malaysia. Indonesia’s second most problematic bilateral relationship is that with Australia. While cordial and professional, the relationship is marked by important differences over the smuggling of refugees from Iraq, Afghanistan and Sri Lanka through Indonesia into Australia, and a variety of other issues. In November 2013, Indonesia withdrew its ambassador to Australia when it learnt of Australian spying operations focusing on then President Yudhoyono and his wife. Relations stabilized in May 2014. Despite occasional tensions with Malaysia and Australia, Indonesia has mostly maintained its strategy of de-escalation and cooperation, making it a significantly more trusted neighbor than in the 1960s, when it was widely perceived as a security threat.
Strategic Outlook

Indonesia faces a variety of policy challenges in the years ahead, but a number of key problems stand out. First, the 2014 elections have further underlined the urgent need for party and campaign financing reforms. Under the current system (i.e., almost no state subsidies for parties and no enforcement of oversight regulations), Indonesia’s policymakers have become dependent on oligarchic interests to fund their political operations. These policymakers include President Widodo, who partially relied on a number of tycoons to finance his 2014 campaign, and was then forced to accommodate them into his government. At the same time, legislators paid for their expensive campaigns either through loans from politically interested sponsors, or – if they were incumbents – through corruption and patronage. If this situation persists, there is little hope for a significant decline in corruption in the foreseeable future. Thus, Indonesia needs to consider the introduction of substantial and institutionalized state subsidies for parties and electoral candidates, aiming to mitigate predatory funding and lobbyist behavior. Obviously, such a system would not completely rule out corruption, but the experience of other countries at comparable stages of democratic development has shown that public financing – combined with strict oversight regimes - can reduce the dependence of parties on nondemocratic actors and narrow elite interests. Of course, these reforms need to go hand-in-hand with fundamental changes to the judicial system as well as continued support for the Anti-Corruption Commission.

A second priority for Indonesia is to begin a discourse on the importance of maintaining the democratic system. More than seventeen years after the end of authoritarianism, many Indonesians take the post-authoritarian achievements for granted, and do not seem to be concerned about the threat of a neo-authoritarian opposition. This was reflected in the paradox that most voters of the radical populist Prabowo, who had announced that he would roll back democratic reforms, professed to be strong supporters of democracy. The abovementioned corruption has led to a certain extent of apathy and disillusionment among many citizens; but the problem seems to run deeper. Before the 2014 elections, it was widely assumed that Indonesian society would not accept – and indeed, rise up against – a return to autocratic rule, but this can no longer be assumed with great confidence. For the first time since 1998, notions of abolishing the existing democratic system have become acceptable again, and pro-democracy forces have thus failed to develop an effective counter-discourse. These circumstances should also serve as a reminder to international development organizations, most of which suspended their democracy assistance programs some years ago, falsely assuming that a democratic system was fully consolidated.

Third, Indonesia must rethink some of its core economic strategies. The end of the commodity boom, and the serious impact it has had on Indonesia’s economy, highlighted the continued natural resource dependence of the country. Much of Indonesia’s impressive growth between the early 2000s and early 2010s had been fueled by skyrocketing commodity prices, rather than by an expansion of the manufacturing or service sector. Under President Widodo, Indonesia must develop an economy that grows through increase in manufacturing and services, independent of
fluctuations in the global demand for natural resources. In the same vein, Indonesia should reconsider some of its recent protectionist measures. While the government may rightfully renegotiate natural resource contracts signed in collusion between Suharto’s cronies and large foreign companies, many of its latest agricultural policies have not been to the benefit of the Indonesian consumers. Increased import and export taxes as well as reduced import quotas for certain commodities have increased inflation and undermined the purchasing power of the lower classes. Uncompromised self-sufficiency in the food sector seems unattainable, but the government is determined to continue on this path – with possibly serious consequences for the Indonesian economy.