

STRATEGY

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Joko Widodo's Indonesia Possible future paths



Peter McCawley

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Dr Peter McCawley

Peter McCawley is an economist who has worked on Indonesian and Asian economic issues for many years. He is currently a visiting fellow in the Indonesian Project, ANU. His most recent work in Indonesia (2011–2013) has been with the SEADI (USAID) project in Jakarta as an economic advisor in the National Planning Board (Bappenas). Earlier, on several occasions he worked as an adviser in the Ministry of Finance in Jakarta in projects with the World Bank and the Indonesian Ministry of Finance.

He has a PhD in economics from the ANU (1972). He later taught at Gadjah Mada University in Yogyakarta in the early 1970s before returning to the ANU and becoming head, Indonesia Project, ANU. In 1986 he joined AusAID as a Deputy Director General and later became an executive director on the board of the Asian Development Bank in Manila. He has worked as a ministerial adviser in Canberra to several Treasurers of Australia and has provided many articles to the Australian media. He was dean of the Asian Development Bank Institute in Tokyo in 2003–2007. He has written a number of books and numerous articles about the Indonesian economy and other aspects of Asian economic development.

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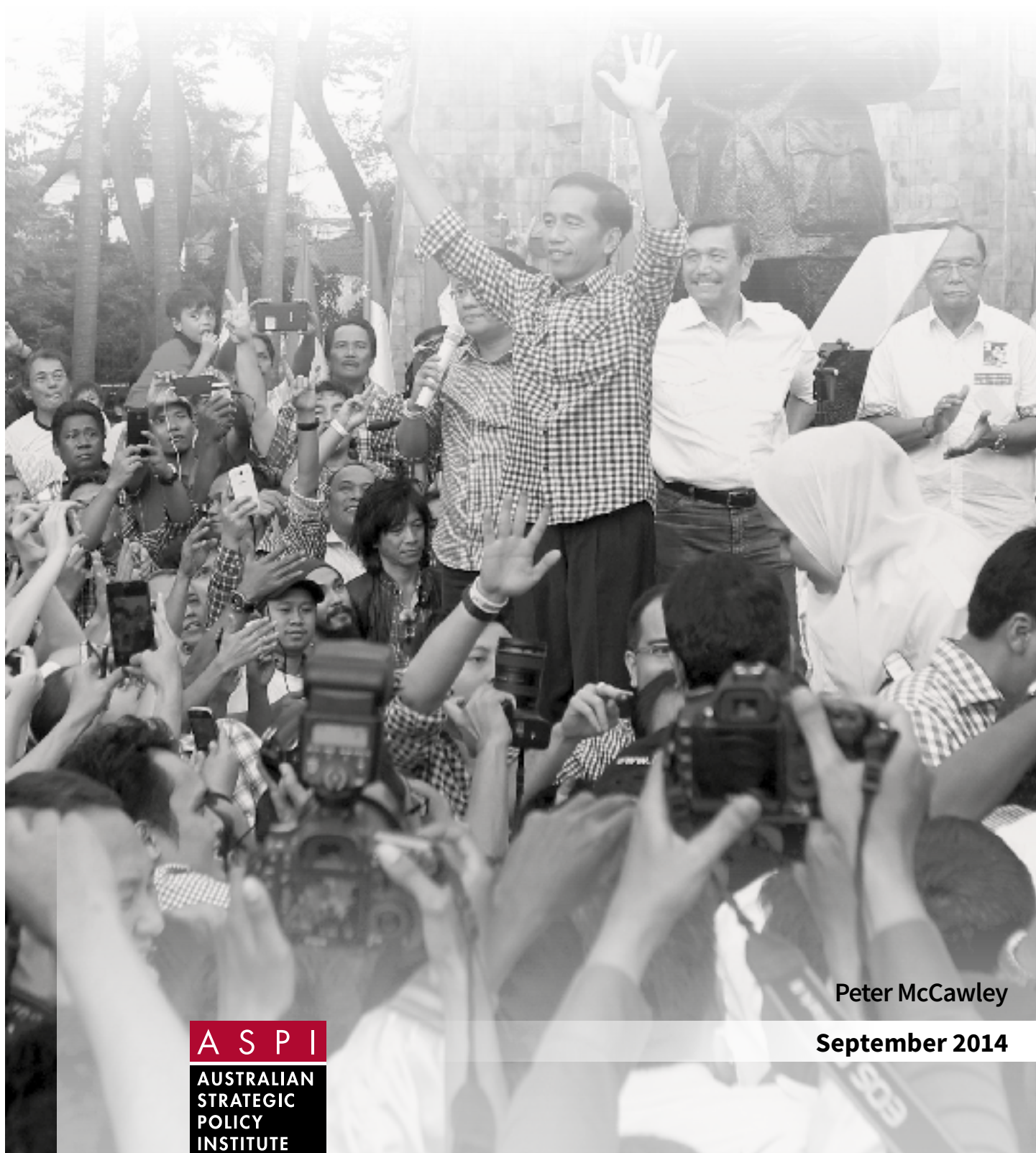
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Cover image: Presidential candidate from the Indonesia Democratic Party for Struggle Joko Widodo waves as he gives a speech in Jakarta, Indonesia, 9 July 2014 © EPA/BAGUS INDAHONO/Corbis.

Joko Widodo's Indonesia

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ASPI

Level 2,
40 Macquarie Street
Barton ACT 2600
Australia

Tel + 61 2 6270 5100
Fax + 61 2 6273 9566
enquiries@aspi.org.au
www.aspi.org.au
www.aspistrategist.org.au



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Late afternoon view of the CBD with building construction and office skyscrapers along Jalan Jend Sudirman, Jakarta © Martin Westlake/Asia Images/Corbis.

EXECUTIVE SUMMARY

With a population of around 250 million, Indonesia is the world's third-largest developing country. What's less well-known is that Indonesia is the de facto leader of ASEAN, a key regional grouping with a population of over 600 million people and a combined GDP (2012 PPP estimates) approaching that of India and Japan. Therefore, Indonesia's prospects to 2020 and beyond should be a central consideration for international policymakers considering likely trends in Asia during the decade ahead.

This survey looks at the possible paths for policy and development in Indonesia under the leadership of the seventh president of Indonesia, Joko Widodo, who will take office in Jakarta on 20 October. The first part of the survey is a stocktake of the challenges that lie ahead after 10 years of largely peaceful and progressive administration under the leadership of Indonesia's sixth president, Susilo Bambang Yudhoyono (SBY). The stocktake assesses the state of play in five areas: the political system; economic challenges; government and administration; social issues; and foreign affairs.

Then two possible scenarios of governance under the new administration are considered:

- An outward-looking *reform path* would be likely to be harder to implement in the short term but promises significant gains in the medium term.
- An inward-looking *resilience path* would perhaps be a more popular option with some powerful groups in Indonesia but would delay many urgently needed reforms.

President Joko Widodo will face a range of early challenges. He'll need to build good political support for his programs within Indonesia to be able to follow a reform path. And the economic challenges he faces are formidable. He has promised to try to reduce Indonesia's large energy subsidies, which are limiting fiscal policy, but that won't be easy. He has also identified the need to encourage investment, boost support for infrastructure development, and implement poverty-alleviation programs. Reform of government and administration will also be needed under a reform path. Widodo has often expressed his personal frustration with the delays and inefficiencies of the public sector in Indonesia. As president, the buck stops with him. It's now up to him to implement public sector reform.

In the area of foreign policy, he'll have little time to review issues before three major international meetings appear on his agenda. Within three weeks of his appointment, there'll be meetings of APEC in Beijing, East Asia Summit in Naypyitaw and the G20 in Brisbane. At those meetings, both he and the policies of the new government will come under close attention. The international community will have an opportunity to gain an early first-hand impression of the style of the new president and of the prospects for Indonesian economic policy under the new administration. Outward-looking statements in two areas would send a clear positive signal: a statement encouraging stronger economic growth by promoting investment and structural reform (not protectionism), and a statement in support of the growing role of ASEAN in regional cooperation programs.

But there's no guarantee that it will be easy for Widodo to implement reforms. He may find that there are considerable pressures on him to adopt a more inward-looking *resilience scenario*. Indeed, the new president might not find it easy to govern.

Widodo's position is difficult because, although he won the presidential election in July, the oppositionist pro-Prabowo Subianto grouping in the parliament appears to have a clear majority of seats after the legislative elections in April. Widodo may need to draw on all of his considerable political and negotiating skills to work with a parliament in which the majority bloc of votes is so unsympathetic to the administration.

The new president may also find it difficult to adopt economic policies promoting outwardly oriented economic growth. Recently, the overall rate of economic growth in Indonesia has been slowing. The Indonesian economy needs to grow at 6% or more per year to generate enough jobs to absorb new entrants to the labour force. But the current growth rate is trending downwards, at close to 5% per year. Somehow, Widodo needs to find ways to boost growth across the economy.

President Joko Widodo may also find that it's not easy to promote reform within government. Recent experience in Indonesia isn't encouraging. Proposed reforms set out in a law introduced by the SBY administration proved difficult to implement. Similarly, the incoming president has raised expectations among civil society groups. There are now wide expectations among activist groups that supported him that he will pursue 'pro-people welfare' programs. But the cost of implementing those programs is considerable, and the national budget is strictly limited.

In contrast to a reform-oriented foreign policy, a nationalist policy focused on domestic resilience could be less accommodating and more cautious about participating in ambitious international or regional plans. Many Indonesians would support an approach of this kind, maintaining that Indonesia can only hope to provide leadership across the region once the country has strong institutions and a strong economy.

At the end of a largely peaceful and progressive 10 years of administration under SBY, Indonesia's institutions have grown stronger, and its international standing has risen. The country's seventh president, Joko Widodo, will now need to decide whether to adopt an outward-looking reform program or to pursue a more inward-looking approach intended to promote resilience at home. Perhaps, depending on circumstances, he'll select policies that combine elements from both the reform and the resilience paths.

CHAPTER 1

Introduction

Indonesia, with a population of around 250 million, is the world's third-largest developing country. What's less well known is that Indonesia is the de facto leader of ASEAN, a key regional grouping with a population of over 600 million and a combined GDP (2012 PPP estimates) approaching that of India and Japan. Therefore, Indonesia's prospects to 2020 and beyond should be a central consideration for international policymakers considering likely trends in Asia during the decade ahead. But, for various reasons, international discussions about the rise of Asia and about the prospects for the 'Asian century' tend to slip quickly over both Indonesia and ASEAN. While it's understandable that the dramatic rise of the Chinese dragon and the Indian tiger have captured global imagination, closer attention to the emerging role of both Indonesia and ASEAN regionalism is needed as well.

This survey considers the possible paths for policy and development in Indonesia under the leadership of a new government. The first part of the survey is a stocktake of the challenges that lie ahead after 10 years of largely peaceful and progressive administration under the leadership of Indonesia's sixth president, Susilo Bambang Yudhoyono. Then two possible scenarios of governance under the new administration of Joko Widodo are considered. An outward-looking *reform path* would be likely to be harder to implement in the short term but promises significant gains in the medium term. An inward-looking *resilience path* would perhaps be a more popular option with some powerful groups in Indonesia but would delay many of the reforms still urgently needed.

Indonesia on the brink of change

In 2014, Indonesia is on the brink of change. In October, a new president, Joko Widodo (known by the nickname Jokowi), will be sworn into office. He's expected to hold office for five years until 2019 and perhaps serve a second term to 2024. The change of the presidency and administration is expected to bring about important changes across the country. It's clear from the recent history of Indonesia that the president's leadership matters. The leadership styles of the six presidents who've held office in Indonesia since independence was declared in 1945 have varied greatly. And so have many policies of the government, both at home and abroad.

The first president of Indonesia, Sukarno, was a flamboyant and charismatic leader who managed the political affairs of the nation with great skill for two decades after independence. But he was adventurous in foreign policy and challenged stability in the Southeast Asian region. He was also careless of economic policies and allowed Indonesian living standards to stagnate. The second president, Soeharto, governed the nation with a firm hand for three decades until the Asian financial crisis in 1997–98. Soeharto's style of leadership, which was cautious and deliberate, was very different from that of Sukarno. He supported policies that underpinned strong rates of economic growth but placed high emphasis on domestic stability, and he controlled political freedoms quite closely (see Wanandi 2012 for a vivid personal account).

Following the dramatic fall of Soeharto from the presidency in May 1998, three presidents held office in quick succession. President Habibie succeeded Soeharto for just over one year. In late 1999, the Indonesian People's Consultative Assembly (*Majelis Permusyawaratan Rakyat*) rejected Habibie's accountability speech, so he accepted that he should stand down. In the election in the Consultative Assembly that followed, Abdurrahman Wahid (known as Gus Dur) was elected as the fourth president of Indonesia, outmanoeuvring Sukarno's daughter, Megawati Sukarnoputri, for the position. Gus Dur was widely respected as a moderate and inclusive Muslim leader but was ineffective as president. Within two years, Megawati was able to push him aside and become president herself.¹ It was only after Susilo Bambang Yudhoyono (often called SBY) won office in 2004 in the first direct election for the presidency that there was again a prolonged period of stability in the office of the president of Indonesia.²

If presidential leadership—that is, the style, attitudes and political skills of the president—has made such a difference in Indonesia in recent decades, what challenges will Joko Widodo face when taking office in October this year? How much room to manoeuvre will the new president have, bearing in mind that the current Indonesian political system is rather similar to that of the US, where the president often faces opposition in the legislature in designing and implementing policy reforms? What are the key economic issues that the new president will face? Which social issues, of the many urgent matters that Indonesian citizens want to see addressed, is Widodo likely to be called upon to respond to quickly? What are the different strategies of government open to the new president?

CHAPTER 2

A stocktake

Indonesia has coped surprisingly well with a period of tumultuous change since the end of the Soeharto era in 1998. A stocktake of the state of the nation at the end of the SBY era can assess the state of play under five main headings: the political system; economic challenges; government and administration; social issues; and foreign affairs.

Political system

In 1999, at the beginning of the *Era Reformasi*, as the early post-Soeharto period is generally described, the Indonesian political system was in a state of remarkable flux. Some observers have argued that the sharp break with authoritarian political processes of the past opened an era of vigorous democracy in Indonesia (Witoelar 2002). Others have been more cautious, noting that Indonesia perhaps still needs ‘strong leadership’ to achieve important national goals.

Like political systems in other countries, the political system in Indonesia can usefully be seen as an industry. There’s a structure to the industry: there are ‘firms’ (that is, political parties); there are financial flows within the industry (often controversial) because revenues are needed to finance the activities of the firms and the supporters of the parties; and the firms set strategic goals and design products (just as corporations do) with the aim of expanding their role and increasing their power in the domestic political market. Furthermore, the firms vie with each other in a highly competitive political market to meet the demands of voters and other supporters who are active in the market.

The strengths of the political system as it has evolved in the past decade are considerable (Table 1). All of the main institutions and actors in the system (both organisations and individuals) acknowledge the importance of adhering to constitutional and other legal processes. In principle, at least, there’s an expectation that senior government and political leaders will commit themselves to making decisions that reflect the national interest. Public policy debate is very vigorous, both in legislatures and especially in the national media, and well-known public commentators and a wide range of specialists from the academic world and community groups are invited to contribute to public comment. The political system, too, is highly contestable, with numerous political parties competing to attract support in the political market. Reflecting the vigour of the political industry, legislatures at all levels of government in Indonesia (national, provincial and district) are active in asserting their authority in key areas of policy that come before them.

On the other hand, it’s widely acknowledged that (as in many other countries) the political system’s in need of reform in key areas (Aspinall & Mietzner 2010). While important parts of the Indonesian system are in a state of flux, other parts reflect enduring elements of social and political life that have been evident in Indonesia at least since independence (Feith & Castles 1970). For example, since independence Indonesia has had a multiplicity of parties. During the 1970s, Soeharto encouraged mergers of the various parties into three main groups—a functional group,

a nationalist group and a religious group. However, although the forced merger more or less existed for nearly three decades, it was never especially successful. And as soon as the *Era Reformasi* began after Soeharto's resignation, the number of parties swelled, reflecting various different groups and personalities (Aspinall & Mietzner 2010, Chapter 1). The result is that the structure of the current political system in Indonesia is rather fragmented. There are several large parties—none of which is able to dominate the processes of government alone—and a range of smaller parties that are usually quite willing to consider coalitions with the main parties, depending on the arrangements that might be agreed to.

Table 1: Political parties

Strengths	Weaknesses
<ul style="list-style-type: none"> • Most main actors acknowledge the importance of the rule of law and due process in such things as elections and appointments to senior political office, and are expected to observe the rules. • Public policy debate is very democratic: a wide range of views is presented in parliament and the media. • The system is highly contestable. There are several major parties and a wide range of smaller parties competing at most levels of government. • The legislatures (at all levels—national, provincial and district) are active and influential. 	<ul style="list-style-type: none"> • The political system is rather fragmented. There's a large number of small, fairly weak, parties and only a few large, strong ones. However, the various parties' methods of operation and often even their main ideas are rather similar; even the large parties often do not formulate clear policies on issues of national concern. • 'Money politics' is ubiquitous. Parties need substantial revenues, but in most cases neither their source of funds nor their accountability is clear. • The division of powers between the president (administration) and the legislature is somewhat uncertain and has been in flux since the end of the Soeharto era. • Elites (at all levels—national, provincial and district) are powerful. The result is that entry into political activity is not easy unless entrants are well connected.

Another feature of the political system in Indonesia (common in many other countries as well) is 'money politics' (Susanto 2014). The precise meaning of this term, widely used in Indonesia, isn't always clear. However, it's usually taken to imply that many of the important items allocated through the political system (such as senior party positions, seats in legislatures, senior government appointments, government contracts and commercial licences) are often for sale. In other words, the suggestion is that government allocations that should be decided through due processes and merit under the principles of good government and effective administration are instead 'marketised' and often bought and sold through the political system.

This causes many problems. For example, because it's widely believed that money politics is virtually ubiquitous across the political system, there's much cynicism about the political process and about political leaders in Indonesia. The marketisation of important parts of the government system both weakens the internal processes of government and contributes to widespread social disillusionment about the reliability and honesty of government.

The factors that underpin money politics in Indonesia aren't easy to deal with. First, the political parties are firms operating in a highly competitive industry and need substantial revenues to cover the costs of their operations (Sherlock 2010). The parties are expected to maintain headquarters, usually in Jakarta, and local offices across Indonesia; leaders are expected to travel frequently, often accompanied by a large entourage; and large party conferences, often held in upmarket hotels and attended by hundreds of delegates and guests, are expensive activities that are regarded as a necessary part of doing business for the parties. But the topic of political financing

isn't often addressed in Indonesia in a measured way. It's widely agreed that political financing is a problem, but few observers have identified any practical solutions to the issue.

Second, the rule of law is weak. The laws and regulations covering political financing are often vague. The rules leave a good deal of room for fundraisers and contributors to manoeuvre. Furthermore, the overall legal system is often ineffective. Attempts to enforce the laws are haphazard.³ In recent years, the well-regarded Corruption Eradication Commission (*Komisi Pemberantasan Korupsi*) has succeeded in having some high-profile political figures imprisoned after convictions for illegal fundraising. However, so far, the disincentive effects of the commission's work seem to have been limited.

Third, the rewards for buying and selling political favours are high, both for the individuals who arrange the deals and for the political parties that facilitate them. Without the kinds of financial deals that are regularly reported as taking place, a staff member in a political party or a middle-ranking public servant might expect to be able to earn an income of around \$5,000 a year. But it's clear, both from the lifestyles of some senior politicians and senior public servants and from media reports, that individuals actively involved in money politics have incomes of perhaps \$50,000 or more. Whatever the precise details (and reliable information is hard to come by), participants in money politics can sometimes hope to increase their incomes by a factor of ten or more. For many people, this is a strong incentive to enter the market, despite the risks that are attached to the activity.

Two other features of the current Indonesian political system are often seen as posing problems: the division of powers between the president (the administration) and the legislature, and the dominant role of elites.

Two other features of the current Indonesian political system are often seen as posing problems: the division of powers between the president (the administration) and the legislature, and the dominant role of elites.

In Indonesia, there's significant support for a strong presidency. Many citizens express the hope that the president will exercise firm leadership to address strategic issues. As a result, there are often calls for 'leaders with courage' and 'decisive leaders.' In the view of many commentators, the strong support that emerged for Prabowo Subianto, the losing candidate in the recent presidential election, reflected such yearning on the part of many voters.

In practice, many of the issues that citizens look to the president and other leaders to tackle (such as corruption, violence of various kinds, and worthwhile improvements to basic public services) aren't amenable to easy solutions. One major problem, taken up below, is the cumbersome nature of the bureaucracy. But another major problem is that—just as in the US—the President of Indonesia must often rely on the approval of the Indonesian People's Representative Council (*Dewan Perwakilan Rakyat*) to progress proposed policy measures. And just as the Congress in the US often chooses to amend proposals from the US President, so the parliament in Indonesia often wishes to review policy proposals from the Indonesian President in considerable detail.

The dominant role of elites—political, business (sometimes called 'oligarchs'), military, media and administrative—is another key feature of the Indonesian political system. The need to look for compromises across the different elites has been a challenge for presidents of Indonesia and their ministers since independence.

The Indonesian elites often interlink in various ways at the national and regional levels and wield considerable power. The real power of the Indonesian President and the cabinet is therefore often quite limited. Actors in the

political elite usually draw their power from their positions in political parties and are thus inclined to look to their parties for guidance when public policy is being considered. Since a significant proportion of cabinet ministers in Indonesia in recent years have been appointed partly because of party backing, the President can't always be sure of undivided loyalty, even within the cabinet.

As in many other countries, political power and business activities in Indonesia are often intermingled, especially because of the ubiquity of money politics.⁴ Aburizal Bakrie, one of Indonesia's most well-known business leaders, has been a dominant figure in the large Golkar party in recent years. It was widely expected that Bakrie would run for president in the 2014 election, until it became clear that there was little public support for his candidacy. Many other well-known national and regional business figures provided resources to political candidates and parties during the 2014 parliamentary and presidential election campaigns. Hashim Djojohadikusumo supported the presidential bid of his brother Prabowo Subianto; Surya Paloh is chair of the Nasdem Party, which supported Joko Widodo in the presidential campaign; Jusuf Kalla joined Widodo's campaign as the vice presidential candidate; and so on (some details are in Yogaswara 2008).

The military, too, continues to exercise considerable influence in Indonesia. The armed forces are a highly respected institution...

The military, too, continues to exercise considerable influence in Indonesia. The armed forces are a highly respected institution: public opinion polls indicate that, among government institutions, the military consistently ranks as among the most trusted organisations in the country. Although the military voluntarily agreed to withdraw from official representation in the Indonesian parliament as part of the reforms that followed the end of the Soeharto era, non-active military figures often occupy senior roles in government. President Susilo Bambang Yudhoyono rose to the rank of lieutenant general before being appointed to cabinet in 1999, and Prabowo Subianto, one of the two main presidential contenders in the recent presidential election, was also a lieutenant general in the army before he was discharged from service in 1998.

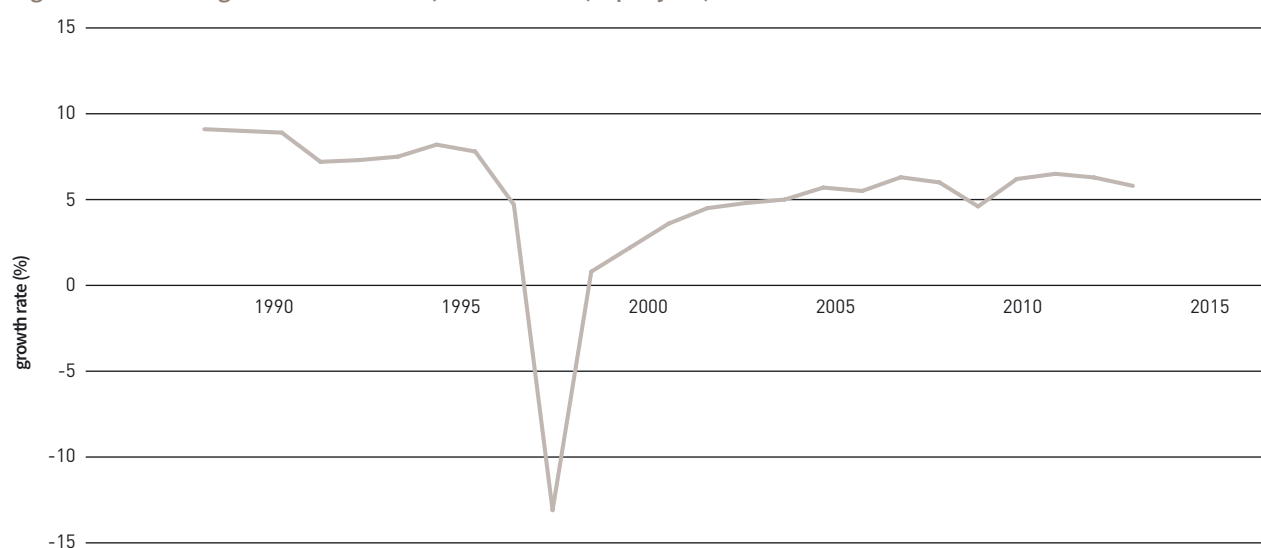
The media have become much more influential with the strengthening of democratic practices in Indonesia in recent years. While it's true that some business tycoons have developed strong market positions in some parts of the media, especially TV, other parts are highly competitive (Ahmad 2011). Politicians and political parties have been paying much closer attention to the need to project an effective media presence.

The Indonesian bureaucracy is also influential, so the president and cabinet of the day must develop managerial techniques to work with it as effectively as possible. In practice, senior political leaders in Indonesia often express considerable frustration with the sluggish responses that they say they experience in dealing with government officials. In turn, the officials point out the realities of administration in Indonesia: that many government agencies must exist on shoestring budgets; that, while officials are rightly expected to follow regulatory procedures in their daily jobs, many of the rules and regulations that govern the bureaucracy are excessively complex and in some cases almost unworkable; and that most of the citizens who live and work in the informal economy often largely ignore government procedures anyway.

Economy

The 1997–98 Asian financial crisis imposed very severe costs on the Indonesian economy. Before the crisis, the economy had been growing strongly around 7% per year. After the crisis, it took almost a decade for growth to return to around 6% (Figure 1), and it hasn't improved much since. For reasons that aren't clear, it seems that the economic 'speed limit' of the economy is now constrained at around 1% less than was possible before the crisis.

Figure 1: Economic growth in Indonesia, 1989 to 2012 (% per year)



Source: Asian Development Bank, *Key Indicators*, accessible at www.adb.org.

Nevertheless, a sustained annual economic growth rate of 6% is hardly disappointing. From this point of view, the economy was well managed during most of the second term of SBY's period in office. This performance reflected a favourable external environment along with good domestic monetary management and a disciplined approach to fiscal policy (Table 2).

So far, so good. But recently—since around mid-2012—some worrying signs have begun to appear. The most noticeable change in overall economic performance during the past two years has been a marked slowing in the growth rate (Figure 2). The overall annual growth rate, which was comfortably over 6% during 2011, began to ease downwards. Most recent data for early 2014 suggests that the economy is now growing at just over 5% a year.⁵ Many observers would prefer to see growth moving back towards 7% a year on a long-term basis (ACDGI 2013).⁶

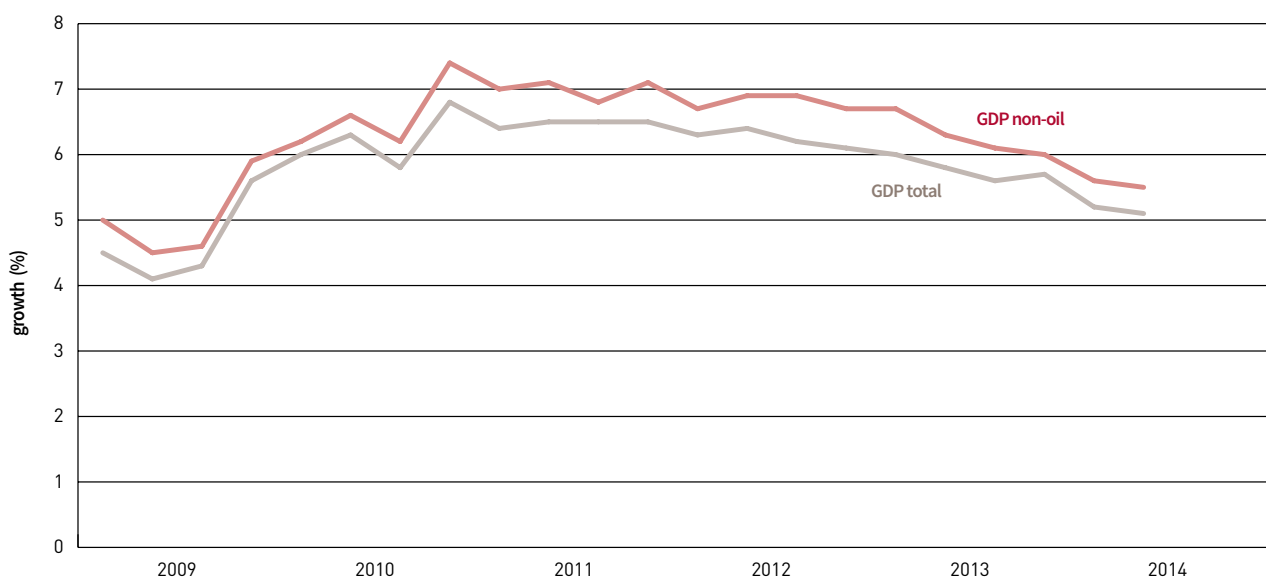
A strong growth rate of at least 6% is needed to create enough jobs for the expanding labour force and to combat poverty. The level of overall poverty edged steadily downwards during the past decade, to include less than 12% of the national population at the end of 2013. But the official poverty line is a harsh measure of less than \$1.00 per day. Even modest increases in the poverty threshold lead to much larger numbers of people being recorded as poor; if \$2 per day were used as the threshold, almost 50% of Indonesians would be classified as poor.

The recent slowing in growth is therefore one of the key economic challenges that Indonesia's new president will need to address upon taking office. One factor contributing to the slowdown appears to be difficulties that have emerged in the balance of payments. For a range of reasons, exports have weakened somewhat during the past few years while imports have remained quite strong. The balance on the current account, which had been in surplus, has thus moved into deficit. The authorities responded appropriately by allowing the foreign exchange rate to adjust (that is, to depreciate), but this hasn't been enough to reverse the deficit on the current account.

Table 2: Economic issues

Strengths	Weaknesses
<ul style="list-style-type: none"> Sustained recovery from the 1997–98 Asian financial crisis and strong economic growth in recent years. Highly flexible domestic market structures in many parts of the large informal economy in such sectors as agriculture, small-scale industries, many local service industries, and labour markets. Flexibility in monetary policy, including in allowing the foreign exchange rate to adjust in response to balance-of-payments pressures. Careful management of fiscal policy, reflected in consistently low budget deficits. Highly disciplined reduction of national debt in the decade following the Asian financial crisis. A boost to growth from strong terms of trade in recent years. Widespread opportunities to lift productivity. 	<ul style="list-style-type: none"> Widespread poverty, which, among other things, contributes to the challenges of economic management in most sectors of the economy. A slowing in economic growth since 2012, reflecting a lack of policy response to external pressures on the Indonesian economy. Continuing difficulties in some key aspects of fiscal management, such as curbing fuel subsidies. Marked supply-side problems in some sectors, especially the manufacturing, mining and oil industries. Low levels of investment in infrastructure, contributing to supply-side challenges in other sectors. A need to adjust to a deteriorating external economic environment since 2012. Sluggishness in taking advantage of opportunities to boost efficiency.

Figure 2: Economic growth in Indonesia, by quarters, 2009 to 2014 (% per year)



Source: Government of Indonesia, Central Bureau of Statistics, *Pertumbuhan Ekonomi Indonesia* [Indonesian Economic Growth], quarterly publications, accessible at www.bps.go.id.

In fact, a sustained deficit on the current account wouldn't necessarily be a problem, provided that Indonesian policymakers could be confident of access to international capital markets at reasonable interest rates.⁷ But those markets have sometimes been volatile, especially after the global financial crisis of 2008–09. In mid-2013, a number of developing countries in Asia, especially India and Indonesia, experienced sudden unexpected outflows of capital when international markets reacted to a possible change in monetary policy in the US (a 'tapering' of policy) by withdrawing capital from emerging markets. This so-called 'taper tantrum' exerted sharp pressure on the foreign exchange rates in countries hit by the outflows (Klemm et al. 20).

Indonesian policymakers also face a range of other challenges in finding ways to lift the economic growth rate towards the 7% mark.

But Indonesian policymakers also face a range of other challenges in finding ways to lift the economic growth rate towards the 7% mark. First, although fiscal policy has been conducted in a disciplined way in an overall sense, there are well-known problems of implementation on both the income and the expenditure side of the Indonesian budget. On the income side, revenues (currently around 16% of GDP) are far too low; on the expenditure side, fuel subsidies (currently running at around \$30 billion a year) are inequitable and are crowding out other much-needed spending (IMF 2013). One view is that a new president will be able to tackle these fiscal problems with new determination in a way that wasn't possible for SBY in his second term. Another view is that the resistance to fiscal reform will be strong and that populist opposition in the parliament will frustrate policy change.

A second major problem is the need to promote infrastructure spending. National spending on infrastructure (public and private sector combined) is clearly too low. For more than a decade since the 1997–98 crisis, investment in infrastructure in Indonesia has trended around 3% or 4% of GDP. This is significantly lower than the 7% level widely regarded as necessary to support a strong economic growth rate (World Bank 2013). It won't be easy for policymakers to overcome the various bottlenecks choking off higher investment in the infrastructure sector. Much more effective coordination of policy across government at both the national and the regional levels will be needed than has apparently been possible in recent years (ACDGI 2013, Chapter 3).

Third, a range of other issues need to be tackled to stimulate higher growth. Key sectoral challenges include revising policy to encourage significantly increased investment, including foreign investment in the oil and mining sectors, finding ways to encourage growth in lagging manufacturing industries, and facilitating expansion in promising service industries. A set of policies to tackle these and other matters is being prepared for inclusion in a new draft National Medium Term Development Plan (*Rencana Pembangunan Jangka Menengah Nasional*) for the five years to 2019. The new plan will become official policy after it's considered by the incoming president in late 2014.

From one point of view, the long agenda that needs to be worked through to promote higher growth is very daunting. Some observers find it hard to be optimistic. A recent survey prepared by a team from the Harvard Kennedy School (ACDGI 2013) points to many difficulties and argues that a set of transformative policies is needed to move Indonesia onto a higher development trajectory. But from another point of view, the potential for sustained growth in Indonesia is promising. Productivity in many economic sectors in Indonesia is still low by world standards, suggesting that opportunities for rapid productivity growth are there for the taking. Furthermore, many domestic markets in Indonesia are extremely flexible, especially in the informal economy, which is often estimated to include over 60% of the Indonesian labour force. Free movement in these markets, sometimes almost entirely unregulated,

gives the Indonesian economy a flexibility denied to markets in Europe (sometimes described as 'sclerotic') and other developed countries.

It's true that the economic flexibility in Indonesia's informal economy has downsides (regulatory standards are often ignored and risks are often high). But the upside is that resources can shift rapidly between sectors in response to changing market circumstances in a way that makes OECD economies look very cumbersome. Informality has important benefits as well as significant costs.

It's widely recognised in Indonesia that government processes, and the operations of the bureaucracy, aren't satisfactory.

Government and administration

It's widely recognised in Indonesia that government processes, and the operations of the bureaucracy, aren't satisfactory (Mardiasmo et al. 2008). There's almost universal agreement that reform is needed (Effendi 2011, 2013). Critics point (constantly) to many well-known problems with the bureaucracy at all levels of government: the bureaucracy's widely regarded as unresponsive; processes are cumbersome; everything takes too long; payments are often needed to move documents forward; and the results of all of this are very disappointing. Clearly, there are major problems with public sector delivery in Indonesia (World Bank 2012, Olken 2013).

In principle, sustained efforts are being made to tackle these issues (Table 3). There have been many studies of problems in public sector delivery in Indonesia (Effendi 2010). Many programs aimed at introducing improved management practices in the public sector have been introduced in government departments and agencies at the national and regional levels. In many departments, detailed and transparent internal guidelines have been issued to staff to define the rights and responsibilities of public servants.⁸ There's no shortage of suggestions about the measures needed to improve public sector management (Table 4).

Many of the suggested activities incorporate most of the main well-known aspects of public sector reforms listed in OECD countries' public sector programs. Many programs in Indonesia are supported by the clear definition of goals, steps for the implementation of activities are spelt out, measurable performance indicators are listed, and time-bound targets are laid out. In principle, government processes are usually designed to minimise the scope for arbitrary discretion on the part of officials.

But the downside is that the severe resource constraints that government agencies face are often not allowed for. In practice, many agencies, especially at the regional and local levels, are severely cash-strapped. For example, government spending at the provincial level in 2010 outside Jakarta was an extraordinarily low \$40 per capita (calculated from CBS 2012). It's barely possible for governments to provide significant services when budgets are so limited.

Table 3: Government and administration

Strengths	Weaknesses
<ul style="list-style-type: none"> There's widespread recognition in Indonesia that bureaucratic processes aren't satisfactory and that reform is needed. Many efforts to introduce better management practices (such as setting and monitoring key performance indicators for government agencies) are underway at all levels of government across the country. In principle, government processes are rule-driven and are designed to minimise the scope for individual and arbitrary discretion on the part of officials. The codification and clarification of government processes is continuing at all levels of government, with the aim of making government more efficient, more transparent and fairer. The overall transparency of government is increasing. More public reports with better data are being released, and regular community consultations with stakeholders about government policies are commonly held. Government departments and agencies are increasingly responsive to legislatures. 	<ul style="list-style-type: none"> There are severe resource constraints on government agencies at all levels. Budgets are often extremely limited, and many agencies have problems with the number and quality of staff. The legal system is quite weak. Legal institutions (courts, police, private legal practices) are severely under-resourced, so that in practice much of the system is dysfunctional. Efforts at bureaucratic reform have proceeded slowly, often meeting resistance both inside and outside of the bureaucracy. Corruption is widely acknowledged as a major problem: links between power-holders and donors are widely believed to favour powerful commercial actors at the expense of the public interest. There's too much red tape. There are so many rules and regulations that staff are often obliged to look for ways to bend them, undermining due process. There's little emphasis on evaluating results or providing incentives for officials that reward them for results. Processes of disclosure and transparency, although improving, are still often unsatisfactory.

Another serious problem is that the Indonesian legal system is weak (Lev 2000). The problem begins at the top, where the Indonesian Parliament passes only a very small number of bills each year. The legal system is underfinanced, overburdened with demands on courts and supporting infrastructure, and mostly staffed by judges, court officials and administrators on low salaries.⁹ There are more than 6,000 judges in Indonesia but many of them work for low official salaries and even need to look for additional sources of income, such as lecturing in local universities, to supplement their incomes. In 2012, the Indonesian Judicial Commission suggested that an acceptable salary for judges might be around Rp7 million per month (around \$700 per month at the time) and noted that, in practice, many judges received rather less than that in official payments.¹⁰

The weakness of the legal system has widespread consequences. One is that many actors in Indonesia—in the private sector, in the bureaucracy, in civil society, and in the political system—look for extra-legal ways to settle disputes. Those methods include reliance on informal interventions by senior figures, such as military or policy officials and respected religious leaders, payments between disputing parties, and the recruitment of local gangs who offer their services for hire. Another consequence is that many commercial activities are carried on in a vague legal environment in which the law of contract is often rather uncertain and it's often difficult to settle such matters as whether a party to a contract is solvent or not. Indonesian firms often find practical ways of operating in this environment, while foreign investors find it hard to cope with the legal uncertainty.

Table 4: World Bank proposals for public sector reform in Indonesia**Key messages of public sector reform in Indonesia**

Indonesia needs to continue to modernize its civil service and build upon the impressive governance, policy, and public finance management reforms of the past decade. A number of structural, organizational and institutional policy reform issues to be addressed over the next five years are as follows:

1. *Reform the existing pay/grading scheme:* Replace the current system, which is characterized by low basic pay and numerous allowances, with a single pay structure with greater transparency linking remuneration to performance, and harmonized salary levels across the public sector.
2. *Modernize the civil service pension plan:* Replace the current defined benefit, pay-as-you-go system with a prefinanced defined contribution scheme.
3. *Strengthen staffing controls* in order to rein in the on-going expansion of the civil service and its administrative budget implications.
4. *Allow flexible organizational design and staffing* to provide for structures and staffing levels based on real operational needs rather than standardized 'policy' requirements.
5. *Reform civil service HR policies* to provide for a modernized, more flexible system and a professional, performance-oriented work force.

Source: World Bank, *Indonesia rising*, 2009

A third consequence is that it's difficult for the bureaucracy to operate effectively under significant legal uncertainty. In recent years in Indonesia, the work of anticorruption agencies such as the Corruption Eradication Commission has led to high-profile prosecutions of many senior politicians and officials. As a result, many government officials have become increasingly risk-averse and cautious in their decisions. After all, if the law is vague and if there's a risk of prosecution after controversial decisions, the safest thing to do is to avoid making decisions.

Another major problem affecting the processes of government and administration in Indonesia is that efforts at bureaucratic reform have proceeded rather slowly. In the early years of SBY's second term, in 2010 and 2011, there was talk of a program of bureaucratic reform. But the plans for reform reportedly ran into considerable resistance within the bureaucracy and within parliament (Parlina & Atmanta 2013). Nevertheless, the approval of an important new Civil Service Law in early 2014 (Law No. 5 of 2014) opened the way for substantial reforms (Effendi 2014). In principle, the incoming Widodo administration will be able to move forward with a program to promote performance-oriented outcomes in the government sector.

Social issues

Since the transition to the *Era Reformasi*, social acceptance of democratic expression and openness to a wide range of views about social issues have increased dramatically in Indonesia (Table 5). In many respects, Indonesia's now a very pluralistic society. Most people in elite positions believe in the principles of flexibility and tolerance, and that those principles, combined with loyalty to the idea of Indonesia, help hold the diverse nation together. The national motto, *Bhinneka Tunggal Ika* (Unity in Diversity), is more than just a motto: it captures the acceptance of diversity found across Indonesia.

Of course, unsurprisingly in a nation of more than 250 million people, there are notable instances of intolerance. The rights of minority groups aren't always respected, especially at the local level when local disputes flare up. The state doesn't always step in to provide protection when there are reports of infringements of rights. International comment on these issues is reflected in the annual *Human rights reports* prepared by the US State Department. In February 2014, Secretary of State Kerry submitted to the US Congress the 2013 annual report, which contained comment about issues in Indonesia as well as many other countries.¹¹

But those issues are hardly ignored within Indonesia. There’s vigorous public debate about civil liberties in the media and in civil society. Government authorities are often sharply criticised for failing to act when there have been apparent breaches of liberties. Indonesian citizens, often acting with the support of important community organisations, vigorously debate what measures are needed to strengthen human rights. The vitality of that debate is one of the defining characteristics of public life in Indonesia since the transition to the *Era Reformasi*.

Community, religious, social and academic groups are very active, as are trade unions when issues touching on labour rights are being discussed. And the volunteer (*relawan*) movement was widely credited as having played a vital role in supporting Joko Widodo in the recent presidential election. Indonesia in 2014 is a country with very wide freedoms.

Paradoxically, the relatively light presence of the state is one of the factors contributing to freedom in Indonesia.¹² While it’s true that the state sometimes fails to provide protections that minority groups look for, it’s also true that the state isn’t especially intrusive on the lives of ordinary citizens. This isn’t necessarily because state agencies lack the will to intervene, but because their limited resources mean that they can’t. In practice, officials adopt a live-and-let-live attitude towards the activities of citizens, the bulk of whom carry out a great deal of their activities in the informal economy. Local authorities hope that citizens won’t disturb the peace. Provided citizens don’t do so, much of the time officials are happy enough to enjoy a quiet life.

The other side of the coin is that civil society groups are, like the state, often unable to find solutions to difficult community problems or provide protection to vulnerable groups. Many civil society groups aren’t well organised. Most operate with restricted budgets and can only provide modest salaries. Furthermore, the extreme diversity of civil society means that confused and sometimes contradictory messages are presented. And many activists in civil society groups tend to be self-selected, so it’s not clear how representative they are. The most effective groups are often based in Jakarta or other main urban areas and have effective links with the media. Minority groups in rural areas or in outlying provinces find it hard to make their voices heard. Sometimes, they’re affected by serious neglect or outright violence.¹³

Table 5: Social issues

Strengths	Weaknesses
<ul style="list-style-type: none"> • Indonesian society is generally tolerant and accepting of religious, ethnic and social differences. All main national institutions endorse ideals of tolerance and, with some notable exceptions, principles of pluralism are widely accepted. • The media is strong; social issues get wide coverage in the public media. • Community, religious and social groups are quite influential. Religious groups, particularly, are recognised as important players in the public policy debate. • Civil society groups such as trade unions, commercial groups, student groups and other organisations are recognised as important participants in the public policy debate and get a good hearing in the media and in the legislatures. 	<ul style="list-style-type: none"> • Civil society groups are sometimes not well organised. Confused and diverse advocacy messages are presented to the public media. • It’s sometimes not clear how representative civil society groups are. Some activists appear to be self-selected and not really representative of the groups they claim to represent. • There’s such a large number of civil society groups that the sector sometimes appears to be quite disorganised. • Minority groups, especially religious minority groups and ethnic groups in outlying provinces, sometimes don’t get adequate protection for their legitimate activities. There have been some quite serious abuses of the rights of minority groups.

Foreign affairs

Indonesia's foreign policy since Sukarno's declaration of independence in 1945 has shown some marked continuities. With the notable exception of the tumultuous approach to policy during the adventurous period of the Sukarno presidency (1945–1966), Indonesian presidents have generally been cautious in international affairs and have tended to rely on a well-established emphasis on a 'free and active' approach to foreign policy (Table 6). The broad outlines of the first 50 years of Indonesian foreign policy were recently summarised by Jusuf Wanandi, a close observer of and participant in policy affairs in Indonesia:

Sukarno was flamboyant and outgoing and had a similarly outsized reputation abroad; Suharto did not, at least for the first 20 years. Suharto just did not have the personality for international relations. He was shy, inward-looking, very Javanese and indirect ... [D]espite leaning towards the West, the basic non-alignment foreign policy he inherited from Sukarno remained. The Foreign Ministry was steeped in the thinking that in the implementation of policy, some freedom and independence would always be maintained, whatever the circumstances the country faced. Because in the end Indonesia's foreign policy, based on non-alignment, meant in practice the freedom to choose. (Wanandi 2012:265)

Since the mid-1970s, an emphasis on working with ASEAN partners has been a central feature of Indonesian foreign policy.

Table 6: Foreign policy

Strengths	Weaknesses
<ul style="list-style-type: none"> • Clear and well-established emphasis on a 'free and active' foreign policy. • Firm and longstanding emphasis on maintaining a non-aligned position. • Experience in weighing Indonesia's interests carefully in response to various proposals from the major international powers in Asia. • Strong bonds with ASEAN; Indonesia plays a leadership role in the region. • Long and well-established institutional experience of the Indonesian Ministry of Foreign Affairs, staffed by very experienced senior diplomats. • Effective connections with multilateral agencies such as the International Monetary Fund, the World Bank, the UN and the Asian Development Bank. 	<ul style="list-style-type: none"> • An emphasis on non-alignment and a preference for a consensual approach, including within ASEAN, which sometimes masks efforts to define Indonesia's own interests clearly. • An inclination to look to multilateral institutions for support, which can dilute bilateral messages from Indonesia. • Financial and other resource constraints, which sometimes restrict the effectiveness of Indonesian diplomacy. • Urgent domestic issues often limit the attention that Indonesian leaders can give to international affairs.

Consistent with the power with which medium-sized developing countries can usually support their interests, Indonesia has often given priority to regional and multilateral diplomacy rather than bilateral diplomacy to respond to international issues.¹⁴ As just one example, in responding to unauthorised boat arrivals in Australia from late 2013, the Australian Government has tended to rely on bilateral relationships to discuss possible approaches with neighbouring countries. In contrast, Indonesia has indicated a clear preference for dealing with the issue through the Bali Process established in 2002 to provide a regional framework for dealing with people smuggling, transnational crime and associated issues.¹⁵

Building regional strength and influence through support for the development of ASEAN has been a key part of Indonesia's approach to diplomacy for over four decades. At first, during the first decade or so of attempts to build cooperation in the region within ASEAN, progress appeared to be slow. In international circles, the cautious 'ASEAN way', which emphasised consensus and careful mutual respect for the different systems of government and values across Southeast Asia, was sometimes regarded as rather ineffective. But ASEAN has slowly emerged to become a very successful regional organisation. The total population in ASEAN is now more than 600 million, and its GDP (PPD) will soon be over \$4 trillion (Table 7). Provided current programs of effective cooperation are sustained, the prospects for ASEAN are encouraging.

Table 7: ASEAN Key Statistics, 2012

	Mid-year pop. 2012 (mill)	%	GDP (PPP) 2012 (US\$b)	%	GDP (PPP) per capita US\$	Index
Indonesia	247	40	1,223	33	4,947	82
Philippines	96	16	427	11	4,457	74
Vietnam	89	14	355	10	3,998	66
Thailand	64	10	692	19	10,745	177
Myanmar	61	10	110	3	1,803	30
Malaysia	29	5	501	13	17,099	282
Cambodia	15	2	37	1	2,500	41
Laos	6	1	19	1	2,923	48
Singapore	5	1	328	9	61,887	1,022
Brunei	0.4	...	22	1	55,000	909
TOTALS	613	100	3,714	100	6,054	100
Comparator countries						
China	1,354		12,471		9,210	
India	1,213		4,793		3,950	
Japan	128		4,491		35,196	
Australia	23		1,008		44,405	

Note: PPP = purchasing power parity.

Source: Asian Development Bank, annual *Key Indicators*.

Several implications flow from the Indonesian authorities' inclination to rely on regional and multilateral channels in conducting international diplomacy. The advantage is that much of the detailed administrative work of negotiations is passed over to regional and international agencies; the disadvantage is that Indonesian representatives can find it hard to keep up with the flow of manoeuvres when there's rapid progress in negotiations. And if Indonesia is expected to reflect the views of the ten ASEAN countries (as is sometimes the case), its own interests can sometimes be diluted in the broader ASEAN framework. A final challenge for Indonesian diplomacy that has become increasingly important in recent years is ensuring that Indonesia can fully participate at the leadership level at international meetings such as APEC, the East Asia Summit and G20 conferences. The incoming President of Indonesia will find the international conference schedule quite pressing as soon as he takes office on 20 October. In early November, there will be heads-of-government APEC, East Asia Summit and G20 conferences where there will be opportunities for him to outline his government's foreign policy priorities.

CHAPTER 3

The period ahead

What are the prospects for Indonesia over the next five years, as a new president takes office? It's helpful to consider two scenarios that, depending on events, Indonesia might follow during the next five years: a *reform scenario* and a *resilience scenario*.

Of course, other scenarios are possible. The recent Harvard Kennedy School study suggested that it's useful to consider three possible paths: a *reactive* path, a *proactive* approach, and a *transformative* set of policies (ACDGI 2013). The study described the reactive path as best reflecting the Indonesian Government's current approach of tending to 'muddle through'¹⁶; the proactive approach refers to the government's practice of tackling reform mainly as a response to a major crisis; and the transformative set of policies characterises the energetic reform approach seen, for example, in the past half-century in the four 'Asian tigers' (South Korea, Taiwan, Hong Kong and Singapore). The Harvard study considered these possible paths partly so that desirable sets of policies might be identified.

The two *reform* and *resilience* scenarios are taken as benchmarks for more optimistic and more problematic paths that Indonesia might follow during the five-year term of the incoming president.

Rather than suggesting specific policy options here, the two *reform* and *resilience* scenarios are taken as benchmarks for more optimistic and more problematic paths that Indonesia might follow during the five-year term of the incoming president.

Reform scenario

Not surprisingly, after the vigour of two extremely competitive political campaigns in Indonesia (for legislatures across Indonesia in early April and for the presidency in early July), high hopes are widely held for a new president. Those high expectations pose problems for President Joko Widodo. After speaking of many bold reforms during the election campaign, he risks coming to be seen as overpromising and underdelivering.

Widodo has had no experience as a minister or as a member of cabinet. His time in administration in Indonesia has mainly been spent as the mayor (*Walikota*) of Surakarta, a middle-sized town in Central Java, from 2005 to 2012. He's widely credited as having been a successful and popular mayor who introduced significant reforms in Surakarta. But it remains to be seen how effectively that experience, combined with the short time he spent as Governor of Jakarta from 2012, will carry over as he responds to the much wider challenges that he must deal with as President of Indonesia.

Politics

The new president will face early political challenges on several fronts. He'll need to focus his attention on several important issues.

First, his relations with the main party that supported him, the Indonesian Democratic Party of Struggle (*Partai Demokrasi Indonesia—Perjuangan*, PDI-P), are said to be under some strain. From one point of view, it seems remarkable that the leaders of the PDI-P, including former president of Indonesia Megawati Sukarnoputri, show any reluctance in demonstrating wholehearted support for their chosen candidate. After all, Joko Widodo has delivered the presidency to the Democratic Party, along with all of the powers and opportunities for patronage that go with the position. But from another point of view, the nagging worries that the traditional elite within the PDI-P have about their relations with Widodo after his victory are perhaps understandable. As president, Widodo will take on all of the authorities of the presidential office and will have less immediate need for support from the party. And lately he's been showing worrying signs of independence. Senior leaders in the PDI-P are said to be uncertain about whether Widodo will pay enough attention to the interests of his erstwhile supporters once he becomes president. Just as Falstaff found that Prince Hal soon regarded former ties as less useful once he became Henry V,¹⁷ so the leaders of the Democratic Party are wondering how strong Widodo's ties to the PDI-P will be once he takes office.

The second major political challenge that Widodo will face as president is in managing relations with the parliament, which won't necessarily be easy. In recent years, the parliament has repeatedly held up and amended proposals sent to it by the administration. During the past decade, parliamentary committees have often exercised their right to call ministers before them to discuss matters of government policy in detail, sometimes for hours on end. In practice, the parliament has very wide powers. In principle, it can even consider the impeachment of the president in the way that the senior chamber, the *Majelis Permusyawaratan Rakyat* (People's Consultative Assembly) decided on the impeachment of Abdurrahman Wahid (Gus Dur), in 2001. For these reasons, the Indonesian President has little choice but to take care in considering relations between the administration and the legislature.

If Joko Widodo manages these relationships well in the early months of his presidency, the prospects for strong and effective government in Indonesia are good. He has already demonstrated impressive political skills. It's possible that he'll emerge as a highly effective leader. In retrospect, it's hard to avoid the impression that he may have had his eye on the presidency soon after winning the governorship in Jakarta in September 2012. If so, he hardly put a political foot wrong during 2013. He took maximum advantage of the access to national publicity that comes from being Governor of Jakarta and handled his media contacts with much skill. Day after day, for months on end, he got wide and very positive coverage in the print and electronic media for his populist, open-necked visits to poor areas across Jakarta to chat to poor people in markets, in alleyways and along river banks. This *blusukan* approach,

as it's known, became his trademark. It was immensely popular, not just in Jakarta but across much of the rest of Indonesia.

Widodo steadily built up momentum as a possible presidential candidate throughout 2013. By early 2014, the leaders in the Democratic Party were under considerable pressure to fall in behind him—and on his terms. For months, the key decision-maker in the PDI-P, Megawati Sukarnoputri, dithered over whether to anoint Widodo as the party's preferred candidate. There were many reports suggesting that she was considering a tilt at the presidency herself (this would have been the fourth time that she had made a bid for the presidency, following earlier unsuccessful attempts in 1999, 2004 and 2009) or, perhaps, supporting her daughter, Puan Maharani. In the end, Widodo got his way. He made it look easy, but he had carefully manoeuvred himself into a position in which the elite of the Democratic Party had little option. They desperately wanted a firm PDI-P hold on the presidency after languishing in opposition for a decade. Widodo, who was widely identified with the Democratic Party, seemed to be promising them victory in the presidential elections. What choice did they have? The old PDI-P elite swallowed their pride, recognised the strengths of the newcomer from Surakarta, and urged Megawati to recognise the facts of political life.

If Widodo, as president, can manage relations with the parliament as effectively as he has managed relations with the PDI-P, the prospects for effective government in Indonesia are good.

If Widodo, as president, can manage relations with the parliament as effectively as he has managed relations with the PDI-P, the prospects for effective government in Indonesia are good. But it seems likely that he'll face significant challenges. The upshot of the combined legislative and presidential elections in 2014 leaves him in an uncertain position in dealing with the parliament. On one hand, he has (as his predecessor, SBY, had) a good personal mandate from the electorate. On the other hand, the combined oppositionist groups that supported Prabowo Subianto in the presidential election have a comfortable majority in the legislature. If luck runs his way, as he settles into the presidency he may find that a useful portion of the oppositionist groups decide that it would be best to get with the strength and work with him in the parliament. If Joko Widodo can gain support in this way, the processes of government in Indonesia will be more secure.

Economy

The most urgent economic challenge facing the incoming president is the need to promote economic growth. As part of his presidential campaign proposals, Widodo mentioned a target rate of economic growth of 7% per year. If he can introduce a package of policies to accelerate growth towards that level, then his position as a reform president will be significantly enhanced.

The broad set of policies needed to lift economic performance in Indonesia is reasonably clear. Analysts differ in their emphases, but generally agree that the following elements are needed (Gobel 2014ab):

- *Improved investment.* While the overall level of national investment, at over 30% of GDP, is encouraging, there are significant concerns about the composition of the investment. The infrastructure deficit is serious, so increases in investment in infrastructure projects are needed. Similarly, investment in the resource sectors—especially mining and energy—has been lagging.

- *Reforms to fiscal policy.* While the overall stance on fiscal policy is both conservative and responsible, it's widely agreed that reforms on both the income and the expenditure sides of budgetary policy are necessary. On the income side, tax revenues are far too low. As Governor of Jakarta, Widodo indicated that he was keen to increase revenues for the Jakarta Government. A similar approach will be needed for the national budget. On the expenditure side, improved spending arrangements are needed, along with reductions in subsidies. Most of these measures will need approval from the national parliament in the annual budget discussions, so successful policy reform in this area would be a clear indication that the new administration is confident in addressing controversial policy issues.
- *Fuel subsidies.* Very large fuel subsidies, consistently amounting to well over \$20 billion a year (around 15% of central government spending), have been the most controversial aspect of fiscal policy in recent years. Senior economic policymakers in the outgoing SBY administration all agreed that the subsidies need to be sharply reduced, but determined efforts by the government during budget discussions with the parliament in 2012 and 2013 made little progress in obtaining legislative agreement to reductions. Both Joko Widodo and his Vice President, Jusuf Kalla, have indicated that they plan to press for a reduction. In an effective reform scenario, the Widodo administration will be able to persuade the parliament to sharply reduce energy subsidies so that budget expenditures can be reallocated to other sectors, such as infrastructure.
- *Infrastructure.* Spending on infrastructure has lagged badly in Indonesia during the past decade. As a rough rule of thumb, Indonesia needs to be spending perhaps around 7% of GDP on infrastructure investment. This was the level sustained for most of the 1990s until the Asian financial crisis in 1997–98 (World Bank 2013, figures 50 and 51; ACDGI 2013, Chapter 3). Since then, however, infrastructure spending has lagged at around 3% of GDP, far below the level required to close the 'infrastructure deficit' widely recognised as a bottleneck to growth in Indonesia. If fuel subsidies can be reduced, the way will be open to reallocate around 2% or more to the infrastructure sector.
- *Sectoral policies.* There are challenges for policymakers in almost all sectors of the Indonesian economy—in agriculture, in manufacturing, in services, and in the export-oriented resources sector. Widodo has a background as a small-scale businessperson in Surakarta. He has often spoken of the need to foster small and medium enterprises (SMEs) in Indonesia, so he can be expected to support programs to strengthen the SME sector. Many previous efforts to foster growth in the sector have borne little fruit, so that approach is likely to receive wide support if the new administration can find effective ways of promoting SMEs. Two other urgent priorities that will need early attention are manufacturing policy and measures to address a looming crisis in the oil and mining sectors. In manufacturing, the new president will face pressures to support recent protectionist 'value added' programs that, among other things, have placed new requirements on mining companies to process minerals within Indonesia before export. As part of a strong reform program, it would be best if these policies were closely evaluated by the new government and perhaps substantially revised. More broadly, in the oil and energy sector, the production outlook is grim. Oil production has been steadily declining since the mid-1990s and there's no sign of any early reversal in that trend. As a result, Indonesia has moved from being an oil-exporting country two decades ago to facing sharply rising oil imports. New investment in other parts of the energy sector—gas and geothermal production—has been sluggish as well. Coal production has risen markedly in recent years, but the long-term global prospects of the coal sector are uncertain. A set of new, more investment-friendly policies in the energy sector would provide a significant boost to the Indonesian economy over the coming decade.
- *Poverty and employment.* Before the 1997–98 Asian financial crisis, strong economic growth in Indonesia generated jobs in agriculture, labour-intensive manufactures and the service sector and helped lift millions of people out of poverty. Following the crisis, poverty rose sharply and there was strong pressure on the government to establish a system of social safety nets. Joko Widodo, as Governor of Jakarta, introduced a new Jakarta Health Card (*Kartu Jakarta Sehat*) in 2012. He has indicated that he'll be looking at similar social security measures as part of his economic program as president. A recent study by Manning and Sumarto (2011) identified five challenges that need to be addressed to improve the quality of social protection in Indonesia: improving program targeting; protecting households from shocks; coordinating across government departments and levels of government; managing 'voice' and 'noise'; and making decentralisation work. On the

other hand, the incoming government will face many calls on the restricted Indonesian national budget, so the scope to expand social protection programs will be quite limited.

- *ASEAN Economic Community.* An early test for the incoming government in international trade policy will be measures needed to adjust to trading arrangements consistent with the ASEAN Economic Community, which is due to come into effect in 2015.¹⁸ Already, the market liberalisation steps likely to be necessary have met considerable opposition within Indonesia. More criticisms can be expected as a wider range of liberalisation proposals is considered. In practice—and reflecting the generally cautious approach within ASEAN to plans for reform—market liberalisation reforms introduced in 2015 can be expected to be modest. Nevertheless, the President of Indonesia is one of the key leaders of the ASEAN region. If Widodo supports an outward-looking economic reform agenda that supports wider liberalisation across ASEAN, that stance would lend important strength to moves to expand the ASEAN Economic Community during the next five years.

There's no shortage of other economic challenges. Joko Widodo has established a transition team that's expected to focus, among other things, on the state budget, an expanded health sector program, public housing, public transport and bureaucratic reform.

Government and administration

The new Civil Service Law No. 5 of 2014 signed into law by SBY earlier this year gives the new administration wide powers to promote reform in the public sector. The aim of the law is ambitious: to transform approaches and culture across the Indonesian public service.

One main change is that all jobs in national, provincial and regency (district) governments will be included in an Indonesian Civil Service. Henceforth, stricter standards are to be set for civil service employees, and staff members may be dismissed for poor performance or specified misdemeanours, such as a criminal conviction. There's to be greater emphasis on appointment by merit and a wider use of contracts within the public sector, with specific performance requirements. A new independent body, the Indonesian Civil Service Commission, will be appointed to oversee the implementation of civil service norms and ethics. Other reforms include improvements to salary and pension arrangements and an extension of the retirement age.

During the next few years, public salaries will be increased substantially, government procedures will be streamlined, clear performance goals and key performance indicators will be established for official agencies, and there will be strong pressure at all levels of government to improve service delivery to the public. In principle, the incoming government is well placed to introduce reforms, but the proof of the pudding will be in the eating. There will be strong public support for Widodo if he announces a clear program of reform of this kind.

Social issues

Widodo takes office with a large reservoir of goodwill from civil society. He's regarded as progressive on social issues and as having the common touch. He's seen as far more willing to engage in a relaxed way with ordinary citizens in his *blusukan* style than traditional elite politicians and public servants. Many Indonesians would say that 'Jokowi is one of us.'

The opportunity's now open to Widodo to build on these strengths. One challenge for him will be to strengthen his links with all parts of the Indonesian Muslim community. There were some suggestions from his political opponents during the presidential election campaign that he wasn't as committed to core Muslim values as he might be. He and his supporters firmly rejected those suggestions, pointing out that they seemed to be just more of the many rumours being spread around as part of the highly competitive politics of the presidential campaign. Indeed, just before the presidential poll, Widodo set aside time to visit Mecca on a minor pilgrimage for two days.

Another main task will be to establish effective links with the labour movement. Trade unions have become much more active in Indonesia since the transition from the Soeharto era. At times, labour groups mount forceful campaigns in support of wage increases and other labour rights. In late 2012, unions pressed for large wage increases of over 40% in the Jakarta area, and Widodo agreed to them. However, legislated wage increases of this kind tend to benefit workers in the formal sector of the economy but bring little if any gain to those in the informal sector. As president, Widodo will need to find a balance between the demands and interests of the two groups.

Many other social groups have welcomed Widodo's election. The indications are that women voters were inclined to support him¹⁹, students and educational organisations tended to do so, and some of Indonesia's most senior journalists expressed a preference for him as president. But few of those groups, taken together, have indicated any notable inclination to support the sorts of economic and governance programs that Widodo will need to consider if he's to design a reform program for Indonesia. It will be up to him to persuade these groups that reform, probably including some unpopular decisions in the short term, is in their longer term interests.

Foreign policy

Widodo will have little time to review foreign policy issues before three major international meetings appear on his agenda. Within three weeks of his appointment, in early November, the 2014 APEC Heads of Government meeting will be held in Beijing, followed just a few days later by the East Asia Summit in Naypyitaw and the G20 Heads of Government meeting in Brisbane.

The meetings will give Widodo his first entrée to high-level international economic diplomacy. He'll meet a wide range of leaders from around the Pacific rim (in APEC and the East Asia Summit) and from the leading nations of the rest of the world (in the G20). However, both he and the policies of the new government in Indonesia will come under close attention. The international community will have an opportunity to gain an early first-hand impression of the style of the new Indonesian President and of the prospects for Indonesian economic policy under the new administration.

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Outward-looking statements in two areas would send a clear signal that Joko Widodo is inclined to pursue internationalist policies as president. First, the main Indonesian statements could emphasise that the new government plans to encourage stronger economic growth not by adopting protectionist measures but by promoting overall investment, economic openness and structural reform. Second, Widodo could lend Indonesia's support for open regionalism in Asia by emphasising the growing role of ASEAN in regional cooperation programs in Southeast Asia. Other key leaders from Southeast Asia will attend the APEC and EAS meetings, but at the G20 meeting in Brisbane Widodo will, in effect, be the voice of ASEAN. G20 leaders will therefore listen carefully to statements from Indonesia to form judgements about the direction of policy across the ASEAN region.²⁰

Resilience scenario

There's no guarantee that it will be easy for a new government in Indonesia to implement organised reform. Just as the new government in India under Prime Minister Modi has been criticised recently for failing to move quickly to introduce reforms (Mallet 2014), Widodo may find that there's considerable resistance in some quarters to plans for change in Indonesia. Furthermore, since Indonesian independence was declared in 1945, there's always been significant domestic support for nationalist and protectionist policies (Feith & Castles 1970). During the presidential campaign, both Joko Widodo and Prabowo Subianto at various times indicated sympathy for some of those ideas. How, then, might policies unfold if reform proves difficult and if nationalist ideas of Indonesian 'resilience' take hold during the early days of the new administration?

Politics

Widodo might not find it easy to govern. For one thing, the margin of Widodo's win—he polled around 53% of the vote in a two-party contest—was notably less than those recorded by SBY in 2004 and 2009, at around 60%. Yet despite clear electoral support, SBY needed to devote a good deal of attention to the politics of governing and often found the parliament difficult to deal with. Partly as a result, he was frequently criticised for taking too long to make decisions and for being indecisive.

SBY's supporters hoped that after his second victory in 2009, finally freed from the need to consider the politics of re-election, he'd be able to govern more decisively. But soon a difficult political row blew up over controversial decisions taken by the central bank, Bank Indonesia, to bail out a troubled commercial bank in 2008. The 'Bank Century' case, as it became known, was taken up by SBY's opponents in the parliament, who used it, time and again, to nibble away at his authority throughout the whole of his second term. The opposition found many ways to frustrate the various proposals that the administration put forward. The debates in 2012 about government suggestions to cut back ballooning energy subsidies were particularly heated. In the end, the government was forced to withdraw the proposals in a humiliating backdown on a vital issue of economic policy.

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Perhaps the main lesson for Widodo from the experience of government during SBY's second term is that the president and his team of ministers can expect to face frequent criticism, and sometimes outright opposition, in the parliament. And Widodo's early position is made even more difficult because the oppositionist pro-Prabowo grouping in the parliament appears to have a clear majority following the legislative election in April 2014. Some drift in loyalty can be expected now that Widodo has won the presidency, but a rough count of seats in the new parliament in April indicated that the parties supporting him could count on the support of perhaps 210 out of 560 members (less than 40%), while the opposition group could rely on the votes of the rest. Widodo may need to

draw on all of his considerable political and negotiation skills to work with a parliament in which the majority is so unsympathetic to his administration.

Sooner rather than later, Joko Widodo will also need to define his relations with the PDI-P, the main party that supported him in the presidential election, and with the leader of the PDI-P, Megawati Sukarnoputri. Megawati (as she's universally known) has dominated the activities of the PDI-P in recent decades. She's the daughter of the first president of Indonesia, Sukarno, and she played a widely honoured role in the political manoeuvres leading up to the fall of Soeharto in 1998. Megawati Sukarnoputri's position in Indonesian public life is such that Widodo will need to ensure that he's seen to respect that position, notwithstanding his own role as president.

The risk in a resilience scenario is that Widodo will find these political hurdles hard to overcome. Many Indonesians are hoping for strong leadership from him, but if he faces strong opposition in the parliament, and if he finds it difficult to reach a *modus vivendi* with the PDI-P and Megawati, he may need to appeal increasingly to nationalist and populist sentiments to bolster his position. In doing so, he may need to compromise on key aspects of his reform program. If so, the risk is that Widodo may begin to be seen as indecisive and ineffective, just as SBY was seen by many of his erstwhile supporters in recent years.

Economy

If there are strong pressures on Joko Widodo, including from the parliament, to adopt populist policies, the incoming government may find it difficult to promote strong economic growth. In an inward-looking resilience scenario in which the government faces resistance to reform measures, the overall rate of economic growth could remain relatively low, perhaps below 6% per year. That wouldn't be sufficient to provide jobs for the expanding labour force, and unemployment could be expected to rise. Criticism of Widodo's leadership would be likely to grow.

The first requirement for a higher rate of growth is a sustained level of investment of over 30% of GDP. But increasing nationalism would be likely to discourage foreign investment, particularly in the oil and mining sectors. In turn, that would also tend to constrain domestic investment. In that case, the other sectors of the economy could also become sluggish before too long.

Investment in the oil and mining sectors has clearly been lagging, and the outgoing SBY administration's failure to deal with the problem more decisively has been puzzling. Oil production has been declining for around two decades, and gas production is stagnant. The legal framework to encourage increased investment in the energy sector is in urgent need of reform (Machmud 2014). Moreover, the current approach to the minerals sector, which is to require mining firms to invest in the domestic processing of ores through the mandatory construction of smelters, is clearly discouraging further investment. Without changes in policies, the outlook for the sector isn't encouraging.

Investment in infrastructure has also been lagging. A package of measures is needed to encourage both state-owned enterprises and the private sector to invest in transport, power, water supply, sanitation, communications, health and education projects. What's needed are a clearer framework of overall policy for the different parts of the infrastructure sector, more predictable regulatory arrangements, an improved pipeline of well-designed projects, and a government commitment to support the introduction of full user-charges to provide investors with the financial incentives needed to support new investments.

It's sufficient to set out this list of problems to show that it will be difficult for the incoming government to introduce a package of appropriate reforms to stimulate investment in infrastructure. Resistance to appropriate pricing policies, particularly, is strong in the parliament, even though it will be very hard to raise the large amounts of revenue needed to support large infrastructure projects without significant price increases. And even if the new government is prepared to work hard to introduce worthwhile reforms, it will take at least five years before larger projects can be completed and the benefits of the new policies begin to be seen across Indonesia.

A second requirement for higher growth is to ensure that overall demand is sustained across the economy. The supply side of the Indonesian economy, especially in the informal economy, is extremely flexible. Sustained demand

in Indonesia usually generates strong supply responses, but in the past two years has led to growing imbalances on the external account. The authorities have responded partly by allowing the foreign exchange rate to depreciate and partly (and more worryingly) by lifting interest rates. Higher interest rates, combined with falling terms of trade, have led to a slackening of demand and a slowing of the growth rate.

The authorities would have more room to stimulate demand if the balance-of-payments constraint on growth were eased, but current structural policy is tending to choke export growth by discouraging new investment in the energy and minerals sectors and by failing to provide incentives for export-oriented manufacturing. In a resilience scenario, the risk is that these inward-looking policies will be continued and that relatively little attention will be given to policies to promote exports.

A third risk in a resilience scenario is that populist economic policies might exacerbate fiscal pressures on the national budget and encourage unions to press for higher wages. Joko Widodo has already indicated that an expansion of the national social safety net, through widened health programs, is under consideration. Yet the government budget deficit is already very close to the legal limit of 3%. The room for increased spending on expensive welfare programs is very limited. Further increases in wages in the formal sector, too, would add to pressures on the government budget and exacerbate problems of international competitiveness, especially in the manufacturing sector.

The economic options for the incoming administration are quite constrained. A tilt towards nationalist policies within a resilience scenario would probably be popular among some business and social groups in Indonesia but would hinder growth, job creation and structural change.

Government and administration

Although the new Civil Service Law No. 5 of 2014 opens the way to significant reform of the public service, the scope for continued debate and further delay is considerable. Strong political leadership will be needed to implement the proposed reforms, especially because there's likely to be significant resistance within the bureaucracy at the provincial and regency levels and in central government agencies.

Recent experience is not encouraging. Proposed reforms outlined in a Law on Public Services introduced by the SBY administration and approved by the national parliament in 2009 (after, it might be noted, four years of deliberation) aimed 'to improve the delivery of public services by creating mechanisms for determining minimum service standards, receiving and acting on complaints when standards are not met and, in some cases, providing compensation' and attempted 'to establish clear guidelines on the principles and objectives of public service delivery, and a framework for their implementation' (Buehler 2011). In the event, the law has proved difficult to implement. The many problems that have arisen include vagueness in the law, ineffective mechanisms for the handling of complaints, weaknesses on the part of legislatures in holding officials to account, and a lack of funding for activities specified in the law.

If the Widodo administration wishes to support the implementation of the new Civil Service Law, increased funding will be needed to support reforms of administration in the public sector. But the Indonesian public and parliaments are usually reluctant to provide more funds for public servants because it's widely believed that the cost of government is already too high. There's frequent comment in the media about the share of government expenditure that's spent on government administration, especially at the provincial and regency levels. Watchdog organisations, such as the Indonesian Forum for Budget Transparency (*Seknas Fitra*), a public finance think tank, are often highly critical of government spending on administration, arguing that public servants frequently misuse budgetary allocations.²¹ While criticisms of this kind aren't surprising, the fact that social watchdog organisations are so antagonistic towards increased government spending will complicate efforts by the Widodo administration to promote public sector reform.

Social issues

The strong support that Joko Widodo received from a wide range of civil society organisations during the presidential election campaign has some strings attached. There's a wide expectation among some activist groups that he'll pursue 'pro-people welfare programs' (programs that are *pro-kesejahteraan rakyat*) and appoint ministers who are 'patriotic ... and will promote the national interest' (*para patriotis ... serta menjunjung kepentingan nasional*).²²

Some observers downplay such talk as little more than activist rhetoric, but 'pro-people' ideas are widely held among some groups in Indonesia and Joko Widodo has gone to some lengths to identify himself with a 'pro-people' approach to policy. At times, he has presented himself as understanding the plight of the ordinary citizen faced with the unyielding bureaucracy of government. In one widely reported incident, as Mayor of Surakarta in 2011, he became personally involved when the Surakarta municipality had overdue bills of close to \$1 million (Rp8.9 billion) owing to the state-owned electricity company *Perusahaan Listrik Negara*. In line with its policy of pursuing a more disciplined approach to the collection of overdue bills, the company imposed a blackout on street lamps in Surakarta just before Christmas. The municipality quickly authorised payment, but protested that the company should have considered the public interest before cutting off the electricity. As a protest, Widodo made a highly publicised personal visit to the local *Perusahaan Listrik Negara* office to pay the Rp8.9 billion in cash, in the form of hundreds of bundles of notes and even small coins (Ayuningtyas 2012).

Public delinquency in the payment of bills to government agencies is widespread in Indonesia. It's one of the key issues that the incoming government will need to address in a program of public sector reform.

While populist gestures of this kind helped to bolster Widodo's pro-people image, they do little to support the improved operation of state-owned enterprises in Indonesia. If, as president, he's inclined to make such gestures, he's likely to find that such an approach contributes to the fiscal problems of the country. Public delinquency in the payment of bills to government agencies is widespread in Indonesia. It's one of the key issues that the incoming government will need to address in a program of public sector reform.

Joko Widodo might also need to consider some broader issues if he decides to continue to emphasise his pro-people *blusukan* approach as president. President Abdurrahman Wahid (Gus Dur) emphasised a somewhat similar pro-people style of public leadership during his relatively brief period as president between 1999 and 2001. This aspect of Gus Dur's attention to public issues was widely appreciated and helped make him a much-loved leader of the nation, but was less appreciated among elite politicians, administrators and business leaders. The domestic and international media, too, quickly became quite critical of Gus Dur. His former press spokesperson, well-known journalist Wimar Witoelar, has spoken of the media 'lynch mob against a president who represented too much uncertainty, especially [for] those who had a stake in the status quo' (Witoelar 2002:174).

Ultimately, the president of a nation needs to demonstrate strength and the ability to use power effectively. In the end, Gus Dur's highly effective outreach to the *orang kecil* (the ordinary people, as Wimar Witoelar calls them) did little to save him from impeachment by the parliament. One of the lessons for future presidents is that the elite in Indonesia holds considerable power. There are risks for any president in trying to bypass the elite through direct pro-people appeals for support. A better approach is to balance the presidential relationship with the broad

electorate with the management of affairs in dealing with the elite. A president who fails to do this may find, as Gus Dur did, that the presidential position can soon become very uncertain.

Foreign policy

A resilient Indonesian foreign policy under a new administration, in contrast to a reform-oriented foreign policy, could well be less accommodating to international and regional programs for change. International agendas are set out, often in vague terms, in high-level communiqués issued from APEC and G20 meetings and many other international meetings held each year. The communiqués are often long and wordy, full of vague language designed to disguise sharp differences of interests between the heads of governments at the meetings.

It isn't surprising that participants from Indonesia are sceptical about the value of such meetings. One of Indonesia's most senior economic policymakers, Professor Widjojo Nitisastro, summarised his experience in representing Indonesia at international conferences in the mid-1980s:

There has already been a plethora of global conferences—high-level conferences, ministerial-level conferences, and so on—which have set out firm commitments about things like international development cooperation, commitments to the need to foster open trading arrangements, and commitments to better manage arrangements for multilateral economic cooperation. But unfortunately none of these international economic conferences has managed to bring about any significant progress in the area of international economic cooperation. And in fact, in all of the North–South forum dialog meetings that have been held, the final results have led to dead ends, or efforts that have just faded away, or even a weakening of earlier commitments that had been entered into. (Widjojo 2010:539)

Reading briefings like this, President Joko Widodo may well conclude that he shouldn't invest too much effort into the international game of meetings of heads of governments.

A nationalist Indonesian approach to foreign policy, therefore, would be cautious about making commitments to participate in ambitious international or regional programs. Rather, Indonesia would focus on a limited number of key goals. Those might include, first, strengthening regional security in Southeast Asia, and second, supporting the measured expansion of ASEAN-related programs in the region.

The disadvantage of a cautious approach of this kind is that some international observers might suggest, as in the past, that Indonesia is punching below its weight in international affairs. And unless Indonesia provided a firm commitment to continue to play a strong regional role, programs designed to expand ASEAN might be held back. However, the nationalist response within Indonesia would be that the first priority for Indonesia should be to build strength and resilience at home. Many Indonesians would say that Indonesia can only hope to provide leadership across ASEAN once the country has a strong economy and has strong government institutions that engender confidence both at home and abroad.

CHAPTER 4

Some implications

What's the outlook for Australia–Indonesia relations—and Australia's relations with ASEAN—in Joko Widodo's Indonesia? Much depends on the broad policy direction—reform or resilience—that Indonesia pursues during the next few years. However, whichever direction is taken, there are likely to be elements of both change and continuity in the bilateral relations between the two countries.

Change can be expected because considerable jockeying for influence is likely to occur during the coming months as Widodo and his team settle into office. The president's own views will be important, of course, but he doesn't have extensive experience in foreign affairs. The push and pull of interest and advocacy groups, the views of senior policy advisers and perhaps pressures from the parliament may have a significant influence on the direction of policy. There's likely to be considerable competition for the ear of the president.

Continuities in policy can also be expected. For one thing, foreign policy isn't a strongly contested area of public policy debate in Indonesia. In recent decades, Indonesian presidents have tended to rely on the advice of seasoned advisers from the Ministry of Foreign Affairs, who've been careful to adhere to long-established principles: firm adherence to a 'free and active' foreign policy; strong support for ASEAN regionalism in Southeast Asia; a tendency to rely on regional and multilateral approaches rather than bilateral action when possible; and caution in responding to the various blandishments sometimes offered to Indonesia by nations such as the US and China and regional groupings such as the European Union.

Also, despite recent uncertainties in the Australia–Indonesia relationship, Indonesian commentators and policymakers are inclined to see Australia's activities in Southeast Asia as benign rather than malign. Certainly, Australia is seen as having the capacity to act somewhat unilaterally, sometimes at short notice, and to be less committed to regional consultations with neighbours than is the custom, for example, between the members of ASEAN. And Indonesian policymakers are aware that the potential for friction between Indonesia and Australia over problems in the Papuan provinces is considerable. As recently as 2006, the Indonesian Ambassador to Australia was recalled to Jakarta for several months following the Australian Government's decision to grant temporary protection visas to asylum seekers from West Papua. Australia, therefore, is seen by many observers in Indonesia as generally having well-meaning intentions but sometimes stumbling along the way.

Reform scenario

If Joko Widodo and his government are able to pursue an effective *reform scenario*, Australia and Indonesia should find it easy to find common ground for cooperation. Widodo has set goals of fostering democratic norms, strengthening domestic stability and civil society, and promoting economic growth. It's in Australia's interests that he succeeds in promoting those reforms and others that he has spoken of. It's also in Australia's interests, as well as the broader interests of ASEAN, that Widodo provides effective leadership within ASEAN.

To provide tangible support for a reform agenda in Indonesia, the Australian Government could look to expand programs of bilateral cooperation, with the agreement of the Indonesian Government, in several ways:

- *Support government reform.* There's wide agreement within Indonesia that public sector reform is a priority. Australia could lend useful support in this area. In recent years, there have been effective twinning programs between Australian and Indonesian government departments in such areas as finance, treasury, immigration, defence, statistics and auditing, among others. Arrangements of this kind provide links that are in the interests of both countries. Links in the defence sector have been especially important in recent decades. There's wide scope to expand twinning into other areas, such as infrastructure management, health and education planning, and environmental policy. On the Australian side, it would be helpful to strengthen incentives for Australian agencies to further develop these types of bilateral programs.
- *Strengthen cooperation with Indonesia at the international level.* In recent years, Australia and Indonesia have identified shared interests in areas of international affairs such as maritime cooperation, quarantine, health and regional security. Differences in priorities remain, but two voices are better than one. When Canberra and Jakarta can work together to support regional and international programs, the joint priorities of Australia and Southeast Asia are more likely to be recognised across the international community. Australia and Indonesia have cooperated effectively in APEC for well over two decades. And, although Australia isn't a member of ASEAN, it has a strong interest in ASEAN's continuing success. More recently, Australia and Indonesia have been working to improve cooperation between leaders within the G20 framework. In all of these areas, it's in the interests of both countries to work together to promote shared goals. Australia should look to opportunities to work with Indonesia to strengthen joint programs in these and other international organisations.
- *Build private sector and people-to-people links.* It's in the interests of both countries to strengthen a wide range of non-government links between the two. Business and trade connections remain surprisingly underdeveloped, considering that in many areas the two economies are complementary rather than competitive. Joko Widodo has emphasised the importance of these sectors in Indonesia, and he comes to office with strong personal experience in the private sector. On the Australian side, it would be helpful to consider what further steps might be taken in Australia to promote links between the two countries in these areas. There are various regulatory and other impediments in Australia that discourage such links. As just one example, many parts of the service sector in Australia are inward-looking and not inclined to venture into markets in developing countries in Asia, such as Indonesia, despite rapid growth in the demand for services in Asia. The Australian tertiary education sector was able to expand the provision of education services into Asian markets in the 1990s, but only after pro-market reforms were introduced into the sector in the mid-1980s. It would be useful to review similar barriers in other sectors, with the aim of facilitating private sector and community links between the two countries.²³

Resilience scenario

If the broad direction of Indonesian policy moves towards a *resilience* scenario, Australia should nevertheless aim to maintain strong and effective relations with Indonesia. It's for the Indonesian people and their leaders to decide which policies are in the best interests of their nation. Many of the social problems and issues of governance in Indonesia are daunting ones, and it would be in the best interests of both countries for Australia to continue to strengthen programs of cooperation with Indonesia. Appropriate approaches might include the following:

- *Work harder to understand Indonesia's challenges.* The two countries are very different. Australia's a rich country with strong cultural and policy links with Western nations of the North, particularly the Anglo-Saxon countries. Indonesia's the third-largest developing country, with important links to other nations of the South, including in the Moslem world. The domestic priorities in each country are also very different. Against this background, it's in Australia's interests for senior policymakers in Canberra and other observers to have a sound appreciation of the domestic challenges in Indonesia. In recent years, Australian policy towards Indonesia has sometimes been changeable and directed towards the achievement of particular short-term goals. But Australia and Indonesia will be neighbours forever. Australia's best interests will be best served if Australian decisions are taken with an eye to the long term in working with Indonesia on issues of joint interest.
- *Continue to build links.* If a stronger nationalist mood emerges within Indonesia during the next few years, it may become more difficult to further strengthen government and other links between the two countries, at least in the short term. Nevertheless, consistent with a policy approach in which Australia looks to the longer term, it would still be in the interests of both countries, as well as the broader interests of the region, for Australia to develop government-to-government twinning links where possible and to promote a range of other people-to-people links. Links between the Australian and Indonesian defence forces have served both countries well for over 50 years and should continue to be strengthened. Opportunities should be taken to strengthen links in many other areas.
- *Scholarship programs.* Many thousands of Indonesian students have studied in Australia in recent decades, both in programs supported by scholarships supported by Australian aid and as private students in courses in Australia. Some of Indonesia's most senior public servants and cabinet ministers have studied in Australia and speak warmly of their experiences in undergraduate and graduate courses here. It's in the long-term interests of both countries to strengthen bonds developed through programs of this kind. Even if a stronger nationalist mood is evident in Indonesia under the incoming government, the scope for an expanded scholarship program would be considerable.

Conclusion

After a largely peaceful and progressive 10 years of administration under the leadership of Indonesia's sixth president, Susilo Bambang Yudhoyono, Indonesia's institutions have grown stronger and its international standing has risen, but the challenges ahead remain daunting. Many aspects of governance across the nation are underdeveloped. Despite good economic progress, close to half of the population live on incomes of below \$2 per day. And prospects for the continued strengthening of regional cooperation through ASEAN depend to a large degree on active support from the Indonesian President.

Indonesia's seventh president, Joko Widodo, will need to decide whether to adopt an outward-looking reform program or to pursue a more inward-looking approach intended to promote resilience at home. The reform path would be harder to implement in the short term, but promises stronger economic growth and development in the medium term. The resilience path would quite probably be more popular with some influential groups in Indonesia and would reflect the direction of policy in some key areas of governance in recent years.

Perhaps Indonesia's new president will, depending on circumstances, select policies that combine elements from both the reform and the resilience paths, but much depends on the emphasis he's able to give to the reform path. The resilience path perhaps offers safer political options but would delay many of the reforms in government, economics and social affairs that are still urgently needed to strengthen Indonesia's place in the world.

NOTES

- 1 These events are discussed in colourful detail by a well-known Indonesian journalist and former presidential spokesman for president Abdurrahman Wahid in Witoelar (2002).
- 2 It is useful to recall the concerns held in some circles in the international community when SBY came to office. *The Economist* summarised some key changes during SBY's first term as follows: 'When he won the presidency in 2004, Mr Yudhoyono took over a country dealing with Islamic terrorism, separatist violence, a fragile democratic record and a military still very much involved in political and economic life. Five years on, these problems have largely faded into the background.' *Economist Intelligence Unit*, 21 April 2009.
- 3 A very useful overall review of developments in the legal system from the Dutch colonial period to the end of the Soeharto era is in Lev (2000).
- 4 A much-discussed example of the intermingling of influential political and business activities at the provincial level in recent years is in the province of Banten, close to Jakarta. The high-profile Governor of Banten, Ms Ratu Atut, participated in the establishment of a so-called 'political dynasty' in the province. Ratu Atut was investigated by the Indonesian Corruption Eradication Commission in 2013. In 2014, she was formally detained by the commission on charges of corruption. Details are in the Wikipedia entry for Ratu Atut Chosiyah (https://en.wikipedia.org/wiki/Ratu_Atut_Chosiyah).
- 5 Quarterly surveys of the Indonesian economy issued by the World Bank are on the World Bank Indonesia website (<http://www.worldbank.org/en/country/indonesia>).
- 6 For example, ACDGI (2013) talks of annual rates of growth of 7% and even higher. In addition, President-elect Joko Widodo has said that he sees a level of 7% as a desirable growth target for Indonesia.
- 7 Many countries maintain deficits on the current account for quite long periods. Australia, which is usually a capital-importing country, has run a deficit of around 3% of GDP on the current account for much of the past century.
- 8 As just one example, the planning agency, Bappenas, issued detailed guidelines of over 300 pages to staff in Bappenas (2009).
- 9 A summary of some of the challenges facing the legal system in Indonesia is on the Wikipedia for the Indonesian Supreme Court (https://en.wikipedia.org/wiki/Supreme_Court_of_Indonesia).
- 10 See 'Judges strive to uphold dignity despite low pay', *Jakarta Post*, 26 April 2012, www.thejakartapost.com/news/2012/04/26/judges-strive-uphold-dignity-despite-low-pay.html. This article includes a listing of official salaries at the time.
- 11 The 2013 US *Human Rights Report* is at www.state.gov/j/drl/rls/hrrpt/. Comments relating to Indonesia are at www.state.gov/documents/organization/220408.pdf.
- 12 Myrdal's (1968) key distinction between 'hard' and 'soft' states is relevant in this context.

- 13 As an example, during 2013 there was a protracted conflict in Sampang district on the island of Madura, near Surabaya, involving a local Shia community. The ongoing issue attracted much attention in the national press. Leading members of the majority Sunni community in Sampang regarded some of the activities of the Shia community as unacceptable. Some of the Shia community were ejected from Sampang and were forced to move to the Sidoarjo district near Surabaya.
- 14 Woolcock (2007) discussed the choices between different types of diplomacy (bilateral, regional, plurilateral, and multilateral).
- 15 Information on the Bali Process is available at www.baliprocess.net/.
- 16 Prominent Indonesian economist and former minister, Professor Moh. Sadli, used to argue that Indonesian policymakers are generally pragmatic and are skilled at 'muddling through' when problems crop up.
- 17 *Henry IV*, Act 5, Scene 5, line 47, 'I know thee not, old man. Fall to thy prayers.'
- 18 A summary of steps towards an ASEAN Economic Community is in ADBI (2010); see also the ASEAN website (www.asean.org/communities/asean-economic-community).
- 19 See comments by Julia Suryakusuma, a well-known writer on women's affairs in Indonesia, in 'View Point: 'Cherchez la femme', Jokowi's "feminine" leadership', *Jakarta Post*, 6 August 2014, www.thejakartapost.com/news/2014/08/06/view-point-cherchez-la-femme-jokowi-s-feminine-leadership.html.
- 20 Issues affecting Asian regionalism and the prospects for an Asian economic community are discussed in Capanelli & Kawai (2014).
- 21 See the *Seknas Fitra* website (<http://seknasfitra.org/?lang=en>).
- 22 'Kabinet Perekonomian Jokowi-JK Harus Pro Kesejahteraan Rakyat' [The Jokowi-JK Economic Cabinet must be Pro-Peoples' Welfare], reporting on a conference held on 7 July 2014, <http://seknasfitra.org/fitra-kabinet-perekonomian-jokowi-jk-harus-pro-kesejahteraan-rakyat/>.
- 23 For details of cooperation of this kind between Indonesian and Australian police forces, see Connery et. al.

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ACRONYMS AND ABBREVIATIONS

APEC	Asia–Pacific Economic Cooperation	ASEAN	Association of Southeast Asian Nations
GDP	gross domestic product		
OECD	Organisation for Economic Co-operation and Development		
PDI-P	Indonesian Democratic Party of Struggle (Partai Demokrasi Indonesia—Perjuangan)		
PPP	purchasing power parity		
SBY	Susilo Bambang Yudhoyono		
SMEs	small and medium-sized enterprises		
UN	United Nations		

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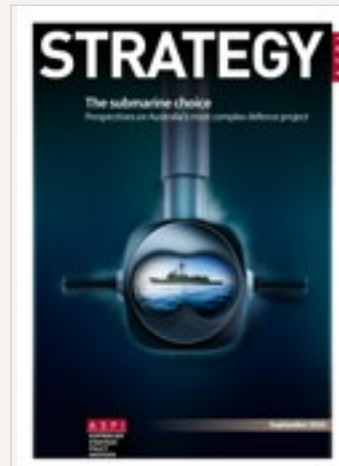


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