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Political Institutions and Economic Policy Reform
in Post-Suharto Indonesia

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A thesis submitted for the degree of Doctor of Philosophy
of The Australian National University
Canberra
February 2008
Declaration

I declare herewith that this thesis is based on my own work unless otherwise referenced or acknowledged. I submit this thesis solely for the fulfillment of the requirements for the degree of Doctor of Philosophy of the Australian National University, Canberra.

Gabriel Lele

February 2008
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Abstract

This research addresses the effects of political institutions, particularly the effects of the new institutional arrangements on policy outcomes in the post-Suharto Indonesia (1999-2007). The core argument is that the new institutional arrangements have brought about many significant effects on policy outcomes. This thesis illustrates this argument by qualitatively investigating how the changes in Indonesia's key political institutions, especially the country's constitution and key political laws, have affected the achievements in economic policy reform. Given the complexity of the institutional reform since 1999, it uses executive strength as its optic. This refers to an aggregated measure of a president's constitutional powers and partisan support in parliament.

This topic is important for two reasons. First, the importance of political institutions is still underplayed in the Indonesian literature despite the many significant changes in this area since 1999. Therefore, this research develops an alternative way of looking at certain policy outcome from an institutional angle. Second, assessing the achievements in economic reform in the post-Suharto era is critical for the prospect of democratic consolidation.

Looking at the achievements in fiscal and investment policy areas, this research finds a stark variation among the post-Suharto administrations. There is a general pattern of policy-making capacity across these areas. President Wahid adopted very limited policy reforms in both fiscal policy and investment policy areas. President Megawati, on the contrary, adopted many significant policy reforms in these areas with elements of delay and partial reversal. President SBY performed the best, adopting many policy reforms in these areas in a very determined manner. The case study of fuel subsidy reform confirms this general pattern.

Without ignoring the effect of political actors and their interests, this research argues that this variation is best explained by the variation in the degree of executive strength. Wahid achieved only limited reforms, primarily because he had insufficient political capital to adopt politically difficult reforms, the most important of which were constitutional protection over president's security of tenure and partisan support. These institutional underpinnings improved under Megawati with the tightening of impeachment procedures. She had constitutional protection over security of tenure though she still lacked partisan support. SBY had sufficient political capital since he was directly elected by the people and had protection over security of tenure as well as sufficient partisan support in parliament.

These findings imply that the new institutional arrangements are of great importance for policy outcomes. Political institutions must therefore be accorded at least the same attention as interest in analyzing certain policy outcomes in Indonesia.
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<th>Description</th>
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<tr>
<td>ABRI</td>
<td>Angkatan Bersenjata Republik Indonesia (Indonesian Armed Forces)</td>
</tr>
<tr>
<td>ADB</td>
<td>Asian Development Bank</td>
</tr>
<tr>
<td>APBD</td>
<td>Anggaran Pendapatan dan Belanja Daerah (Regional Budget)</td>
</tr>
<tr>
<td>APBN</td>
<td>Anggaran Pendapatan dan Belanja Nasional (National Budget)</td>
</tr>
<tr>
<td>Bappenas</td>
<td>Badan Perencanaan Pembangunan Nasional (National Development Planning Agency)</td>
</tr>
<tr>
<td>BCA</td>
<td>Bank Central Asia</td>
</tr>
<tr>
<td>CGI</td>
<td>Consultative Group on Indonesia</td>
</tr>
<tr>
<td>DPR</td>
<td>Dewan Perwakilan Rakyat (People’s Representative Council; Indonesia’s House of Representatives)</td>
</tr>
<tr>
<td>GBHN</td>
<td>Garis-Garis Besar Haluan Negara (Broad Guidelines of State Policy)</td>
</tr>
<tr>
<td>GDP</td>
<td>Gross Domestic Product</td>
</tr>
<tr>
<td>GOLKAR</td>
<td>Golongan Karya (Functional Party; a hegemonic ‘state’ party under Suharto)</td>
</tr>
<tr>
<td>IBRA</td>
<td>Indonesian Bank Restructuring Agency</td>
</tr>
<tr>
<td>IMF</td>
<td>International Monetary Fund</td>
</tr>
<tr>
<td>JICA</td>
<td>Japan International Cooperation Agency</td>
</tr>
<tr>
<td>KEPRES</td>
<td>Keputusan Presiden (Presidential Decision)</td>
</tr>
<tr>
<td>KKI</td>
<td>Kesatuan Kebangsaan Indonesia (Indonesian National Unity)</td>
</tr>
<tr>
<td>KPU</td>
<td>Komisi Pemilihan Umum (General Election Commission)</td>
</tr>
<tr>
<td>MPR</td>
<td>Majelis Permusyawaratan Rakyat (People’s Consultative Assembly; Indonesia’s Congress)</td>
</tr>
<tr>
<td>NU</td>
<td>Nahdatul Ulama (Revival of the Religious Scholars)</td>
</tr>
<tr>
<td>P3I</td>
<td>Pusat Pengkajian dan Pelayanan Informasi (Research and Information Center; DPR’s research department)</td>
</tr>
<tr>
<td>PAN</td>
<td>Partai Amanat Nasional (National Mandate Party)</td>
</tr>
<tr>
<td>PBB</td>
<td>Partai Bulan Bintang (Crescent and Star Party)</td>
</tr>
<tr>
<td>PBR</td>
<td>Partai Bintang Reformasi (Reform Crescent Party)</td>
</tr>
<tr>
<td>PD</td>
<td>Partai Demokrat (Democrat Party)</td>
</tr>
<tr>
<td>PDKB</td>
<td>Partai Demokrasi Kasih Bangsa (Democracy and Love the Nation Party)</td>
</tr>
<tr>
<td>PDIP</td>
<td>Partai Demokrasi Indonesia-Perjuangan (Indonesian Democratic Party-Struggle)</td>
</tr>
<tr>
<td>PDS</td>
<td>Partai Damai Sejahtera (Prosperous Peace Party)</td>
</tr>
<tr>
<td>PDU</td>
<td>Perserikatan Daulatul Ummah</td>
</tr>
<tr>
<td>PERPRES</td>
<td>Peraturan President (Presidential Regulation)</td>
</tr>
<tr>
<td>PERTAMINA</td>
<td>Perusahaan Tambang Minyak Nasional (National Oil Mining Company)</td>
</tr>
<tr>
<td>PK</td>
<td>Partai Keadilan (Justice Party)</td>
</tr>
<tr>
<td>PKB</td>
<td>Partai Kebangkitian Bangsa (National Awakening Party)</td>
</tr>
<tr>
<td>PKD</td>
<td>Partai Katolik Demokrat (Democrat Catholic Party)</td>
</tr>
<tr>
<td>PKP</td>
<td>Partai Keadilan dan Persatuan (Justice and Unity Party)</td>
</tr>
<tr>
<td>PKPB</td>
<td>Partai Karya Peduli Bangsa (Works and Concerns for the Nation Party)</td>
</tr>
</tbody>
</table>
| PKPI         | Partai Keadilan dan Persatuan Indonesia (Indonesian Justice and
<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Full Name</th>
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<tbody>
<tr>
<td>PKS</td>
<td>Partai Keadilan Sejahtera (Prosperous Justice Party)</td>
</tr>
<tr>
<td>PKU</td>
<td>Partai Kedaulatan Umat (People’s Sovereignty Party)</td>
</tr>
<tr>
<td>PLN</td>
<td>Perusahaan Listrik Negara (National Electricity Company)</td>
</tr>
<tr>
<td>PNIM</td>
<td>Partai Nasional Indonesia Marhaenisme (Indonesian Nationalist Party-Marhaenism)</td>
</tr>
<tr>
<td>PNI-FR</td>
<td>Partai Nasional Indonesia-Front Marhaen (Indonesian Nationalist Party – Marhaen Front)</td>
</tr>
<tr>
<td>PNI-MM</td>
<td>Partai Nasional Indonesia-Massa Marhaen (Indonesian Nationalist Party – Marhaen Mass)</td>
</tr>
<tr>
<td>PNU</td>
<td>Partai Nadhatul Ummah (Revival of the Religious Scholars Party)</td>
</tr>
<tr>
<td>POLRI</td>
<td>Kepolisian Republik Indonesia (Indonesian Police Department)</td>
</tr>
<tr>
<td>PP</td>
<td>Peraturan Pemerintah (Government Regulation)</td>
</tr>
<tr>
<td>PPDI</td>
<td>Partai Penegak Demokiasi Indonesia (Indonesian Democracy Upholders Party)</td>
</tr>
<tr>
<td>PPDK</td>
<td>Partai Persatuan Demokrasi Kebangsaan (Unity Democracy and Nationhood Party)</td>
</tr>
<tr>
<td>PPP</td>
<td>Partai Persatuan Pembangunan (United Development Party)</td>
</tr>
<tr>
<td>PROPENAS</td>
<td>Program Pembangunan Nasional (National Development Program)</td>
</tr>
<tr>
<td>REPETA</td>
<td>Rencana Pembangunan Tahunan (Annual Development Plan)</td>
</tr>
<tr>
<td>RKP</td>
<td>Rencana Kerja Pemerintah (Government Work Plan)</td>
</tr>
<tr>
<td>Rp</td>
<td>Rupiah (Indonesia’s currency)</td>
</tr>
<tr>
<td>RPJM</td>
<td>Rencana Pembangunan Jangka Menengah (Medium Term Development Plan)</td>
</tr>
<tr>
<td>RPJP</td>
<td>Rencana Pembangunan Jangka Panjang (Long Term Development Plan)</td>
</tr>
<tr>
<td>SBY</td>
<td>Susilo Bambang Yudhoyono</td>
</tr>
<tr>
<td>SOEs</td>
<td>State-Owned Enterprises</td>
</tr>
<tr>
<td>TNI</td>
<td>Tentara Nasional Indonesia (Indonesian Armed Forces; now called ABRI (see ABRI))</td>
</tr>
<tr>
<td>UD</td>
<td>Utusan Daerah (Regional Delegates; Indonesian version of senate, only applicable until 2004)</td>
</tr>
<tr>
<td>UG</td>
<td>Utusan Golongan (Societal Delegates)</td>
</tr>
<tr>
<td>UNDP</td>
<td>United Nations Development Programme</td>
</tr>
<tr>
<td>UU</td>
<td>Undang-Undang (Law)</td>
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The importance of political institutions

1.1 Introduction

This thesis assesses the effects of political institutions, in particular the effects of the new institutional arrangements on policy outcomes in post-Suharto Indonesia (1999-2007). The core argument is that the new institutional arrangements have brought about many significant effects on policy outcomes. This thesis illustrates this argument by qualitatively investigating how the changes in Indonesia’s key political institutions, especially the country’s constitution and key political laws, have affected achievements in economic policy reform. Given the complexity of institutional reform since 1999, this thesis will only assess the effects of executive strength on the adoption of politically difficult economic policy reform. Executive strength is a term used in the thesis to represent an aggregated measure of a president’s constitutional powers, especially the presence (or absence) of constitutional protection over the president’s security of tenure, and partisan support in parliament. In terms of economic policy reform, this thesis will only look at economic policies which require significant changes that provoke strong opposition when adopting them is more a necessity than a choice. After the 1997 economic crisis, all presidents have been forced to adopt painful agendas such as fiscal prudence, trade liberalization, privatization, and subsidy removal. They have all been committed to pushing reform in these areas but have had different degrees of success. I will argue in this thesis that the achievement in economic policy reform is substantially explained by the degree of executive strength of a president.

The choice of the topic is theoretically and practically important for two reasons. First, by using an institutional approach, this thesis tries to bring political institutions back into the study of Indonesian politics. This is a significant breakthrough because political institutions have long been underplayed in the study of Indonesian politics even after many significant changes in the country’s key political institutions since 1999.
In addition to this improved performance, her administration also made other important achievements in the fiscal-related policy area. First, it passed Law 24/2002 on Treasury Bonds on 22 October 2002 within about one year of its submission to the DPR. This was part of the agreement with the IMF. The law is important to provide a stronger legal base to support the government plan to issue more treasury bonds on both the domestic and international markets. This is also intended to maintain transparency and accountability in the management of treasury bonds. As expressed by Minister Boediono, the law was expected to provide an incentive for private sector involvement which would then ease the budget constraint and improve fiscal sustainability at the same time (Tempointeraktif 06 February 2002). So important was the law that Megawati requested the DPR to propel the process (Sinar Harapan 17 July 2002). The DPR initially voiced its opposition but then approved the law.

Second, at a more practical level, assessing the achievements in economic policy reform provides a bridge to the much broader topic of effective government or government capacity. The comparative literature claims that government capacity, especially in the economic area, is critical to democratic consolidation (Diamond 1997; Gasiorowski and Power 1998; Misher and Rose 2001a; Misher and Rose 2001b; Espinal, Hartlyn and Kelly 2006; Gilley 2006). The failure to improve government performance can lead to what O'Donnell and Schmitter (1986) call 'uncertain democracy'.1 Arguing that government capacity is partly institutionally engineered, research such as this is important for further institutional engineering to improve government capacity in general and policy-making capacity in particular which is critical for the prospect of democratic consolidation.

With these two concerns in mind, this is not theory-testing research. Rather, it develops an alternative way of understanding governance problems in general and economic policy making in particular which has so far been dominated in the debates by the interest-based approach.

1 See also Plattner (1998), Zakaria (1997), Mishler and Rose (2001a), Mishler and Rose (2001b), Espinal, Hartlyn and Kelly (2006), and Gilley (2006) for the discussion on this issue. A more extensive discussion on the types of democracy can be found in Collier and Levitsky (1997).
In this chapter, I will discuss the overall background of this thesis. I will start with a short overview of how political institutions have been underplayed in the Indonesia literature. After that I will address the debate in contemporary Indonesia regarding the effects of the new institutional arrangements in general. Then I bring this debate into a more nuanced issue, namely, the effects of the new institutional arrangements on effective government. After formulating a guiding research question, I will conclude this chapter by presenting my core argument and outlining the whole plan to extend the argument through the thesis.

1.2 Bringing political institutions back into Indonesian politics

For a long time, the importance of political institutions – rules of the game that structure human interactions in the political arena – has been neglected in the Indonesian political literature. Such negligence is especially clear for the working of government institutions, especially the presidency and the parliament. As stated by MacIntyre (1999), scholars have been more interested in applying state-society relations, class analysis, civil-military relations, patron-client relations, intra-elite factionalism, or ethnic and religious politics as well as bureaucracy as their analytical optic to analyzing government performance. The reason is that under an authoritarian regime, political institutions are subject to violation by arbitrary rulers. Moreover, Liddle (1985:69) argues that colonialism in Indonesia 'has left a legacy of only rudimentary government institutions and even less-formed political parties and interest group organizations'. It is also for this reason that the personalities of the rulers occupy the center of political inquiry. Consequently, the easiest way to grasp Indonesian politics is by looking at the preferences, behavior, and interests of the rulers and their cronies. Political institutions are something epiphenomenal or even irrelevant. To understand the performance of the New Order regime (1966-1997), for example, one simply needs to investigate the personality, leadership, and/or preference of Suharto and his 'iron triangle cronies': the Armed Forces (ABRI) which actively supported the regime, the bureaucracy that controlled policy making and implementation, and the business elites that supported the regime and extracted benefits from it (Liddle 1985:70; McLeod 2005a:370). During his era, Suharto acted as the only and arbitrary policy maker, putting all other actors and institutions under his control.

2 See for example Barton (2002a); McIntyre (2005).
This trend has changed dramatically since 1999 in which the 1997 economic crisis played a significant role. It uncovered the very fact of Indonesia’s economic and political foundations in which Suharto’s New Order regime was seen to be a part of the problem, even the problem itself. Moreover, it demystified a long-held idea that democracy is inimical to economic development (Acharya 1999; Dittmer 2007). Although the nexus between economic crisis and transition to democracy is inconclusive (Freedman 2005), institutional reform was seen as unavoidable in bringing about immediate recovery. At the bottom of the project lies the belief that the severity and longevity of the crisis is a more political than economic (McLeod 2000:6). This forced Habibie as the transitional president (1998-1999) to start reforming Indonesia’s key political institutions.

Against this background, political institutions have recently regained their importance in the study of Indonesian politics. Many scholars and organizations have been involved in and/or monitored the process of institutional reform and raised some concerns about its possible impacts on the future of Indonesia’s newly born democracy (Haris 1999; Sonata 1999; UNDP 1999; NDI 2000; NDI 2001; World Bank 2001; Gaffar 2002; NDI 2002; Widjojanto 2002; King 2003; NDI 2003a; NDI 2003b; Sherlock 2003; King 2004; NDI 2004; Sherlock 2004; Stockmann 2004; Manan 2005; UNDP 2005; Sherlock 2007). During the same period, some scholars have turned their attention to look at the working of government institutions, especially the parliament (Fealy 2001; Fatwa 2003; Aminy 2004; Fatwa 2004; Rachman 2004; Amir and Purnomowati 2005; Manan 2005; Ziegenhain 2008), the president (Mahfud 2003; Manan 2003; Soesastro, Smith and Ling 2003; Wiratma 2006) and political parties (Tan 2002; Putra 2003; Kalla 2004; Koiruddin 2004; Tan 2006). This is an acknowledgement that political institutions are of importance for the country. Political structure which was previously overwhelmed by political agency is now beginning to attract at least the same attention (King 2003:3). However, with very few exceptions, no systematic inquiry has been done to assess whether the new institutional arrangements have brought about the expected effects on Indonesia’s social, political, and especially economic conditions. Only few scholars seem to realize that there is a significant connection between the nation’s institutional arrangements and its social, political and economic conditions.
1.3 Locating the debate

In assessing the effects of the new institutional arrangements, scholars and other informed people can be divided into two main groups. The first one argues that the new institutional arrangements have brought about many positive effects. These mainly refer to the fulfillment of democratic principles such as the improvement of civil liberties, human rights protection, public participation, civil society, and freedom of expression and association (Samego 2003; Ghoshal 2004a; Ghoshal 2004b; Stockmann 2004; DEMOS 2005). Others within this group argue that the new institutional arrangements have enhanced the working of checks and balances between the executive and the legislature with the former being highly circumscribed and the latter becoming more independent and assertive in the policy-making process (Tanjung 2003; Fatwa 2004; King 2004). This stands in contrast to the condition under Suharto when the DPR – Indonesia’s House of Representative – was no more than the president’s rubber stamp. Still others point to government’s increased accountability due to the presence of clear punishment mechanisms (Tan 2006; World Bank 2007a). In considering these positive effects, this group is strongly against those voices calling for the return of the pre-reform institutions.

The second group argues that, on the contrary, the new institutional arrangements have had more negative than positive effects on Indonesia’s democracy and people’s living conditions in particular. They also point out that the new institutional arrangements have only benefited some elites with entrenched interests. Other negative effects raised are the prominence of oligarchy, especially within political parties (O’Rourke 2002; Robison and Hadiz 2004), collusive democracy which leads to no policy change and a deficit of accountability (Slater 2004; Slater 2006), widespread corruption at both national and especially local level (Kuncoro 2006), and many more. Part of the explanation for this is the nature of institutional reform which is elite-guided (Törnquist 2005; Ellis 2006) and half-hearted (Haris 1999; Sonata 1999; King 2003). Others also argue that the new institutional arrangements have prevented government institutions from dealing effectively with the country’s social and especially economic problems (Boediono 2005; Bird, Hill, and Cuthbertson 2007; Boediono 2007). At worst, they are a serious liability for an effective government. For this reason, people have even been skeptical about the existing
institutional arrangements despite the fact that they are much more democratic than the previous ones.

Drawing on these debates, this thesis argues that the new institutional arrangements have had many significant effects. Certain aspects of the new institutional arrangements have created problems while others have strengthened the optimism for an effective government and democracy in general. These are inherently engineered within the structure of incentives – both opportunities and risks – created by the new institutional arrangements. For example, while the enhancement of checks and balances between the president and the DPR has put the government under democratic control and made it more accountable to the people, it has at the same time compromised government capacity to respond to national concerns in a timely and effective manner. This is the trade-off a country has to make when choosing certain institutional arrangements but not many people seem to realize it. Since the new institutional arrangements are already at work, it is now time to reflect on their merits as well as their perils and push further reform if necessary. In line with previous concerns, the focus is now on how to transform the new institutional arrangements to be more supportive for an effective government.

To pursue my argument, I will causally connect the new institutional arrangements to a more nuanced but very important issue, namely, effective government or government capacity. This is a common policy challenge all the post-Suharto administrations have had to face. Since they work under different institutional arrangements, they provide a good base for assessing the effects of political institutions. Moreover, assessing government capacity is very important considering the condition of contemporary Indonesia. While democracy was expected to bring about better social, political and economic conditions, especially given the severity of the impacts of the 1997 economic crisis, the results in the field are far from those expected. McLeod (2005a:367) maintains that after the collapse of the New Order regime, ‘Indonesia gained democracy but lost effective government’. This contradicts the initial objective to make institutional reform the means – not the end – for improving the country’s troublesome economic and political conditions. Reform euphoria following the fall of Suharto’s authoritarian regime soon faded away and people started worrying about their real lives. McLeod and MacIntyre (2006:3) articulate this concern in a simple but precise account:
Most people have little interest in politics and government; they are much more concerned about their standard of living, and about their ability to survive when things go wrong. They worry about being able to send their children to school; about their ability to cope with significant illness or injury within the family; about how they may be affected by floods and fires, natural disasters and economic shocks. They worry about their vulnerability to theft, extortion and violence, and to state-sanctioned expropriation of their assets. They worry about the prevalence of catastrophic accidents in the transportation sphere, with trains running off the rails, ferries sinking, planes and buses crashing, and so on.

The concern about the effectiveness of the new democratic institutions is empirically justified. Poor capacity of almost all government institutions at both national and local level has become more a rule than an exception (IFES 2003; DEMOS 2005; IFES 2005; LSI 2006b; Mujani 2006; World Bank 2007). Several examples of this concern can be found. Macroeconomic instability, low economic growth, poor law enforcement, widespread corruption, uncertain business climate, deficient investment due to policy uncertainty, and poor public services are among those concerns. These have all led to ‘deficiency fatigue’ among people (Kassim 2005:174). Frustration over these aspects has even led many people to lost faith in the new administrations while others have become utterly cynical (Tornquist et al. 2004:32). Still others become so fed up with the new administrations that they wish for the return of the Suharto regime given the stability and predictability of the politics and economy (Far Eastern Economic Review 18 December 2003; Ghoshal 2004b:507; LSI 2006a; Sriwijaya Post 23 December 2003). For the same reason, politics which is supposedly an instrument to improve people’s welfare is now widely assumed to be ‘something of a dirty word, used to describe the motivations behind unwanted and unpopular decisions’ (Antløv 2003:75). This is a quite measured response from the people to the performance of governmental institutions. For example, as a representative body, the parliament has notoriously become ‘a more fertile field for wealth and aggrandizement by a barely changed power elite’ (Sherlock 2003:30) where the practices of money politics are commonly found (Wessel 2005:21). The executive branch and the bureaucracy also perform poorly. Similarly, a strong anti-party feeling is expressed by the people due to their attitudes to current politics (Tan 2002:489). Consequently, there is no other way but to
improve the functioning of all public institutions, reforming them so that they can perform their basic functions in serving the people. More than merely paying lip-service to public criticism, such an effort is crucial for democratic consolidation.

Why has institutional reform resulted in such troublesome institutional indeterminacy? What explains the gap between new democratic institutional supply and demand? These are the big questions raised among Indonesians that have driven me to conduct this research.

The first and most popular optic in response to such questions is by looking at the nature of the transition itself and this mainly leads scholars to scrutinize the actors and interests involved. The new institutional arrangements have failed to bring about the expected results since they have been captured by the old entrenched actors such as GOLKAR and the Armed Forces (ABRI) who have a strong motive for maintaining the status-quo. The involvement of these actors has simply made institutional reform a democratic instrument to secure their own vested interests (DEMOS 2005). Under this interpretation, institutional reform does not intend to establish more democratic governance in response to public demand but simply to disguise the entrenched political practices and interests (Widjojanto 2002; Young 1999). Elite compromise, negotiation and pact have become the norm of politics which have led to more continuity than expected change. Understandably, Indonesia faces problems of elitist reform (Törnquist 2005) as reform was piecemeal or half-hearted in its scope and depth. Comparative literatures posit that as far as institutional reform in transitional democracies fails to distance itself from the old authoritarian practices, the prospect of democratic consolidation will be compromised (Valenzuela 1992). This can also explain both the policy and institutional indeterminacy which has triggered persistent public skepticism and has placed government legitimacy at risk as shown by several reliable surveys (Asia Foundation 2003; DEMOS 2005; IFES 2005; LSI 2006).

This interest-based perspective is very powerful and is shared by many scholars of Indonesia. However, it has some limitations. Though self-interested actors do drive politics, they cannot act independently from their macro political environment which is now more democratic. Under the new democratic system, any arbitrary practices are not only tightly constrained, but also punished if found out. If the involvement of self-interested actors is
the main culprit in the problem of policy and institutional indeterminacy, why do these very same actors comply with democratic rules? Even the most notorious arbitrary actor, ABRI, has chosen to play within the existing democratic institutions (Liddle 2002:374-375). This changing behavior implies that there is another structural variable which affects actors in pursuing their interests. Another question is whether it is sufficient to remove these self-interested actors to improve policy and institutional performance, and thereby, enhance the prospects of democratic consolidation.

Another related issue in the interest-based perspective is the fact that it gives inadequate attention to the variation in capacity among post-Suharto administrations. Comparatively, they exhibit quite stark differences in their capacity to deliver expected changes. In pushing politically difficult economic policy reform, for example, there is a wide variation among them, especially in areas which raise strong opposition such as privatization and fuel subsidy reform. What explains this variation? The interest-based approach by itself cannot address this question satisfactorily, but nor can it be simply ignored.

These limitations bring the explanation to the second optic, namely, the choice of political institutions. With the restoration of democratic system, it is now time to connect economic demand to political supply. It is no longer possible to examine economic outcome in isolation from its broader political or institutional context, something which has long been neglected under the authoritarian regime (Ananta and Riyanto 2006:9). This is not to argue that institutional perspective offers perfect explanation for any policy outcomes. It indeed has limitations. However, given the capacity of political institutions to bias the battle over certain policy and by treating interests constant, institutional perspective offers something other perspectives do not.

The institutional approach maintains that political institutions structure political outcomes by creating certain incentives – opportunities and risks – and limiting others. It is argued that certain institutional arrangements produce certain political outcomes. Therefore, the fact that post-Suharto Indonesia faces many difficulties in bringing about expected changes can be explained by the institutional arrangements established since 1999. This thesis will argue that government capacity is partly institutionally engineered. For example, the presence of multipartism and an assertive but fragmented parliament in post-Suharto
Indonesia predictably poses many difficulties for a president in pushing difficult policy initiatives. This is especially true for a weak president in both constitutional and partisan aspects. He or she will have to build alliances with other political parties in the DPR to enact any legislative agenda. More often than expected, a president must buy political support from the DPR through many strategies such as coalition, patronage, and bribery, when he or she is trying to adopt politically difficult legislative agenda. The absence of a legislative majority will almost certainly bring such an agenda to an end. This explains, for example, the reality of the policy status quo when policy reform is desperately required. Institutional arrangements such as these open up chance for self-interested actors to pursue their own interests which sometimes compromise the prospect of reform. On the other hand, a strong president can deal effectively with the DPR and adopt difficult policy reforms when he or she needs to do so. This is the approach I will employ in this thesis.

1.4 Focus and question

Given the complexity of government capacity issues, this thesis will only address policy-making capacity. More specifically, it will look at the achievements in economic policy reform in the post-Suharto era (1999-2007). Following the 1997 economic crisis, all post-Suharto administrations have been forced to adopt market-oriented economic policy reform. Until at least 2003, in cooperation with the IMF, adopting market-oriented economic policy reform was more a necessity than a choice. This was a precondition of obtaining financial support from the IMF and other donors, the failure of which would have had severe consequence not only for their support but also for market confidence in general. This left the government with limited room of maneuver. Even such a populist president as Wahid and a nationalist president as Megawati must commit to this agenda. After that, the graduation from the IMF did not automatically change the requirement. Given the still-vulnerable economic conditions, the government must push further market-oriented economic policy reform. In 2005, for example, given the worsening macroeconomic conditions, President Susilo Bambang Yudhoyono – hereafter SBY – was required to push more reforms of this type.
The experiences from other countries implementing market-oriented policy reform indicate that reform of this type is politically difficult, socially unpopular and economically painful to such an extent that almost every body is ready to put up opposition. Under a democratic system, such opposition comes mainly from within the parliament. In post-Suharto Indonesia, such opposition is notable. The DPR has manipulated populist and nationalist sentiments to block any market-oriented policy reform.

Many informed scholars argue that this opposition is the main obstacle to the adoption of market-oriented economic policy reform in post-Suharto Indonesia. While this argument is widely acknowledged, it must be treated carefully. Looking more deeply into the achievements in economic policy reform in the post-Suharto era will reveal a quite stark variation among administrations. While all post-Suharto administrations faced strong opposition in pushing reform agendas, one administration adopted more economic policy reform initiatives than others. A clear example is in the area of privatization. Strong opposition from the DPR prevented Wahid from pushing his agenda. In this area, during his administration, no single state enterprise was privatized despite a strong commitment to achieving this. This was not the case for Megawati. Her administration also committed to pushing privatization, and also faced strong opposition. Amidst this inimical condition, it privatized many state enterprises, even strategic enterprises where opposition had in the past succeeded in blocking their progress. Another important case is fuel subsidy reform. All post-Suharto presidents committed to pushing reform in this area by cutting the fuel subsidy allocation in the national budget, increasing fuel prices, or a combination of both. Opposition to this initiative was also very strong. Amidst these similarities, three post-Suharto administrations present stark variations in the degree of achievement. Wahid only adopted limited reform, with the incidence of reversal and delay especially in 2000. Megawati adopted significant reform in 2002 with a partial reversal in 2003 and a delay in 2004. Meanwhile, SBY adopted the most significant reform in terms of the scope of the reform and amidst very strong opposition from the DPR. This pattern is quite similar to that seen in fiscal policy reform and investment-related measures. What explains this variation?

The argument pursued in this thesis is that it is not the political opposition which matters but rather the inability of the executive to cope with opposition that substantially explains the variation in the adoption of market-oriented economic policy reform. While political
opposition is almost always there to block reform initiatives, one administration seemed better able to cope with this opposition than the others and, therefore, the adoption of the reform initiatives. In a democratic system, such capacity is indeed embedded in the choice of the institutional arrangements.

Against this background, this thesis will address the following question: how have the new institutional arrangements affected the adoption of economic policy reform in post-Suharto Indonesia?

1.5 Argument

The core argument of this thesis is that the variation in the adoption of economic policy reform in post-Suharto Indonesia is substantially explained by the variation in the degree of executive strength. A president with high executive strength could adopt significant economic policy reform. A president with moderate executive strength could also adopt economic policy reform but it is more limited. Such an achievement is very limited for a president with low executive strength.

In understanding the nexus between the degree of executive strength and the adoption of economic policy reform, this thesis takes the position that institutional arrangements are not the only factor in or even the determinant of such an outcome. It argues that institutional arrangements provide both opportunities and constraints for other factors such as interest and idea to structure certain political outcomes. In this respect, as proposed by MacIntyre (2003:102), institutional arrangements are best understood as a ‘crucial enabling condition rather than as determinant’ of certain policy outcome. Or, borrowing the terms of Weaver and Rockman (1993:447), political institutions are best understood as a structure of incentive which provides certain opportunities and risks.

Another important consideration is that, as in other developing countries, a president with a high degree of executive strength could be dangerous for the country. Executive strength
could equally be used to push through damaging changes to the economy. This thesis proposes that such a threat is far from real in post-Suharto Indonesia. The new institutional arrangements have functioned relatively well to control such behavior and no leader will be stupid enough to pursue such agenda. This is, however, not to say that all post-Suharto presidents have been or are benevolent leaders trying to pursue good policies for the sake of the people. The truth is that they are not. However, as discussed earlier in this chapter, given the limited choice following the 1997 economic crisis and the incredibly high public expectations of bringing about economic recovery, pushing difficult economic policy reform is more a necessity than a choice for them. The involvement of the IMF only confirms the limitations of policy room of maneuver, leaving the government with no choice but to pursue painful measures to improve the economy. No president would be willing to pursue them if social and economic conditions were as normal as one would expect, at least as that of the pre-crisis conditions.

1.6 Concepts and measurement

Two key concepts used in this thesis must be clarified here. The first one is 'executive strength'. As mentioned earlier in the Introduction, executive strength refers to an aggregated measure of a president’s constitutional powers and partisan support. It is therefore not a president’s personality, leadership quality, charisma, or other personal traits such as Neustadt’s ‘power to persuade’ (Neustadt 1990) as seen in the American presidency literature. As will be elaborated more in Chapter 2, a president’s constitutional powers refer to both legislative and non-legislative powers as stipulated in the constitution. In the adoption of difficult economic policy reform, with limited legislative veto and decree powers, the most important aspect is the constitutional protection of the president’s security of tenure. Meanwhile, partisan support refers to the status of a president in the legislative arena, either majority or minority. To be successful in pushing any legislative agenda, a president is required to have a legislative majority by especially establishing coalition. The fact that all the post-Suharto presidents came from a minority parties makes building coalition unavoidable and this is accomplished through the distribution of cabinet posts to coalescing parties.
Looking at these two aspects, executive strength is high if a president has constitutional protection over security of tenure and is supported by a legislative majority. Executive strength will only be moderate if a president only has one of them, either a protected security of tenure or legislative majority. The degree of executive strength is low if a president has neither of them.

The second key concept is ‘economic policy reform’. In this thesis, it refers to policy issues where significant changes are required amidst strong political opposition. Even when readers find the terms ‘policy reform’ or ‘reform initiative’, both refer to economic policy reform. To measure its achievement, this thesis will compare what one administration actually tried to adopt to what it actually adopted. A simple measurement of this is whether or not the proposed economic policy reform is adopted.

Given the complexity of economic policy reform, this thesis will only focus its assessment on areas of policy-making which involve the president and the DPR, where the latter poses a strong opposition to the former’s reform initiatives. Using this standard, all executive’s reform initiatives that do not face opposition from the DPR are excluded from the assessment. It also excludes reform initiatives proposed by the DPR because this thesis aims specifically to highlight the ability of presidents to pursue their policy reform agenda. Moreover, it will only focus on economic policy areas which the executive maintains as important priorities to bring about economic recovery. This brings this thesis to investigate two important policy areas, namely, fiscal policy and investment-related measures. It uses fuel subsidy as a case study to look more closely into the effects of executive strength on economic policy reform and compare its achievement among the three post-Suharto administrations.

By clarifying these concepts, this thesis expects to avoid the problem of analytical tautology. Some might argue that ‘strong’ executive will certainly dominate policy-making process and get what it wants. Again, executive strength is an institutional term used in this thesis to refer to an aggregated measure of a president’s constitutional power and partisan support. It is employed to illustrate the effect of certain institutional arrangements on policy outcomes.
1.7 Data collection

To extend the above argument, this thesis employs qualitative method with a case study. The method is suitable to answer ‘why’ and ‘how’ questions (Yin 1989:23; Baker 1994:299; Macpherson et al. 2000:52; Long and Goodfrey 2004:183) which are the main concern of this thesis.

This thesis uses both primary and secondary data. It started with secondary data by conducting documentary desk studies, through which, all relevant documents or records, previous researches, publications, and other relevant materials on institutional reform, economic policy reform, the budget making, fuel subsidy reform, executive-legislative relationships, and other related data were collected. They came mainly from the libraries, reliable newspapers and magazines, journals, internet resources, research reports, and meeting materials and minutes of meeting in the DPR, the Ministry of Finance, the Ministry of Energy and Mineral Resources, and the Ministry of National Development Planning. Documentary data are very important as they are textual realities which contain significant meanings from any event. These documentary data helped focus the interview, develop the questions in a more structured manner, and also clarify some points which were still unclear or were doubtful. Also important is that using this technique helped enhance the objectivity and valid inference as it could triangulate secondary data with primary data, and vice versa (Punch 1998:190).

On the other hand, primary data were collected through conducting an in-depth interview with key informants, especially the leaders and members of parliament (Budget Committee, Finance Committee, Energy Committee, and fractions), government officers in the Ministry of Energy and Mineral Resources, the Ministry of Finance, the Ministry of National Development Planning, the Ministry of Trade, the Ministry of Industry, the Central Bank, and the Office of Parliament Secretariat, experts, researchers, and informed observers. Involving this wide range of informants with different backgrounds enabled this thesis not only to avoid selection bias but also to produce more balanced information.

The interview was used not only to deepen the understanding on the information from the
secondary data but also for the purpose of crosscheck. It also enabled to capture both external reality (facts or events) and internal experience (perception, interpretation, or even feelings) of the informants. From the interview, this thesis got valuable information on what really happened prior to, during and after certain important events, especially those of politically sensitive events with very limited or no coverage at all. The interview was conducted in a semi-structured manner to also cover other related information during the process.3

Given that this thesis uses a relatively new approach in the study of Indonesian politics, interview was conducted with only 50 key informants comprising 'gate keepers, individual elites, and experts about individuals, events, processes or institutions' (Moyser 1988:114-115).4 The gate keepers5 and individual elites come mainly from the DPR and some executive bodies such as the Ministry of Finance, the Ministry of Energy and Mineral Resources, the Ministry of National Development Planning, the Ministry of Trade, the Ministry of Industry, and the Central Bank. They were asked for their experiences in the policy-making process, especially regarding fiscal policy and investment policy reforms as well as fuel subsidy reform. A special arrangement was made to keep their identity anonymous.

Beyond interview and documentary data, this thesis also employed observation as a complementary technique to get information. In this respect, I attended some parliamentary sessions when important agenda were discussed and decided upon by the DPR and the executive. The purpose of this approach is to better understand the legislative process: how a bill is proposed, debated, and finally decided, how actors behave in the legislative arena, how they bargain, and others. Following the process provides more insights on why policy outcomes are as they are.

3 Fontana and Frey (2000:653) argue that semi-structured interview enables researchers to get an understanding of a complex perception, action, or process without any a priori categorization or concept. This is also to show that respondents are the most crucial element of the process while putting researcher as an active listener.

4 The number of interviewees was arbitrary as there is no common agreed standard. Most of the interviewees are political and bureaucratic elites so that this research can be categorized as an elite research (Moyser 1988).

5 Gate keepers are those whose approval is mandatory for a researcher to proceed with collecting data in their respective jurisdiction. They also have key information from which the researcher will pursue further investigation.
For data analysis, this thesis used an internal assessment of the results of the interview and triangulation. The latter was applied to compare primary data with secondary data as well as data from interviewees. This is important to confirm, clarify or enrich any perception before a more general inference and concepts are constructed and to check the consistency and coherence, and therefore, the internal validity of data (King et al. 1994:479; Hall and Rist 1999:295-6; Denzin and Lincoln 2003:8; Janesick 2003:66-67; Stake 2003:147-8; Verschuren 2003:131; Tetnowski and Franklin 2003:161). It also employed among-steps triangulation technique as proposed by Miles and Huberman (1994:12) and peer-review. Moreover, this thesis uses a historian-sociologist-like approach. While some documents speak for themselves, others must be unpacked and analyzed to obtain the deepest meaning, for which this research employed an interpretive understanding and or structural approach (Punch 1998:230). It also relied on the existing theories to develop the analysis, compare, and or even criticize them. Findings from the field were linked to and tied together to the existing concepts or theories to enrich their virtue and were used to develop the new ones.

1.8 Chapter organization

This thesis is organized into six chapters. In Chapter 2 it will discuss the existing theories on the linkage between institutional arrangements and government capacity. It will look especially at the theoretical nexus between institutional arrangements and government capacity to adopt economic policy in politically difficult areas. It starts by discussing what scholars of Indonesia say about the topic and link their views to the broader literature and vice versa. This is to address the limitations of scholarly work on this topic in contemporary Indonesia. Due to some limitations, partly theoretical and partly empirical, it then develops executive strength as the optic used to illustrate the argument that the new institutional arrangements matter for the achievement in economic policy reform. It concludes this chapter by developing the research framework and the core argument for the rest of the project.

6 In among-steps triangulation, research process is seen as a collection of concurrent streams or activities, which are mutually related. Data reduction, data display and conclusion drawing occur concurrently. This enables researchers to check the consistency and coherence, and therefore, internal validity of the data since data will speak for themselves (Fontana and Frey 2002:661).
Chapters 3 to 5 are the core of this thesis. Given the complexity of the issue, it will discuss each post-Suharto administration separately regarding how the new institutional arrangements structure the degree of executive strength which then affects the achievement in economic policy reform. Each chapter will be presented using the same structure. In Chapter 3, it discusses what happened to economic policy reform during the Wahid administration (1999-2001). It starts by assessing the achievements in economic policy reform during his term in office. It then links this achievement to the degree of executive strength prevailing at the time. The core argument of this chapter is that since Wahid had low executive strength, his administration only adopted limited economic policy reforms especially in politically difficult areas. The period under his administration epitomizes what some scholars call the 'government by legislature' or an Indonesian version of the 'legislators as chief executive'. This is mainly due to Wahid’s vulnerability to dismissal by the parliament.

In Chapter 4, this thesis will discuss what happened in economic policy reform under the Megawati administration (2001-2004). Though Megawati was elected by the parliament, she had a stronger institutional status than Wahid. The constitutional amendment enacted right after her election restored the power of the president by the introduction of direct presidential election and making impeachment more difficult. Her main obstacle came from the lack of partisan support though she established an oversized coalition cabinet. This combination provided her with improved executive strength, at least compared to Wahid. This institutional underpinning significantly explains the improved achievements in economic policy reform under her administration.

Chapter 5 discusses the achievements in economic policy reform under the SBY administration (2004-2007). The institutional arrangements in this period gave the president a high degree of executive strength, the highest among all post-Suharto presidents. He was directly elected by popular vote and established an oversized but more consolidated coalition. These factors gave him sufficient political capital to achieve his own policy agenda. This institutional underpinning enabled him to adopt many contentious economic policy reforms in a way that was clearly different from his predecessors.
After discussing the performance of each administration, this thesis then moves to the conclusion in Chapter 6. In this chapter, it summarizes the key findings with the overall conclusion that the degree of executive strength affects the adoption of economic policy reform. Drawing on the findings, it will conclude that the new institutional arrangements have already had a significant effect on government capacity.
2

Political institutions and economic policy reform

2.1 Introduction

This chapter will present the theoretical framework adopted to investigate the effects of institutional arrangements on economic policy reform. First it will discuss general issues pertaining to institutional reform and government capacity. This extends the discussion in Chapter 1 and puts it into a more proper context. The key point for this section is to show the real challenges a transitional government must cope with especially if the country also faces economic crisis, as Indonesia has had to since 1997.

The next section will move to the primary issue of this thesis, namely, how institutional arrangements affect economic policy reform, especially in politically difficult areas. For this purpose, it will first locate the debate in the literature on Indonesia and link it to the broader comparative literature with regard to pursuing policy reform. Several institutional approaches are reviewed, such as the importance of power concentration, elite insulation, elite autonomy, elite cohesion, and veto player. While these arguments are widely acknowledged, they are insufficient to understand the achievements in economic policy reform in post-Suharto Indonesia. Therefore, this thesis will instead look at the degree of executive strength as the approach for this thesis. This is an aggregate measure of a president's constitutional powers and partisan support; it does not go into the personal traits of any president. Using this approach enables me to investigate the variation in the achievement of economic policy reform of post-Suharto administrations. The key argument is that institutional arrangements which compromise executive strength prevent a president from adopting politically difficult economic policy reform while institutional arrangements which strengthen it have the opposite effect. Based on this core argument, the variation in the degree of executive strength among post-Suharto administrations will be presented in the final section.
2.2 Institutional reform and government capacity

The coming of institutional reform and the victory of democratic ideas in transitional countries have at the same time raised great concern about government capacity or the effectiveness of the new democratic institutions (Weaver and Rockman 1993:1). In this context, sometimes tensions arise between efficiency and representation or between democratic governance and effective governance. As articulated by Maravall (1993:77), 'once democracies are reestablished after a period of dictatorial rule, new problems emerge: the efficiency of the new political system, and not just its legitimacy, becomes the main issue – that is the capacity of democracy to solve problems and fulfil expectations'. It is in this context that the discussion needs to be extended to cover the quality of democracy (Diamond and Morlino 2004), not just democracy per se. As discussed briefly in Chapter 1, this is similar to what post-Suharto Indonesia is facing.

Such concerns must be put in perspective. To a certain degree, they are understandable as part of the process of democratic transition. Indonesia has come a long way to end authoritarianism, only to witness that still a much longer journey lies ahead to achieve what it has dreamed of. Moreover, the citizens often have a somewhat unrealistic expectation that the new democratic government will bring about immediate changes. This is reasonable since the country has been dealing with an economic crisis since 1997 which was then followed by democratic transition. Under such circumstances, the need for better governmental performance confronts a number of difficulties such as low economic growth, high inflation, enormous government debt, limited financial resources, and most importantly, the fragmentation of power resulting in difficulties in taking concerted action to cope with those problems. It is in this context that Indonesia, as other new democracies, finds such a daunting challenge. There is clearly a wide gap between what the people need and the capacity to meet this need. Haggard and Kaufman (1989:59-60) argue that the combination of an increased level of political mobilization and conflict due to prolonged repression by previous authoritarian regime on the one side and political freedom on the other, the lack of political consensus among elites as to how to manage the country, and the high turn-over of personnel in almost all government institutions renders the challenge for new democracies even more complicated. Given such confusion, government’s
determination to perform its functions is more than critical as the prospect of nascent
民主机构的成立依赖于它（Pereira et al. 1993:1）。

Since the issue of government capacity is so broad, this thesis will confine its analysis to
policy-making capacity. Beside policy implementation, policy-making is one of the most
critical stages in public policy: it is where interests are aggregated and sanctioned legally by
the government. Policy-making clearly reflects the fights among different interests and
priorities of many actors both inside and outside the government. It is politically sensitive
in the sense that it includes certain interests while at the same time excludes others (Stone
2002). It is this political fight that makes policy-making an interesting area of inquiry.
Among the central questions are why public policy is as it is, why it includes certain
interests but excludes others, why government can only provide a slow response to certain
policy issues but a quick one to others, and many other related questions. Therefore,
conceptualization and operationalization are extremely important here.

When looking at policy-making capacity, scholars use different concepts and measurements
for different purposes. Some scholars measure policy-making capacity as the number of
pieces of legislation passed each year as well as their speed of passage (Mezey 1989; Fealy
2001; Rülland et al. 2005). Such an approach has the disadvantage of making no distinction
between important and unimportant bills. Therefore, other scholars use more substantive
indicators by looking at the dynamics of legislative making and the content of the bills such
as government capacity to control the legislative agenda (Fatwa 2004; Negretto 2004)
especially in systemic or strategic agenda (Gleiber and Shull 1992; Mouv and MacKuen
1992; Eshbaugh-Soha and Peake 2004); others focus on effective presidential leaderships
(Weatherford 1994; Price 1996; Aberbach and Rockman 1999), particularly concerning
interest representation, procedural rationality, and public accountability (Hult 2000); and
still others look at the degree of government responsiveness (Shapiro and Jacobs 2001;
Manza and Cook 2002).

A more generally used measurement for assessing policy-making capacity is by looking at
capacity to make and implement policy change (decisiveness) and capacity to sustain policy
in the long run once it is made (resoluteness) (Cox and McCubbins 2001:26-7). These two
properties work in the opposite direction: the more decisive a government is, the less
resolute it is; and vice versa. Similarly, MacIntyre (2003) defines capacity as ability to maintain credible commitment on one side and ability to respond quickly to policy problems on other side. The challenge for modern democracies is to find a balance between these two properties and institutional arrangements can meet such a challenge through certain types of political engineering.

While all these capacity attributes are important for understanding contemporary Indonesia, this thesis will simply look at the adoption of economic policy reform when the executive plans to or must do so. More specifically, it focuses its assessment only on policy areas which require significant changes as proposed by Bates and Krueger (1993). This is in line with the context of economic reform since the coming of the 1997 economic crisis. To propel economic recovery and as part of the agreement with the IMF, the government must adopt a number of market-oriented reforms, or neo-liberalism as many critics of the IMF in Indonesia might call it (see for example Baswir 2003; Baswir 2006; Wibowo 2003). Even after the graduation from the IMF program, the challenge for Indonesia to push further reform in key economic areas remains reasonably high. This applies especially to microeconomic or business-related areas such as investment.

Experiences from other countries implementing similar IMF-imposed policy packages show that market-oriented reform always triggers opposition since most people oppose change, even the government itself, should it have other alternatives. These are initiatives which are politically difficult, socially unpopular and economically painful and, therefore, many people are ready to block the process. Even if there is consensus among key players on the importance of reform, nobody is ready to bear the cost. These initiatives generally trigger strong political opposition given the potential (or real) losses they bring, the ignorance of which can be costly. However, as the nature of policy reform investigated in this thesis implies, pushing such change is more a necessity than a choice considering the high stakes at hand and the limited alternative available to the government. The government has no choice but to change the existing status-quo in a timely and determined way; any

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7 The authors define policy reform as 'significant changes in a sizable number of economic policies' (Bates and Krueger 1993:5). Therefore, not all policy changes will be addressed in this thesis. It will focus only on those policies with economic and political significance. A more loose definition is offered by Grindle and Thomas (1991:4), defining reform as 'deliberate efforts on the part of government to redress perceived errors in prior and existing policy and institutional arrangements'.
delay could be even costlier.

There are many market-oriented policy initiatives with contentious nature such as maintaining fiscal sustainability, trade liberalization, privatization, divestiture, tax reform, price deregulation, and subsidy removal. Once implemented, policy measures such as these will clearly bring potential losers in the short run on one side and unspecified winners in the long run on the other side (Bates and Krueger 1993:456; Biglaiser and Brown 2005:672). Moreover, while potential losers are more organized, winners tend to be self-evident in the future (Nelson 1989:8; Schneider 2004:458). This is because the risks potential losers will have to bear are much clearer than the benefits winners might enjoy. These are measures which ‘tend to make things worse before they make them better’ (Rodrik 1996:29). That is why losers become politically active opponents while winners express no immediate or concerted support and instead take a comfortable stand of ‘wait and see’. Haggard and Kaufman (1995:156) summarize the problems in pursuing policy reform of this type into three common areas: the dilemma of collective action, distributive conflicts, and policy discount that policy makers make with regard to successful reform.8

Cutting the fuel subsidy is a clear example and Indonesia has been dealing with this issue since the 1997 economic crisis. While the initial purpose was to control the budget deficit by eliminating inefficient and ineffective resource allocation – to which most people agree – it potentially affects inflation, unemployment, social unrest, and other redistributive effects for the people. It is also politically difficult because it incurs costs that are concentrated, immediate and highly visible while the benefits are contingent, diffuse and long term (Nelson 1989:5; Remmer 1998:4; Williamson and Haggard 1994:531). Moreover, for reform initiative of this type, people have a ‘negativity bias’ (Pierson and Weaver 1993:110): they are more aware of (potential) pains than of equivalent gains. As such and this is very important, an initiative of this type is not only unpopular but also raises tension between policy reform and democracy (Przeworski 1991:161), at least in the

8 While the dilemma of collective action and distributive conflicts are recognized widely and investigated accordingly, less attention has been paid to the problem of policy discount. This generally refers to a situation when the incumbent government is relatively unwilling to take a painful measure considering that the gains from such an initiative are long-term in nature and will go to the next government (Haggard and Kaufman 1995:156).
short term. At worst, democracy is more a liability than an asset for the success of a policy reform initiative of this type. However, adopting a policy reform against democratic principles would endanger not only policy legitimacy but also government legitimacy in general up to a level where no government would be willing to bear the risk. The tension then is how to adopt this “undemocratic” agenda through a democratic procedure. In essence, the main challenge for pushing difficult policy reform of this type is how to create a balance between technocracy and democracy.

Privatization also faces the same problem. Experiences from countries implementing this initiative show that the key success factor is more political than technical (Desai and Goldberg 2001; Banerjee and Munger 2004; Rahman et al. 2004; Pejovich 2005; Kaufman 2007; Vis and van Kersbergen 2007). On the one hand, opposition from actors with entrenched interests who have enjoyed benefits in the past and will lose them once new policy is implemented is understandably strong. Under a democratic system, these actors may even play within the rule of the game and try to take advantage of it. In the Philippines during the Ramos administration, for example, the Congress was dominated by a reasserting oligarchic class, making reform poorly targeted (Araral 2006:271-2). These reviving actors sometimes manipulate ideological, nationalist and populist sentiments arguing that the main justification for opposing the privatization of state-owned enterprises, regardless of how insolvent they are, is to protect the public interest. Privatization, for them, will put public interest at risk, and as such, it is against democratic principles. Such justification is especially common in countries with certain constitutional provisions requiring state ownership for certain strategic businesses on which most people depend, such as in the case of Indonesia (Choirie 2004:13). On the other hand, the support for such a measure is not only dispersed but also elitist in nature even among the policy makers.

9 While this argument is widely held, it must be viewed with caution. Fish and Choudhry (2007) argue that policy reform under the banner of the Washington Consensus or economic liberalization enhances rather than undermines democratization.

10 Article 33 of the 1945 Constitution stipulates that (1) the economy shall be organized as a common endeavor based on the principle of the family system; (2) branches of production which are important for the state and which affect the lives of most people shall be controlled by the state; (3) land and water, and the natural resources found therein, shall be controlled by the state and shall be exploited for the maximum benefit of the people; (4) the management of the national economy shall be conducted on the basis of economic democracy upholding the principles of togetherness, efficiency with justice, sustainability, environmental perspective, self-sufficiency, and keeping a balance in the progress and unity of the national economy. Clause (2) is the most controversial one and is frequently used to oppose privatization.
To conclude this section, adopting economic policy reform in a politically difficult area and sustaining it once it is decided present overwhelming challenges, especially for a transitional country such as Indonesia. While the content of these initiatives is often against the principles of democracy, it must be decided within democratic rules. The following section will discuss how scholars of Indonesia have responded to this challenge.

2.3 Institutional arrangements and economic policy reform

Indonesia's economic policy reform since 1998 presents a mixed picture. It varies across issues and times. A dominant view argues that it has failed to progress and bring about expected results, especially when economic recovery is used as its short-term target. This is only partly true, however, and one must not ignore the variation in the achievement of each post-Suharto administration in the adoption of economic policy reform. Comparatively, there is stark difference in the degree of achievement during this period, with one administration adopting more policy changes than others, especially for politically unpopular and difficult measures. What explains this variation?

To answer this question, comparative literature provides abundant resources. A good point of departure is the work of Grindle and Thomas (1991). They offer a theoretical framework for understanding policy reform from society-centred and state-centred perspectives. The other important contribution is the works of Nelson (1990), Haggard and Kaufman (1992), Bates and Krueger (1993), Williamson (1994), Tommasi and Velasco (1996), and Rodrik (1996). The inquiry into answering the question also benefits from previous researches on individual countries from Latin America to Southeast Asia to Eastern Europe. For example, Mariscal (2004) argues that the difference in policy response toward telecommunication reform in Mexico, United States, New Zealand and Brazil is explained by the structure of political institutions and policy context in each country. Similarly, Bambaci et al. (2002) maintain the importance of inter-actor bargaining and general rules of political game in understanding the outcomes of economic policy reform in Argentina. Araral (2006) also gives important contribution to the literature by emphasizing the importance of leadership, policy attributes and political rules of the game in understanding economic policy reform in
the Philippines. The cases of privatization in Russia (Desai and Goldberg 2001) and Central and Eastern Europe (Pejovich 2005) also send strong message on the importance of ideas, interests, and political institutions. More generally, Banerjee and Munger (2004) investigate market-oriented reform in developing countries and find that political institutions, foreign aid regimes and property right development level are significant determinants of policy reform. Basically, though these authors present different answers, all seem to acknowledge that a decision to change policy status-quo in terms of timing, scope and pace depends on many variables. Some of the variables are embedded in the policy makers such as leadership, ideas, and interests while others are institutionally embedded.

With some exceptions, scholars on Indonesia also employ these perspectives when confronting the above mentioned question. In general, these scholarly responses can be put into two groups. The first group of scholars focuses their inquiry on the effects of interest or rent-seeking actors while the second one locates its argument in the existing institutional arrangements.

2.3.1 Interest-based approach

The central claim of scholars who maintain the effect of interest is that the scope and speed of reform is a function of bargaining between platonic guardians and state predators. Basri (1999), for example, argues that economic policy reform is a result of bargaining among the government, interest groups and also multilateral institutions such as the IMF. This is especially true for Indonesia during the early years of economic crisis until the end of 2003 when Indonesia graduated from the IMF program. During this period, the role of the IMF was exceedingly important since Indonesia relied on its financial support to calm market turbulence. As one would expect, interest groups also played an important role in the (economic) policy-making process and tried to structure the content to safeguard their interests. The government, on the other hand, has the responsibility to maintain the balance between all conflicting priorities and interests, including its own interests. With many actors involved, the cost of consultation also increases. This has resulted in policy reform being limited in scope, slow in speed and poor in its content.

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11 This requirement sometimes deprives optimal policy so that only a second-best alternative can be pursued.
This line of argument is powerful and it captures almost all reform initiatives in the post-Suharto era. The transition to democracy has opened up the policy-making arena for those having interests in certain issues, making the policy process tremendously noisy and ineffective. However, it ignores the variation among post-Suharto administrations in adopting economic policy reform. It might be more helpful and indeed powerful to assess the performance of each administration discretely. A flaw soon appears if such an argument is placed in a comparative perspective, taking all post-Suharto administrations into account.

One administration apparently performed better than others in adopting economic policy reform amidst strong opposition from certain interest groups. Even with the pressure of the IMF, such variation still existed where the Wahid administration and the Megawati administration presented a stark contrast (Boediono 2002; Martinez-Diaz 2006). This is also true for the SBY administration when it adopted many more policy reforms amidst strong opposition from interest groups and after the graduation from the IMF program. Therefore, an alternative explanation must be sought, especially to better capture the variation among the post-Suharto administrations.

A similar interest-based argument is proposed by Hadiz and Robison (2003) and Robison and Hadiz (2004). These scholars argue that Indonesia’s market-oriented reforms were continuously compromised by predatory oligarchic interests. For them (Hadiz and Robison 2003:2):

...while neo-liberal economists believed that progressive macroeconomic reforms would, in themselves, be sufficient to transform and undermine rent-seeking interests, private oligarchies controlling the state apparatus and business proved able to hijack them to consolidate and extend their own position. They used market reforms to seize lucrative monopolies formerly vested in the system of state capitalism and its state-owned sector.

These scholars also realize the importance of insulation of reformist technocrats from predatory forces. However, they do not identify this as the main culprit in the failure of neo-liberal reforms in the post-Suharto era. They instead point to the failure in establishing
'a politically cohesive and effective coalition to drive the neo-liberal agenda' (Hadiz and Robison 2003:2; see also Robison and Hadiz 2004:12).

This argument is also acknowledged by other scholars of Indonesia (Munir 2001; O'Rourke 2002). Again, its main flaw lies on the fact that it poorly addresses the variation among post-Suharto administrations and policy areas since one administration performed better than others in one if not all policy areas. For example, the Megawati administration performed better than the Wahid administration in pushing privatization forward despite the fact that both faced strong political opposition from entrenched interests. Drawing on the interest-based argument should therefore indicate a substantially similar pattern of policy outcome across these administrations.

Still other scholars point to opposition from anti-market groups in the society as the main culprit in the slow progress of policy reform in the post-Suharto era. Using the case of trade liberalization, Soesastro and Basri (2005:10) argue that the presence of protectionist groups that are still prevalent and hold key positions in both the government and the business sector has compromised market-oriented reform. The fall of Suharto and the coming of a democratic system have not automatically eliminated the rent-seeking activities of these groups. On the contrary, the coming of democracy has enabled these groups to organize lobbies for certain policies at the cost of the whole society. Similarly, Prasetiantono (2005) points to parliament's opposition as the main political obstacle to the policy-making process in privatization in the post-Suharto era. This stands in contrast to what happened under Suharto when he could push privatization without any serious challenge. Once again, this seemingly convincing argument fails to explain why one administration performed better than others in adopting policy reform. An alternative explanation must therefore be found and this brings me to look at the institutional arrangements in each administration.

2.3.2 Institutional approach

While recognizing the importance of interest, the second group of scholars links the achievement in policy reform to the choice of institutional arrangements and argues that the new democratic institutional arrangements have had a significant effect on achievements in
policy reform. This is to argue that interests alone are not a sufficient explanation to understand the achievement in policy reform. Under a new democratic system, these interests have captured the existing institutional arrangements and used them for their benefit. The variation among post-Suharto administrations in the adoption of policy reform can therefore be examined by looking at specific institutional arrangements under each administration, in order to find an explanation for it.

In maintaining the importance of institutional arrangements, these scholars mainly point to the concentration of power in or the insulation of policy-makers. Martinez-Diaz (2006:406), for example, argues that the fragmentation of power in the post-Suharto era is inhibiting effective policy-making, including government efforts to adopt economic policy reform toward economic recovery. This appears to have been true under the Wahid administration when many new democratic actors entered into the policy-making arena, making it difficult to manage conflicting priorities and push policy reform agendas forward, especially those with political significance. Similarly, drawing on the lesson from the Suharto era, Boediono (2005:318) emphasizes the importance of having a strong team with sufficient protection from external pressure to enable it to adopt any reform agenda. He even proposes to insulate economic policy-making from politics, something that he also realizes is unfeasible under the new democratic system given the fragmentation of power (Boediono 2007:8; Boediono 2005:317).

That the fragmentation of power is a recipe for policy paralysis is acknowledged by some scholars and this generally leads them to refer to what happened under Suharto. Drawing on the experience of the New Order regime in undertaking far-reaching policy reform in the 1980s, Azis (1994:397-8) and Sadli (2002:39), for example, argue that concentration of power enabled Suharto to adopt policy reform in that period in a relatively effective manner. This is because he controlled both the legislative and judiciary branches and was supported by GOLKAR in the legislative arena. He maintained full control over the course of the policy-making and insulated his economic team from political pressure. This, however, must not be exaggerated. MacIntyre (1992:150) argues that certain interest groups also involved in that process, resulting in reduced insulation of the policy process (see also Rosser 2002:12). Now in the post-Suharto era, as power becomes highly fragmented among
many political actors, government decisiveness in policy-making process is simply a distant memory.

The importance of elite insulation or power concentration for pushing difficult economic policy reform is widely acknowledged in the comparative literature (Callaghy 1989:122-3; Haggard and Kaufman 1989:71; Nelson 1990:25; Maravall 1993; Pierson and Weaver 1993:143; Remmer 1998:5; Mariscal 2004). Until the early 1990s, the first generation of market-oriented reform even took the insulation of technocratic team for granted (Santiso 2004:272). Pereira et al. (1993:9), for example, maintain that since policy reform must confront organized opposition from potential losers, a minimal condition for success is to consolidate reform supporters to be strong enough while at the same time marginalizing those who resist policy reform to such a degree that they become too weak to be an effective opposition. This is important to create a degree of insulation for decision makers. 12

Another version of power concentration or insulation is referred to as elite autonomy. Williamson and Haggard (1994:577) argue that institutional arrangements which guarantee an elite’s relative autonomy will facilitate the rise of strong and visionary executive leadership to adopt reform in difficult policy areas. Similarly, Lolos (1998:93) concludes that while the absence of political consensus among elites, strong opposition, party polarization and an incoherent economic team are important, it is the lack of autonomy in the hands of the executive that matters most for the failure of policy reform. The executive that lacks autonomy will be under real pressure from strong political opposition and this makes the decision-making process more political than technocratic in nature. Mariscal (2004:93-94) further maintains that only an autonomous executive can adopt radical policy change. So important is elite autonomy that scholars even call for the presence of an autonomous state which can guarantee that ‘those in power are sufficiently entrenched so that within a fairly wide range they may pursue their objectives without paying very much regard to any political opposition to the policies undertaken’ (Lal and Myint 1990 quoted in

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12 The degree of insulation itself depends on several factors, both situational and institutional, such as elites’ perception of the current condition especially under economic crisis, the extent to which policy-making can be accomplished through a more economic than political approach, elite autonomy from socio-political pressures, the capacity of state bureaucracy and the level of economic development, and the influence of external factors and actors (Callaghy 1990:263).
Krueger 1993:61). When the decision makers are sufficiently autonomous, policy reform can be pushed forward even amidst strong opposition from its surroundings.

Based on these arguments, scholars have also looked at more concrete institutional arrangements which can create power concentration, insulation or elite autonomy. One group of scholars looks at the performance difference between an authoritarian system and a democratic regime. The argument that an authoritarian regime can perform better than a democratic government in adopting difficult policy reform is then broadly challenged (Bates and Krueger 1993:459; Haggard 1986; Haggard and Kaufman 1992:32; Remmer 1986; Williamson and Haggard 1994:568). With the coming of the third wave of democratization (Huntington 1990), a second group of scholars then locates the search within democratic regimes only and tries to explain the variation among them. It is argued, for example, that concentration of power is only present under parliamentarism (Weaver and Rockman 1993:17; Shugart and Mainwaring 1997:31; see also Cheibub 2002:285). Moreover, as many critics of presidentialism argue, the dispersal of legislative powers between the president and legislature under the separation of power system tends to make it a system of gridlock, stalemate, or deadlock (Shugart and Carey 1992:33; Linz and Valenzuela 1994; Cox and McCubbins 2001:30). It is also argued that elite autonomy is difficult to achieve under divided governments or governments with checks and balances, multiple veto points, federalism, and a strong parliament (Bergara et al. 1998:23).

A third group of scholars tries to extend the debate beyond the presidentialism-parliamentarism dichotomy by looking at the variation within each regime type. They look at, for example, the combination of regime type and more micro institutional characteristics such as electoral rules, party system, parliament structure, and federalism. Mainwaring (1993) provokes the debate by arguing that presidentialism and multiparty are a difficult

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13 Remmer (1986), for example, finds no systematic difference between authoritarian regimes and democratic governments in implementing structural adjustment and stabilization programs. Haggard (1986) and Haggard and Kaufman (1992:32) even find no common pattern to confirm the argument on the merit of authoritarianism. Some authoritarian regimes performed poorly in undertaking such programs while certain democratic government could accomplish such mission in a fairly comprehensive manner.

14 These strong constraints sometimes force the executive to avoid risk and it will only push policy reform as far as it provides immediate gains rather than future benefits; in this, opposition is relatively moderate if not absent (Merlevede and Schoors 2007:42).
This is because of the permanence of executive-legislative conflicts, difficulties to establish coalition, and ideological polarization. These three properties make power concentration impossible under presidentialism.

The general argument of these groups is that institutional arrangements which disperse power pose difficulties for effective policy-making, especially for the adoption of difficult economic policy reform (Bergara et al. 1998:21). This is especially true for presidentialism or a combination of presidentialism and multiparty. The opposite is true for majority governments or party governments such as Westminster two-party systems (Maravall 1993:115; Pierson and Weaver 1993:143). This argument is broadly challenged. Bates and Krueger (1993:455) even conclude that countries undertaking economic policy reform rarely have concentrated power. Conflicts between the executive and legislative or between the military and civil society, different interest groups trying to occupy public institutions, and partisan clashes under new democratic institutions are among those factors that make power concentration almost impossible, yet some progress have been achieved in those countries. Haggard (1986) also cites countries which have a high degree of power concentration but have failed to accomplish determined policy reform such as Zaire and Haiti, two authoritarian regimes implementing the IMF Extended Fund Facility Program. In a more general sense, policy elites dealing with policy reform are never fully autonomous (Grindle and Thomas 1991:37).

In addition to this criticism, scholars also raised concerns about the democratic requirement. For policy reform to be sustainable, its speed must be balanced by one other important concern, namely policy legitimacy. In many cases, policy reform can only progress as far as it achieves broad public support. The opposite is also true: a lack of public support has often compromised policy progress in a more substantive sense. Policy as well as government legitimacy is at a critical point where people keep posing opposition to policy reform which sometimes leads a government to back down its already-announced decision. This only places government legitimacy at risk without any real gain. Even in the

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15 His 'difficult combination' thesis has triggered widespread discussion both to confirm and or falsify it (see for example Shugart and Carey 1992; Stepan and Sachs 1993; Power and Gasiorowski 1997).

16 In defense of presidentialism, some scholars argue that the concentration of power has the disadvantage of concentrating the accountability in the hands of policy makers. For example, a prime minister can be easily punished if he or she pushes unpopular reform initiatives. For this reason, parliamentary governments are argued to have less opportunity (more risks) to adopt difficult policy reform than under a presidential system (see for example in Weaver and Rockman 1993:11).
absence of a reversal mechanism, government could lose its legitimacy and finally step down as in the case of Suharto in 1998. Due to this reason, public consultation or compromise is required besides other strategies such as the phasing out or compensation (Nelson 1989:13-14; Pereira et al. 1993:9).

The points of criticism presented above are of relevance for post-Suharto Indonesia. This is because, first, the first wave of institutional reform since 1999 has brought about a multiparty system with power becoming highly dispersed among many new political actors. This was triggered by the call for the importance of checks and balances among government institutions as well as freedom and participation for the people. Since then, as in other countries in the Asia and Pacific where institutional reform has put more emphasis on efficiency than representation (Reilly 2006:176), the second wave of institutional reform has tried to reduce the number of parties. Quite paradoxically, while being successful in reducing the number of parties significantly, this attempt has resulted in more fragmentation of power in parliament epitomized by an increase in the effective number of parties. Power is now dispersed more widely among these new actors. From the standard argument of power concentration, post-Suharto Indonesia should have been consistently marked by policy paralysis. However, as will be discussed in detail in the coming chapters, many significant economic policies were adopted amidst strong opposition, though marked by a stark variation among administrations. Therefore, while concerns about policy immobilism are important (Ruland et al. 2005:236; Ellis 2006; Liddle and Mujani 2006), one must not ignore the variation. Therefore, applying this optic to understand post-Suharto Indonesia will bring more questions than answer.

Second, policy legitimacy is no less important than policy speed. Boediono (2005:318), for example, argues that while power concentration or elite insulation is important for effective policy-making, the present political setting makes it 'neither possible nor, strong proponents of pluralism would say, desirable'. Similarly, drawing on the experience of some local governments which introduce policy reform, Erawan (2006:67) concludes that elite insulation alone is not sufficient for reform initiatives to succeed. Under the existing democratic system, it must be accompanied by building political coalition to achieve legislative majority and creating a broader network of social support. This is also true at the national level where the government (president and/or the DPR) has often in many policy
areas consulted organized groups in the policy-making process. This gives the government a minimum guarantee of policy legitimacy that ensures that reform initiatives can be broadly accepted and more sustainable.

Taking this last criticism into account, a daunting tension becomes evident between policy speed on one side and policy legitimacy on the other. While the first requires a certain degree of power concentration to insulate decision makers from their environment, the second demands limitation and control over government by dispersing power to involve several key players (Desai and Olofsgrad 2006:97). Government is required to act in a timely and decisive way to push change but it must be controlled and held accountable from acting as an arbitrary agent (Haggard and Kaufman 1989:73). For countries facing economic crisis and democratic transition at the same time, this tension is so frustrating, sometimes resulting in policy inaction and delay. Under such conditions, accomplishing economic recovery which requires concerted and bold measures from a relatively insulated institution must confront the reality that, in the early stage of democracy, politics sometimes takes precedence over the economy (Maravall 1993:84). Boediono (2007) clearly expresses this concern in relation to the post-Suharto era. While the real practices of politics have frequently compromised effective policy-making, it can no longer be ignored as it was under Suharto.

Considering all these criticisms, this thesis seeks to find a supplementary, if not alternative, explanation for the power concentration or insulation argument. This is not to neglect the merits of the power concentration or insulation approach. Rather it will extend the argument and develop an alternative way of looking at what happened in post-Suharto Indonesia. One possible explanation in the area of market-oriented policy reform is elite cohesion (Nelson 1984). This refers to the degree to which policy makers 'share and act upon a common set of policy and political interest' (Weaver and Rockman 1993:24). It follows that power concentration in one insulated body does not necessarily lead the elites at the center of the policy-making arena to take a cohesive policy stand to cope with certain

17 Similarly, Cox and McCubbins (2001) and MacIntyre (2003) raise a concern regarding the tension between policy decisiveness and policy credibility. The tension requires the balance between government capacity to respond quickly to any issue and its capacity to maintain policy in such a way as to create certainty and set credible grounds for any related actors to base their decision. While the first requires high degree of power concentration with fewer effective veto players, the latter calls for dispersal of power among numbers of veto players.
problems. In this respect, multiparty government in either parliamentary or presidential systems poses difficulties for enhancing elite cohesion due to certain ideological differences or simply different policy preferences. At its best, this type of government performs better in maintaining the policy status quo than changing the current one, especially in areas with social and political significance (Roubini and Sachs 1989). In contrast, two-party systems such as USA, Britain, or Australia\(^\text{18}\) are more capable than multiparty coalition governments of maintaining elite cohesion due to higher policy congruence and ideological resemblance and a narrow policy spectrum. Therefore, such a government has more opportunities to push difficult policy reform.\(^\text{19}\)

However, this line of explanation shares a similar flaw with the power concentration argument and it is inadequate for capturing the performance of the post-Suharto administrations in delivering difficult policy reform. If elite cohesion is a sufficient condition for adopting difficult policy reform, one should be able to find that only party government can achieve it. On the other hand, multiparty government will mark the prevalence of policy immobilism. Empirically, this can be nullified by the fact that multiparty governments can also adopt difficult policy reform while party government tends to maintain the policy status quo. This is because systems with high elite cohesion embody the risk of being punished directly by the people once they adopt controversial agenda due to a clear point of accountability (Weaver and Rockman 1993).

Looking at post-Suharto Indonesia, a similar problem can be identified. In the Suharto era, elite cohesion enabled the government to pursue many reform initiatives in a relatively technocratic and determined manner. Acting as an arbitrary leader, Suharto maintained full control over his economic team consisting of acknowledged technocrats with a shared policy outlook on how to manage the economy. This very team helped Suharto cope with

\(^{18}\) The two-party system, or some might call it party government, refers especially to a government where only two main parties compete for an election, win and lose the election in a certain time, and hold the government almost interchangeably. There are some other small parties in such a system but their existence has marginal leverage (see also Weaver and Rockman 1993:20). Clear examples of party government are the Democrat Party and the Republic Party in USA, the Conservative Party and the Labour Party in UK, and the Labor Party and the Liberal Party in Australia.

\(^{19}\) Besides party system, electoral laws also play a significant role in affecting elite cohesion. A proportional representation with closed list system offers an opportunity to enhance elite cohesion while a single member district system and a proportional representation with an open list system tend to provoke an elite split, as MPs are more responsible to their constituents than to their party leaders (see for example Ames 2001).
the many reforms required until he stepped down in mid 1998. The advent of institutional reform in 1999 has made such cohesion no longer viable (Bird et al. 2007:11). All the post-Suharto presidents (with the exception of Habibie) have been forced to cope with the coming of a multiparty system. To achieve legislative majority, they must build a coalition involving several (if not all) major parties. One immediate cost for such an arrangement is the requirement to share cabinet portfolios with coalition allies. Even in areas as important as the economic portfolio, the president must accommodate parties' interest by putting their members in it. The Wahid cabinet is the worst example of this (Haggard 2000:124; Martinez-Diaz 2006:406). With ministers being drawn from different political backgrounds, elite cohesion is merely a distant memory. The need for more policy consultation among these actors has also delayed decisive responses to many urgent problems. Yet, numbers of reform initiatives could be and were adopted during this period despite the high variation among administrations in terms of the degree of achievements. Therefore, there must be an alternative explanation to the cohesion-based argument to understand the post-Suharto politics of policy reform.

Another alternative explanation for understanding the achievements in adopting difficult policy reform comes from the veto player literature. This is a relatively new approach in institutional literature. The central argument is that 'policy stability increases with the number of veto players, decreases with their congruence, and increases with the cohesion of them' (Tsebelis 1995:313). Similarly, Cox and McCubbins (2001:27) conclude that 'as

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20 For a more extensive discussion on the effect of veto players on policy outcome, see Tsebelis (1995); Tsebelis (1999); Cox and McCubbins (2001); Tsebelis (2002); MacIntyre (2003). See also Hallerberg and Basinger (1998); Crepaz (1998); Birchfield and Crepaz (1998); Bawn (1999); Crepaz (2001); Obinger (2002); Zohlnhofer (2003); Kastner and Rector (2003); Benz (2004); Franchino (2004); Andrews and Moninola (2004); Beyers and Trondal (2004); Natali and Rhodes (2004); Santoni and Zucchini (2004); Minnich (2005).

21 Elgie (2005) categorizes the study of political institutions into three main waves. The first one focuses on the difference between presidentialism and parliamentarism which refers mainly to Linz's thesis on the perils of presidentialism and the virtues of parliamentarism. The second wave extends this dichotomy by incorporating other institutional properties, especially the party system and the executive's power. Mainwaring's difficult combination thesis can be seen as pioneering work for this group. Veto player approach comes as the third wave with a more direct explanation. It holds regime type as constant by focusing on the veto power holder as one common institutional property. George Tsebelis is the most prominent scholar in this group.

22 From these three properties, it is the number of veto players which is commonly used to assess the effect of any institutional arrangement on potential for policy change given that the last two properties are difficult to operationalize. It consists of institutional veto players as stipulated in the constitution and partisan veto player. The later refers to those involved in the real political game and generated inside institutional veto players (Tsebelis 2002:79). This includes coalition and its members, the courts, interest groups, pressure
the effective number of vetoes increases, the policy becomes more resolute and less
decisive; the reverse is also true'. It follows, for example, that in a political system with
only one effective veto player, policy direction will depend very much on the choice of this
actor. However, merely increasing the number of veto players does not necessarily change
such direction. Policy congruence between veto players also matters. If these actors share
the same policy preference, policy change will be easier. Such a condition also applies to a
situation where the newcomers can be co-opted by incumbents. Indonesia under Suharto is
a good example of this situation (MacIntyre 2003). However, it is extremely difficult to
apply this approach to the post-Suharto context.

Indonesia's constitution only stipulates two constitutional veto players, namely, the
president and the DPR. However, the politics of decision making presents totally different
story. The coming of multiparty system since 1999 has brought many partisan veto players
into policy-making arena, the most important of which is fraction. It is this political
configuration that really matters in the practices of policy making. In such circumstance,
the role of partisan veto players cannot be underestimated. The DPR’s Rules of Procedure
confirm the importance of these actors and both the president and the DPR must really
consider them to win any legislative agenda. The problem is that even if one focuses on this
group, it is not easy to count the number of veto players as they change across policy issues
and time. The salience of short-term interests and a lack of experience with coalition make
such arrangement even more volatile. Considering these difficulties, this thesis will not

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groups, mass media, international agencies, and so on, which varies from one country in one time to the
other.

23 In addition to that, since 2003 Indonesia has had a constitutional court with the authority to undertake judicial review. Regarding policy reform, it has only a retrospective veto power after a bill is declared (see Law 24/2003).

24 The word “fraction” is the translation from “fraksi” and this might be confusing for political scientist outside Indonesia. Its closest synonym in political science literature is caucus with more formal and institutionalized manner (see Sherlock 2007:11, footnote no.8). After the collapse of New Order, there was initially no stipulation as to how many fractions shall be established in line with the spirit of democracy and reform. Only after 2003, the revised DPR’s Rules of Procedure maintains that political parties must have at least 10 seats to be able to form one fraction while those with less than 10 seats are required to merge either with other parties to meet the requirement or merge with other fraction. In 2004, this rule was again revised by increasing the number of seats from 10 to 13 seats for any party or parties to form a fraction. Beyond any other reason, this is to reduce political configuration in the parliament.

25 Taking this into account, Tsebelis' argument must be applied with caution to Indonesia. He argues that 'according to the constitution, the agreement of institutional veto players is a necessary and sufficient condition for policy reform, while the agreement of partisan veto players is, strictly speaking, neither necessary nor sufficient' (Tsebelis 1995:302). Tsebelis seems to ignore the informal aspect of policy-making process, something which is broadly practiced especially in developing countries such as Indonesia.
employ this approach.

The discussion so far has not provided a satisfactory theoretical answer that explains the variation in policy reform achievement in the post-Suharto era. When power concentration or elite insulation are absent if not undesirable and elite cohesion is a distant memory, what can explain the variation among the post-Suharto administrations in adopting policy reform?

Considering the complex nature of institutional reform in the post-Suharto era, my response to such questions is to look at the degree of executive strength, a term applied to represent a combination of the president’s constitutional powers and partisan support. When power is highly dispersed due to the nature of the party system and the constitutional separation of power, policy-makers’ autonomy and cohesion are compromised. Under such circumstances, the achievement in economic policy reform especially in areas with political significance will depend mostly on the degree of executive strength. As a matter of fact, it is the executive which bears the major responsibility for the success or failure of any initiative in adopting difficult policy reform. This is not to say that parliament’s strength and party influence do not matter. Indeed, executive strength is important because parliament and party play important roles in either opposing or supporting the executive’s policy initiatives. In adopting market-oriented policy reform, many of the initiatives endorsed by the IMF must secure parliament’s approval to be enacted. This reactive power of the parliament requires the president to craft his or her proposal extremely carefully and build legislative support to achieve it. Therefore, executive strength is best understood as the relative degree of the strength of parliament and the political parties. The following section will discuss this approach in detail.

26 Presidential scholars dub this approach ‘presidential power’ or ‘presidential strength’. This thesis uses instead the term ‘executive strength’ to cover the president and also his or her team in the cabinet.

27 The new DPR resulting from the 1999 and 2004 elections has been subject to criticism due to its limited role in the legislative arena despite the power it has. Most important bills were proposed by the executive. The area where the DPR really dominated policy-making process is especially related to the establishment of new local governments (Fitrani et al. 2005; Rüland et al. 2005:230-1; Ziegenhaim 2008).
2.4 Executive strength and economic policy reform

Institutional reform in Indonesia since 1999 has brought about many significant effects, one of which is the degree of executive strength. In this respect, the first wave of institutional reform up until 2000 made the president less capable in dealing with the parliament. After that, at least since 2001, the second wave of institutional reform has again strengthened the position of the president to create more balanced relationships with the parliament. This stems especially from the introduction of direct presidential election and the tightening of presidential impeachment which consequently gives the president some protection over security of tenure. This brings a fundamental change to Indonesia’s key institutional underpinnings but ‘almost nobody noticed it happen’ (NDI 2002:1). It had an immediate effect on the degree of executive strength and, combined with partisan support, this has enabled the president to govern more effectively. However, despite its significance, no systematic research has yet been undertaken to assess its effect. My argument is that it is the change in the degree of executive strength which significantly explains the variation of achievement in economic policy reform in the post-Suharto era. Only a strong president can adopt economic policy reform. The contrary is true for a weak president, with policy inaction or even policy reversal as the main feature of policy-making process (see also Haggard and Kaufman 1995:163).

To better understand the effect of executive strength on economic policy reform, it is important to look first at the sources of executive strength. In this respect, the most important factor is the executive’s security of tenure and this is one key characteristic of presidentialism. This is to argue that constitutionally protected security of tenure is the minimum condition for a president to be able to adopt difficult policy reform. Maravall (1993:116) argues that only the survival of the office can modify the executive’s commitment to adopting policy reform. Haggard and Kaufman (1995:158) emphasize further that the protection of security of tenure is a minimal requirement for a successful policy reform. This provides a president with a sense of autonomy, for example, to assign his or her own economic team, ensure control over it, back it up and change it whenever necessary, and enhance its cohesiveness. Above all, it gives a president a degree of freedom from political opposition. The job is even easier when policy reform has been decided by
the previous government and is irreversible. In contrast, a president without constitutional protection over security of tenure will not risk his or her office by taking politically sensitive initiatives. By this standard, presidentialism is argued to have the advantage of being able to adopt difficult policy reform as the president has security of tenure or fixed terms of office which are not dependent upon the parliament (Linz 1994; Mainwaring and Shugart 1997; Lijphart 1999). However, for a presidential system with a loose condition of impeachment and/or if impeachment can be politically engineered, the executive will be very vulnerable when adopting any politically sensitive agenda.

For post-Suharto Indonesia, such a requirement can be seen as the most important one without which the president will almost certainly avoid taking painful policy measures under his or her jurisdiction. It is this political capital which substantially creates the significant variation in economic policy reform among post-Suharto presidents. While claiming to have a presidential system, the empirical practices denote a parliamentary system or a semi-presidential system at its best (King 2001; NDI 2001:24; Wessel 2005:15; Ziegenhain 2005:28-29). This is because of the absence of security of tenure for the executive which is subject to parliamentary confidence. Wahid suffered such a constitutional flaw and had to leave office before his term expired. Only after Wahid is Indonesia’s president in a secure position. Megawati and SBY enjoyed this protection when the constitutional amendment introduced direct presidential election, made presidential impeachment constitutionally more difficult and legally-bound, and reduced the power of the MPR significantly. These changes have given the presidents a certain degree of freedom from political pressure when pursuing a difficult policy reform.

Though very important, the executive’s security of tenure alone is not sufficient to enable the president to adopt difficult policy reform. Thus this type of protection is best seen as a necessary condition given the president’s limited legislative powers and the nature of the policy-making process in Indonesia where joint approval is required for any legislative initiative to be enacted. Therefore, the president’s legislative powers as stipulated in the Indonesia’s constitution and partisan support in parliament must also be considered. Haggard and Kaufman (1995:8) call these powers executive authority and structure of the party system while Mainwaring and Shugart (1997) dub them constitutional and partisan
powers. Mariscal (2004) also raises similar concerns, pointing to the importance of the nature of representation and distribution of power among actors. These two combinations will affect the 'status' of the executive especially in the legislative arena, whether weak or strong, minority or majority, and therefore the executive's strength relative to other political actors when it decides to change the existing policy status-quo. These scholars seem to take the executive's security of tenure for granted due to the standard characteristic of presidentialism, that the president has a fixed term of office. As mentioned before, this was not the case for Indonesia until late 2001 when there was no constitutional protection over the executive's security of tenure. It follows that only a president with strong constitutional powers and partisan support as well as constitutional protection over security of tenure can adopt difficult policy reform.

I will now look briefly at the two sources of executive powers starting with the executive's constitutional powers. Scholars such as Shugart and Carey (1992), Frye (1997), Mainwaring and Shugart (1997), and Metcalf (2000) have offered significant contributions on how to measure them. This is not a difficult task given that the executive's constitutional powers are stipulated in the constitution. In a presidential system, such powers can be grouped into legislative and non-legislative powers (Shugart and Carey 1990:150).

28 The other contribution distinguishes the sources of executive strength as formal and informal. While the formal strength stems from the constitution, the informal aspect rests in the president's ability to use all availability resources surrounding him/her such as public appeal, persuasion, and professional bureaucracy (see for example Mayer and Price 2002).

29 So far, Shugart and Carey's categorization is the most commonly referred framework for calculating presidential power. They list 10 different types of presidential legislative and non-legislative powers. Included in presidential legislative power are package veto/override, partial veto/override, decree, exclusive introduction of legislation, budgetary powers, and proposal of referenda, while non-legislative powers consist of cabinet formation, cabinet dismissal, censure, and assembly dissolution (Shugart and Carey 1990:150). For a closer look, see Appendix A.

30 Frye lists at least 27 types of presidential power starting from dissolving the parliament, calling the referendum and election, appointing the constitutional court, supreme courts, central bank chief, judges, prosecutor general, security council, and senior officers, proposing legislation and constitutional amendment, issuing non-emergency decree, to assuming emergency power. For a closer look, see Frye (1997).

31 Shugart and Mainwaring (1997) focus their attention on presidential legislative powers which they categorize as veto (and override) power, partial (item) power, decree power and exclusive introduction of legislation.

32 Metcalf tries to revise the lists of presidential powers already proposed by Shugart and Carey and applies it to semi presidential system such as Austria, Finland and France and to six countries with purely presidential system in Central and East Europe, namely, Bulgaria, Croatia, Macedonia, Poland (1997), Romania and Slovenia. For a closer look on his revised version, see Metcalf (2000).
The legislative powers include veto, decree, bill introduction, budget making, and referendum while the non-legislative powers consist of cabinet formation and dissolution, parliament censure over cabinet formation, and parliament dissolution by a president (see also Baliaev 2006; Frye 1997; Metcalf 2000). Using Shugart and Carey’s measurement, a president can be very powerful when he or she has strong powers in both the legislative and the non-legislative areas. A president can also be very weak with limited legislative and non-legislative powers. In other circumstances, a president can have weak legislative but strong non-legislative powers or strong legislative but very weak non-legislative powers (Shugart and Carey 1992:156-8).

As far as legislative-making is concerned, these combinations can be simplified into two main categories. They are (1) a president with strong legislative power which covers veto, decree, special bill introduction, budget-making and referendum, and (2) a president with weak legislative powers. The latter covers the situation when veto is subject to override with less demanding conditions (simple majority or less), limited or no decree power at all, bill introduction subject to parliament amendment, and budget-making subject to unlimited amendment by the parliament.

Based on Shugart and Carey’s framework, it can be concluded that Indonesia’s amended constitution provides comparatively strong constitutional powers for the president with nine points of legislative powers and 12 points of non-legislative powers. The legislative powers come from package veto without override (scored a 4), partial veto without override (scored a 4) and limited authority to issue decrees which requires early subsequent ratification from the DPR (scored a 1). Indonesia’s constitution does not provide the president with the powers of exclusive introduction of legislation in certain areas (scored a 0) and proposal of referenda (scored a 0). As for budgetary power, the constitution gives the president the authority to propose the annual budget bill. However, the parliament has unrestricted power to amend the budget bill (scored a 0). Meanwhile, for non-legislative powers, the score

33 A more extensive discussion on the provision and use of decree, either constitutional decree power or delegated decree power, can be found in Carey and Shugart (1998). Research on this topic especially in Latin American countries has developed progressively.

34 The authors argue that this combination hardly exists reflecting the logic that the president should not have strong legislative powers if he or she even has only poor control over the establishment of the cabinet.

35 In this area, it was only after 2003 that the power of the parliament was limited. Law 17/2003 stipulates that the DPR may amend annual budget proposal to a degree not to exceed deficit of -3 per cent of GDP. Using
derives from cabinet formation without a need for parliament’s confirmation or investiture (scored a 4), dismissal of cabinet ministers at the president’s will (scored a 4), and the absence of parliament’s power to censure or remove the cabinet or ministers (scored a 4). On the other hand, the president has no power to dismiss the parliament (scored a 0).

For non-legislative powers, the real practices are quite different from what the constitution stipulates and this is related to the presence or absence of constitutional protection over the executive’s security of tenure. The score is only practically valid for presidents with such protection. In contrast, a president without such protection must consult with parties in parliament in establishing the cabinet and reshuffling or dismissing the ministers, the ignorance of which can be very costly for his or her survival. The absence of tenure protection makes a president’s non-legislative powers extremely weak.

An alternative way to look at the executive’s constitutional powers is offered by Shugart and Mainwaring (1997:41). Focusing on legislative authority, they categorize the executive’s powers into proactive and reactive powers. The former refers to the president’s power to establish a new status quo, that is, to push policy reform by issuing a decree, while the latter is the president’s power to maintain the policy status quo through the use of veto. The strength of these two powers is subject to a constitutional provision on the extent of parliamentary override or ratification and, if so, the requirement for parliamentary support to do that (extraordinary majority, absolute majority of the whole members, or simple majority of the quorum).36

Shugart and Carey’s scoring system, this increases the president’s power (scored a 2). This increase does not change the overall powers of Indonesia’s president in the legislative arena.

36 Using this standard, Shugart and Mainwaring (1997) present four different power configurations. The first represents the president who is potentially dominant when he or she has both proactive (decree) and reactive (veto) powers even sometimes with exclusive power over the introduction of certain bills such as budget. Included in this group are Chile, Argentina, Columbia (1968-1991) and Ecuador. The second one is a president with only proactive power without any reactive power. Veto power may exist but it is weak (for example given the easy requirement for parliamentary override). This includes Brazil, Columbia (since 1991), and Peru. The third group stands in contrast to the second in which a president only has reactive without proactive powers. Here the president may have a strong veto power and/or exclusive introduction of a certain bill, but he or she has no power to issue a decree. This includes Uruguay, Bolivia, Dominican Republic, El Salvador, and Panama. The last one is a potentially marginal president who especially has no veto power such as Mexico, Costa Rica, Honduras, Nicaragua, Paraguay and Venezuela (Shugart and Mainwaring 1997:49).
Using this approach, Indonesia’s president has only comparatively moderate legislative powers. Though the president has proactive power (decree), it is only for emergency conditions, especially for national emergencies, and is subject to parliamentary override. Article 22 of the Constitution stipulates that (1) should exigencies compel, the President shall have the right to establish government regulations in lieu of laws, (2) such government regulations must obtain the approval of the DPR during its next session, and (3) should there be no such approval, these government regulations shall be revoked. The requirement for parliamentary override is the simple majority principle, that is, 50-per cent-plus-1-vote of the MPs present on the floor voting. Meanwhile, the constitution does not provide any clear stipulation of the president’s veto power. The score presented before is simply based on my interpretation of the constitution. Article 20 of the constitution stipulates that each bill shall be discussed by the DPR and the President to reach a joint approval. If a bill fails to reach a joint approval, that bill shall not be reintroduced within the same DPR’s session. My interpretation of this stipulation is that both the president and the DPR have package as well as partial veto powers. The constitution then gives the power to the president to sign a jointly approved bill to become law. However, should the president fail to sign it within 30 days following such approval, that bill shall legally become law and must be promulgated. This implies the removal of the presidential pocket veto power (NDI 2000:8). To confirm the DPR’s domination in the legislative arena, the whole process must comply with the DPR’s Rules of Procedure. This thesis will refer to this categorization since it looks more deeply into the real practice of policy-making.

The fact that Indonesia’s constitution provides only moderate legislative powers for the president raises concern about the potential difficulty in adopting difficult policy reform. A president can only pursue such an initiative with the approval of the DPR and with the DPR being more assertive in the policy-making arena, the possibility of a president facing difficulty in adopting a contentious agenda is very real. To achieve a legislative agenda, therefore, a president must build a parliamentary majority support. Therefore, the other element of executive powers, namely, partisan power, must be examined as well. This comes from the interplay between the president and party in parliament. It refers to the

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37 The practice is much more complex than this. Indonesia’s administrative law requires all laws to be promulgated by the president through the State Gazette to be applicable. If the president reuses to promulgate the already approved bills beyond its 30-day deadline, such laws are practically toothless. Many administrative scholars are against this administrative convention.
‘abilities to shape (or, conceivably, dominate) the lawmaking process that stems from the
president’s standing vis-à-vis the party system’ (Shugart and Mainwaring 1997:13) or the
degree of the president’s reliance upon parliamentary majority support (Mainwaring
1997:56). A president can have minority or majority status in the parliament subject to
whether he or she can craft legislative support coming from his/her own party or a coalition
with other parties.

The importance of partisan power for a president wishing to push through difficult policy
agendas is undeniable given the nature of policy-making. Indonesia’s constitution only
stipulates that any bill requires a joint approval from the president and the DPR to become
law (Article 20). The details of such stipulation are found in the DPR’s Rules of Procedure
which emphasize the salience of consensus or musyawarah untuk mufakat (verbally means
‘deliberation to reach agreement’). Voting is perceived as the last resort and is rarely used.
This is part of Indonesian culture which was in the past manipulated by Suharto’s
authoritarian regime to avoid criticism. Sherlock (2003:31) maintains that its persistence
after the restoration of a democratic system is to ensure that all parties are happy with the
decision and that no minority parties feel excluded or vanquished.

In practice, the reliance on consensus in decision-making process has produced many
disappointing effects (Sherlock 2003:31-32). Firstly, it delays many urgent decisions.
Decision can only be made after a time and energy-consuming process resulting in
‘consensus by exhaustion’. Due to this reason, decision is sometimes made outside the
parliament making informal politics a very integral part of Indonesian politics.38 The other
effect is that each fraction has the same weight of effective veto regardless of the number of
seats it has. It is this partisan block that matters, not the individual parliamentarians. Any
decision must be approved by majority fractions and voting on individual basis is extremely
rare. This gives each fraction effective veto power which can be employed for certain
political ends. For this reason, the president must really consider partisan configuration in
parliament. Therefore, establishing a legislative majority is absolutely important for any

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38 This is hardly surprising. Pike (2000:281) observes that informal politics – ‘interpersonal activities
stemming from the a tacitly accepted, but unenunciated, matrix of political attitudes existing outside the
framework of legal government, constitutions, bureaucratic constructs and similar institutions’ – has been at
the center of politics in Asian and other developing countries including Indonesia.
To understand the president’s partisan power, the nature of the party system must be considered, bringing the discussion to party fragmentation and polarization. Party fragmentation refers to the number of parties competing for votes in an election and getting parliamentary seats. The commonly-used method to measure it is the effective number of parties, as developed by Laakso and Taagepera (1979). Using this measurement, Haggard and Kaufman (1995:168), Mainwaring and Shugart (1997:398-399), and Lijphart (1999:67) conclude that a party system becomes more fragmented as its effective number of parties exceeds 3.5. While this conclusion seems arbitrary, it is in fact a helpful judgment. Based on this formula, post-Suharto Indonesia clearly has a multiparty system. The 1999 election brought 21 parties into the parliament while the 2004 election brought 16 parties to parliament. While the number of parties winning parliamentary seats decreased, the effective number of parties had increased from 4.6 in the 1999 election to 7.1 in the 2004 election. This implies increased party fragmentation on the one hand (Sherlock 2004:6) but also a more consolidated party system on the other hand.

Meanwhile, polarization refers to the ‘ideological distance among parties’ (Haggard and Kaufman 1995:167). In Europe and other established democracies, this especially refers to the left-right continuum besides the presence of anti-system or radical parties. In reality, even with such distinctions, scholars find it difficult to put any party into a particular category. This stems from the fact that ideological preference is sometimes volatile, moving from one issue to another. In developing countries, such categorization is even more problematic given the lack of a strong ideological tradition (Haggard 2000:44). For countries with a strong religious affinity, polarization is best understood along the secular-religious continuum. In contemporary Indonesia, while it is common to distinguish parties into secularist and Islamist, or along a nationalist-Islamic dichotomy (Thompson 1999; Evans 2003; Pahlevi 2003), it is in fact misleading. Parties are predominantly pragmatic in their struggle and their ideology is called upon only in certain circumstances when it is

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39 Lijphart (1999:67) argues hypothetically that a country has a two-party system if its effective number of parties is 2.0, two-and-half party system if it is 2.6, multiparty system with one dominant party if it is 3.5 and multiparty system without a dominant party if it is 4.5 or more. This thesis uses 3.5 as an arbitrary score for a multiparty system regardless of the presence or absence of a dominant party.
politically beneficial (Denny 1999). Beyond that, as reflected in their programs, parties have no clear ideological preference but power and interest (Djadijono 2006; Priyadi 2006). At best, parties are of a catch-all type as reflected in the use of populist jargon like “for the people’s welfare” or “for the national interest”. Considering this, this thesis will focus more on party fragmentation when assessing a president’s partisan power.

The comparative literature indicates that party fragmentation and polarization have a significant effect on government capacity to adopt difficult policy reform. As presidentialism is frequently prone to the rise of minority governments (Shugart and Mainwaring 1997:31; Cheibub 2002:285), party fragmentation and polarization will pose many difficulties for a president in achieving his or her policy agenda (Mainwaring and Shugart 1997:396). It will complicate the need for policy coordination which stems from ideological differences or simply from pork-barreling (Haggard and Kaufman 1995:171). Moreover, a fragmented and polarized party system can result in public policy being packaged in a more ‘private-regarded’ than ‘public-regarded’ manner to please different stakeholders (see also Cox and McCubbins 2001:28). This stands in contrast to the requirement for adopting difficult policy reform, especially those with a redistributive nature. Moreover, when national interest is at stake, this institutional configuration tends to be a liability.

Party fragmentation and polarization also render the executive-legislative relationships not only conflict-laden but also unpredictable. A president trying to pursue a national agenda must confront a parliamentary contingent with a more partisan orientation, raising the possibility of conflict. When the national agenda potentially endangers partisan interests and no compromise can be reached, executive-legislative conflicts take place since each branch claims to have the legitimacy to represent the people. Moreover, a president will find it unreliable to work with a parliament of this nature. Despite this flaw, ignoring the parliament in policy-making process will only trigger further conflicts. A president can only choose either ‘governing through the assembly’ or ‘governing around the assembly’ (Cox and Morgenstern 2001:177) and every choice has its own risk. Ideological polarization makes it even harder for a president to rely on his or her partners in the parliament for a legislative support. No permanent support can be secured since it is subject to the nature of policy initiative.
These negative sides of party fragmentation and polarization are an important message for post-Suharto presidents. With the increase of party fragmentation, they will find it difficult to move forward with any policy reform agendas unless the majority of partisan blocks approves it. Very often, the president must give up his or her initiative due to parliament's opposition. The most fundamental challenge for a president wishing to adopt policy change, especially in politically difficult areas, is then how to form a legislative majority. The only means to such end is by establishing a coalition.  

However, even this commonly prescribed recipe for minority presidents under multiparty systems is not without problems. While its existence in the presidential system is common (Amorim-Neto 2002:48; Cheibub et al. 2004:574; see also Lijphart 1992; Linz 1994; Jones 1995), coalition is argued to work better under parliamentary system (Mainwaring 1993:200; Mainwaring and Shugart 1997:396-397). Unlike coalition in a parliamentary system, coalition in a presidential system does not necessarily lead to a legislative coalition. Parties can have their members in the cabinet but their legislators do not automatically commit to support the president. Worse than that, incentives for parties to break the coalition agreement are generally greater in a presidential than in a parliamentary system especially in difficult times. This is because the performance of the president does not necessarily reflect the performance of the parties joining the coalition. Based on an electoral calculation, the members of a coalition often feel a need to distance themselves from the government, especially when the president faces a bad time and an election approaches. This is to escape the blame of being part of the problem should the president perform poorly. Even if government performance is good in the eyes of voters, it is the president and his or her party who enjoy the benefit, not the parties joining the coalition. Efforts to consolidate coalition support by transplanting proportionality rule as under the parliamentary system are no less problematic (Amorim-Neto 2002:49).

The last problem with a coalition under a presidential system is the fact that coalition sometimes precedes an election and wanes sooner after that. This is because coalition is used as a short-term strategy to acquire parliamentary seats or to support certain presidential candidates. Once achieved, each party will return to their original stand. Therefore, even if coalition parties can bind themselves to the president, they do not bind

40 The other choice is of course patronage but this is politically undesirable and risky under a democratic system. At best, it is combined with other democratic instruments such as a coalition.
themselves to each other. Other parties are after all still their competitors. This will further affect the ability of the presidents not only to secure legislative majority but also to ensure policy coherence, the cost of which is sometimes unbearable.41

These concerns are quite a general reflection of how difficult it is to build a majority legislative coalition under presidentialism and post-Suharto Indonesia is no exception to this rule. Many informed scholars and the people have expressed their criticisms of the way post-Suharto presidents have dealt with parties in crafting their coalition cabinet. For them, coalition is even more a problem than a solution to Indonesian politics. This stems from the nature of coalition in post-Suharto politics, two are primarily important.

The first prominent feature of coalition in post-Suharto Indonesia is the dominance of distributive motive of the parties involved. While Laver and Shepsle (1996:282) maintain that coalition implies both collection and distribution of power among coalition partners, the practices of coalition in post-Suharto Indonesia mark the prominence of distribution over collection of power. Indonesia might not be the only case but such a motive is incomparably prominent in any standard. Slater (2004:62) even concludes that ‘political parties share power far more than they fight for it’ (italics in original). Wessel (2005:118) also expresses the same concern that ‘coalitions are formed in order to gain power or to prevent other groups or individuals from doing so’. This is mainly due to the material luxury embedded in the executive bodies. Being a member of coalition means obtaining access to state resources so that having their representatives in the cabinet is the ultimate motive for parties to join coalition. Coalition is surely no more than the elite’s strategy to capture state resources by controlling state institutions. Other motives for forming coalition such as winning a policy agenda are simply secondary, if not irrelevant.

The second prominent feature is a coalition’s temporariness. Coalition is issue-based and therefore changes from one issue to another. Its sustainability and reliability in the legislative arena are of big question. Therefore, a president’s party must work hard in every policy initiative, especially those with political significance, to get sufficient support from

41 A clear example is what happened in Brazil under President Sarney. He had to sacrifice financial adjustment and stabilization measures to buy political support to secure his five-year mandate (Mainwaring 1997:93).
other partisan blocks. There are hardly any permanent coalitions. PAN even avoids building permanent coalition with any other parties. The reason for this is to avoid making permanent enemies in politics (Detikcom, 26 November 2005). PKS also takes the same stance. So do other parties though they do not proclaim it publicly. This implies that after obtaining the cabinet portfolio, each party's contingent in the DPR will pursue its own interests that very often run counter to the president's agendas. At best, coalition partners will simply not challenge the president's agendas. Once the cabinet is established, the president will find himself or herself alone in pursuing a national agenda. This poses difficulties for the president in maintaining control over his or her administration and policy coherence. At worst, the president will be dictated to by partisan blocks in the parliament during decision-making processes which will create 'double jeopardy'.

This sometimes leads the president to decide to govern alone, excluding his or her coalition partner from the cabinet as in the case of the Wahid administration. Wahid recognized the danger of excluding other parties from the cabinet but, at the same time, he seemed to have realized that coalition was not working as expected (Gorjao 2003:33).

By raising these concerns, this thesis does not mean to say that coalition is unworkable and ineffective for a minority president. It is indeed important for a minority president to enhance legislative support. The only and ultimate concern is its reliability despite the power the president must share. In Indonesia, with parties employing negative opposition, excluding parties from the cabinet is much more dangerous than involving them, especially for an effective government and political stability. The danger is very real especially when executive's survival is dependent on parliamentary support. For this reason, the executive's security of tenure is an important precondition for building a consolidated and reliable coalition.

42 The term 'double jeopardy' is used to describe the fact that, on one hand, (1) the president must share cabinet portfolios with political parties which compromises his decisiveness, but on the other hand, (2) he or she still needs to mobilize – or buy – parliamentary support to win a legislative agenda. This logically makes coalition building meaningless for the president. For a counter-argument in the broader literature see, for example, Figueiredo and Limongi (2000).

43 Negative opposition refers to the practices when parties not joining a coalition employ every means, including dirty politics, to ruin the reputation, performance and legitimacy of the president and ruling party and, if possible, to bring him or her down even before the next election, rather than trying to ensure that the president and the ruling party perform their tasks in a responsible and democratic manner. Once these parties get power, they will undertake what they have opposed previously. It is for this reason that Indonesian scholars urge for 'loyal opposition'. This refers to opposition parties which base their political action on a rational and fair approach. They support the ruling party when its policy is for the majority of the people and oppose it if it is against public interest (Sugiarto 2004).
The difficulties faced by a president from party fragmentation and polarization are complicated if party discipline becomes another concern. This refers to the degree to which ‘legislators of the same party [are] voting together almost all the time especially on issues that cleave the legislature as a whole’ (Mainwaring and Shugart 1997:418). Coalition, even with parties having a similar ideological inclination, is less reliable when party discipline is weak. Strong party discipline leads to coalition being more stable and reliable under parliamentarism than presidentialism. For this reason, a president will have to continuously consolidate parliamentary support for every initiative he or she wishes to take by approaching individual MPs on an ad hoc base. The process is much simpler if party discipline is strong so that a president only needs to negotiate with party leaders on a more sustainable and predictable manner (Mainwaring and Shugart 1997:418-419).

Indonesia’s institutional arrangements in respect of the party system produce strong party discipline. All three institutional mechanisms to enhance party discipline as proposed by Mainwaring and Shugart (1997:421) are applied, namely, (1) control of candidate selection, (2) control of order according to which the members of party will be selected to be legislators, and (3) the pooling of votes among party’s candidates. These three mechanisms give the party leaders strong control over their members in parliament and therefore create a sense of dependency among parliamentarians toward their party. Those violating the party’s policy guideline will risk exclusion from the party. In addition to that, Indonesia’s party law includes a recalling mechanism, through which legislators violating party guideline can be dismissed from the parliament at any time during their term. This arrangement was first introduced by Suharto’s authoritarian regime. It was removed in 1999 but then restored since 2003, triggering widespread criticisms (Crouch 2003:18). Political parties now have even stronger control over their members. While such an arrangement is criticized for compromising the independence of parliamentarians in performing their functions, it is extremely useful for effective policy-making since the party will vote as a block. The president will also only need to deal with party leaders when trying to build legislative support.

Considering all these party system attributes, the president’s partisan power can be categorized as either strong or weak. A president’s partisan power is weak when he or she controls only a minority of seats in parliament. This may be because he or she comes from
a minority party in parliament and from failure to build a majority legislative coalition. In countries with a bicameral system, a minority status occurs when the president fails to control a majority of seats in at least one of the chambers (Cheibub 2002:287). In contrast, a president’s partisan power is strong if he or she has majority support in parliament, either because he or she comes from a party with legislative majority status in the parliament or the ability to establish a majority coalition. Such status is also applicable to a bicameral system in which the president controls a majority of seats in both chambers. Again, this definition is only valid when the degree of party discipline is high. Counting on the numbers of parliamentary seats while ignoring the degree of party discipline among party members is indeed a fatal mistake. A president might control a majority of seats in parliament but still fail to get his or her agenda approved because of the lack of party discipline.

Now, having discussed the two sources of executive strength, the following paragraphs will present the combination of two sources of executive strength and linking it to economic policy reform. Based on constitutional and partisan powers as previously discussed, several institutional configurations can be developed, each with consequential effect on effective policy-making. The best configuration supportive of the adoption of difficult economic policy reform is when a president has both strong constitutional power and strong partisan power. The other possible configuration is when a president has strong constitutional power but weak partisan power. A president can still adopt difficult policy reform but due to the lack of majority support, the reform will face political opposition from the parliament which sometimes has an interest in seeing the president fail or simply discredited (Linz 1994:35). Such a combination tends to result in an imperial president especially when the president has strong proactive power with strong override requirement (Cox and Morgenstern 2001). Mainwaring (1997:107) argues similarly that the combination of strong constitutional power and weak partisan power will lead the president to ‘oscillate between omnipotence and impotence’. Subject to constitutional provision, the executive in this type can use constitutional decree power to adopt policy reform resulting in a unilateral

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44 This configuration shares some similarities with the power concentration argument. Adopting difficult policy reform is simply a matter of willingness by the president. The only risk from this combination is the rise of hyper-presidentialism as found in certain Latin American countries (Weldon 1997:227). Such configuration is also inimical to the working of checks and balances, sometimes resulting in policy initiatives with questionable legitimacy.
decision-making process (Amorim-Neto 2002:59-60), government by decree (Carey and Shugart 1998; Negretto 2004) or 'president as the chief legislator' (Schroedel 1994:156) with different degrees of success. The other possibility is the rise of an exceedingly powerful executive lacking horizontal accountability toward other state institutions, especially parliament (Anderson 2006:141; see also O'Donnell 1994). This is especially true when the president has constitutional security of tenure and is independent from the parliament.

By raising this point, this thesis is not arguing that strong executive constitutional power is a liability for a president. Nor that strong constitutional power promises everything. It argues that when partisan support in the legislative arena is weak or when the parliament becomes a blocking force to reform measures as is the case in contemporary Indonesia, the president can still rely on his or her constitutional power to push policy reform. This explains why even a minority president – or minority government – can push significant policy reform despite the absence of majority support. However, a minority president and strong constitutional power are not a good combination for a stable government. While the use of decree power is sometimes constitutionally limited and subject to parliament override (with different consequences varying from pushing the agenda back into its initial position to the requirement for the executive to simply revise certain parts), its introduction tends to provoke legislative-executive conflicts. Its exercise is even vulnerable in the early stage of democratic transition considering the memory of notorious presidential authoritarianism. In the long run, unilateral policy-making cannot provide an effective mechanism for policy coordination as well as the management of distributive conflicts commonly found in difficult policy measures (Haggard and Kaufman 1995:165). Only under exceptional conditions when decisive action needs to be taken and delay is costly can this combination be politically justified.

The other combination is when a president has a weak constitutional power and strong partisan support. In this situation, the president can still adopt policy reform given a favorable constellation of partisan power (Siavelis 1997:356). However, this sometimes comes at the cost of the constitutionality of any policy initiative. Finally, controversial policy reform is extremely difficult to adopt if a president is weak in both constitutional and partisan powers.
Looking at these combinations, some scholars argue that partisan power is more important than constitutional power in pushing controversial policy agenda. Many executive’s initiatives fail mostly due to the lack of partisan support. In many if not all legislative initiatives, the executive will rely more on partisan support than its constitutional power. However, this ‘situational constitutionalism’ (Pious 2002:740) must be taken provisionally. This might be true only for inconsequential initiatives with low political significance where national interest is not at stake. Otherwise, as far as the executive has strong constitutional power, it can push policy reform with national significance regardless of partisan support. In addition, the ultimate emphasis on partisan support can put democracy at risk and result in policy initiatives with questionable constitutionality. The tyranny of the majority must be avoided and this is important to boost policy and government legitimacy. Moreover, policy initiatives with questionable constitutionality cannot be sustained in the long run and are subject to reversal. This will further compromise government credibility and legitimacy. For a young democracy like Indonesia, such a requirement is even mandatory for the survival, and thereafter consolidation, of democracy.

Classifying post-Suharto Indonesia into one of these combinations needs further qualification. The problem lies in the degree of constitutional legislative power which is only comparatively moderate. Given moderate legislative power and considering the nature of the policy making process as discussed earlier in this section, a president willing to adopt difficult economic policy reform must have both constitutional protection over security of tenure and strong partisan support. This thesis will argue and present evidence that executive’s security of tenure is a precondition for establishing consolidated partisan support. This topic will be discussed in the next section of this chapter.

To conclude this section, the core argument of this thesis is that in adopting politically difficult policy reform where power is so dispersed among many players, it is the degree of executive strength that matters. The executive strength is highest when it secures both constitutional powers and majority partisan support in addition to constitutional protection over executive’s security of tenure. However, even when partisan power is weak or absent, if the executive is constitutionally strong and there is constitutional protection for security of tenure, the opportunity for adopting policy reform in politically contentious areas is still open.
2.5 Research design

Drawing on the discussion from previous sections, this final section will establish the research framework by bringing the previously discussed materials altogether. The core argument is that executive strength affects the adoption of economic policy reform. It has been defined that executive strength comes from the combination of constitutional powers and partisan support. This configuration has significant consequences for post-Suharto Indonesia.

In terms of constitutional powers, all post-Suharto presidents have had the same degree of legislative and non-legislative powers. What distinguishes them is the degree of constitutional protection over the executive’s security of tenure. Wahid had no such protection since the MPR still had the constitutional power to remove the president from office even on policy ground. He was finally dismissed from office through a dramatic and politically-engineered impeachment. In contrast, Megawati had constitutionally protected security of tenure. This came from the tightening of the impeachment procedure through the constitutional amendment following her election which significantly reduced the power of the MPR over the president. Meanwhile, SBY enjoys the advantage of being the first president directly elected by the people and benefits from constitutionally tightened impeachment. On analyzing this variation, three different degrees of security of tenure emerge: it is extremely low for Wahid, moderate for Megawati, and high for SBY.

As will be argued in the coming chapters, this has variation proved consequential for the adoption of economic policy reform. The presence of constitutional protection over the executive’s security of tenure is a minimal political capital that will enable the president to adopt politically difficult economic reform, especially in the absence of reliable partisan support. This protection also enables the president to deal with the parliament in a balanced manner rather than being dictated to by it, especially in the legislative arena. Since Wahid had no such protection, he found it difficult to have any of his economic reform agenda adopted. DPR opposition to any of his reform agenda simply meant restoring the status quo. Consequently, only limited economic policy reforms were adopted under the Wahid
administration. For the opposite reason, this thesis identifies some significant economic policy reforms under both the Megawati and SBY administrations.

Since constitutional protection over the executive’s security of tenure is only a necessary but not a sufficient political capital for the presidents wishing to adopt economic policy reform, we need to look at the other important factor, namely partisan support. Having security of tenure only creates a degree of independence from the opposition for the president. Since the DPR has veto power to block any of the executive’s agenda and the president has only limited decree power to enact policy agenda, all presidents must have a legislative majority to win their agenda.

To capture a president’s partisan support in the post-Suharto era, this chapter discussed several institutional underpinnings that come especially from the party system. They are party fragmentation, party polarization, party discipline, and coalition size. All post-Suharto presidents must confront a multiparty parliament with increased party fragmentation under the SBY administration. It has been argued as well that party polarization is inconsequential, if not irrelevant, since parties are predominantly pragmatic. Meanwhile, party discipline is consistently strong. What distinguishes post-Suharto presidents is their coalition size. Here, two different yet interrelated attributes are especially important. The first one is the percentage of seats from parties joining the coalition. In this respect, another stark variation among post-Suharto presidents is found. Wahid established a grand coalition with 95 per cent of DPR seats. With all major parties joining the coalition, there was almost no room for the opposition. This changed under Megawati. She established an oversized coalition with 83 per cent of DPR seats. There was a minor opposition mainly from two major parties—PKB and PK. This changed again under SBY. He established a more consolidated though still oversized coalition with 74 per cent of seats in the DPR. There was an element of opposition coming mainly from PDIP with a quite significant percentage of DPR seats (20 per cent).

The other related attribute is the number of fractions joining the coalition. This is very important since the decision-making process in the DPR is based more on fraction configuration than individual votes. Only in extremely limited cases is decision making based on voting. Even if voting is applied, party (and fraction) always votes as a block
given strong party discipline. Therefore, to win any legislative agenda, the president must secure a legislative majority comprising the majority of fractions. Here we find another variation among post-Suharto presidents.

Under the Wahid administration, there were overall 10 fractions in the DPR. From this number, eight fractions joined the grand coalition with overall 97.2 per cent of DPR seats while two tiny fractions – PDU and PDKB – with only 2.8 per cent of DPR seats staying outside it. Considering their tiny share of parliamentary seats, they did not proclaim themselves to be the opposition. Even if they did so, they could simply be ignored. This configuration changed under the Megawati administration. There were still 10 fractions in the DPR until July 2003 when PDKB dismissed itself and joined the PKB fraction. From this number, seven fractions joined the coalition with overall 87 per cent of DPR seats. PKB declared itself the opposition party with only 10.2 per cent of DPR seats. PDU and PDKB were still excluded from the coalition given their insignificant share of seats, resulting in the increase of the percentage of DPR seats for fractions outside coalition to 13 per cent.

These configurations are quite different from the SBY administration. There were still 10 fractions resulting from the 2004 election. From this number, seven fractions joined the coalition with 75.29 per cent of DPR seat. PDIP declared itself the opposition party, was joined by PBR and PDS, resulting in 24.7 per cent of DPR seats outside the coalition. Table 2.1 presents the configuration of the executive strength of post-Suharto presidents.

This chapter has discussed as well the importance of partisan support for achievements in difficult policy reform. However, in post-Suharto Indonesia, the reliability of partisan support for the president’s legislative agenda cannot be taken for granted simply because all presidents were supported by a more-than-adequate partisan contingent. Rather, the reliability of such support is subject to the presence of the executive’s security of tenure. This is a precondition for the establishment of a consolidated coalition with reliable support in the legislative arena. It follows that a president whose fate is dependent on parliamentary support cannot force the parliament to support his or her legislative agenda. This combination – the executive’s security of tenure and partisan support – produces a variation in the executive strength among post-Suharto presidents.
Table 2.1 Executive strength of the post-Suharto presidents

<table>
<thead>
<tr>
<th>Variables</th>
<th>Wahid</th>
<th>Megawati</th>
<th>SBY</th>
</tr>
</thead>
<tbody>
<tr>
<td>Security of tenure</td>
<td>Low (the MPR can impeach the president)</td>
<td>Medium (presidential impeachment is tightened)</td>
<td>High (presidential impeachment is tightened and the president is directly elected)</td>
</tr>
<tr>
<td>Coalition size</td>
<td>Grand coalition (95.6% of DPR seats)</td>
<td>Oversized coalition (83% of DPR seats)</td>
<td>Oversized coalition (74% of DPR seats)</td>
</tr>
<tr>
<td>Number of fractions</td>
<td>8 (97.2% of DPR seats)</td>
<td>7 (87% of DPR seats)</td>
<td>7 (75.3% of DPR seats)</td>
</tr>
</tbody>
</table>

Note: The percentage of DPR seats for fractions in coalition is larger than that of the coalition size because it also includes parties without a portfolio in the cabinet.

Source: Author’s calculation

For Wahid, despite the involvement of all major players in a grand coalition, his partisan support was highly unreliable since he was dependent on parliament’s support to remain in office. He certainly had neither security of tenure nor consolidated partisan support, making it extremely difficult for him to adopt any politically difficult economic policy reform. Only when the DPR approved could any reform measure be adopted. Predictably, policy status-quo, delay or even reversal became a prominent feature of the policy-making process during his administration.

This was not the case for Megawati. She had constitutional protection over security of tenure due to the tightening of the impeachment process. Since this change came only after her election, she was forced to establish an oversized coalition with major parties other than PKB and PK. As so, she had less consolidated partisan support. This institutional underpinning provided her with the minimal political capital to adopt politically difficult economic policy reform. She could maintain a degree of independence from parliamentary opposition and not be fully dictated to by the DPR as under Wahid. Consequently, her administration adopted some important economic reform agendas in certain areas with political significance. However, she sometimes also had to give up her reform agenda to the opposition from majority fractions in the DPR, resulting in policy reversal.
The best combination found so far belongs to SBY. He was elected directly by the people and has constitutional protection over security of tenure. This has enabled him to establish a more consolidated partisan support though it is still an oversized coalition. This institutional underpinning has provided him with sufficient political capital to pursue difficult measures. Consequently, his administration has been able to adopt more difficult economic policy reforms in a more determined manner, especially in areas where strong political opposition used to succeed to block their progress.

With this framework in hand, the thesis proceeds to the next step. In the next three chapters, it will discuss the achievements in economic policy reform under each administration in turn and link it to the theoretical framework just developed in this chapter.
3

Economic policy reform
under the Wahid administration, 1999-2001

3.1 Introduction

This chapter assesses the achievements in economic policy reform under the Wahid administration. My argument is that given Wahid's extremely low executive strength in both constitutional and partisan terms, only limited economic policy reform was adopted, if any, during his administration. His lack of security of tenure and, therefore, vulnerability to dismissal by the MPR, implies that he had to establish and maintain coalition with other parties to achieve a legislative majority. His confrontation with the parliament not only risked his already vulnerable position but also triggered the DPR to become involved more deeply in and dictate legislative process, making compromise, delay, or even reversal a prominent feature when timely policy response was desperately required. When the executive planned to adopt economic policy reform, the DPR opposition almost always meant maintaining policy status quo.

Other scholars of Indonesia might criticize this argument and instead point to other factors. Some focus on the prevalence of the predatory interests of oligarchic actors who survive the collapse of the New Order regime (see for example, Hadiz 2004; Robinson and Hadiz 2004; Munir 2001). With strong resource bases, these actors serve as an effective obstacle for any economic policy reform initiative. As reform in this area might directly affect their interests, they employ every means to block it. My response to this line of argument is that under the new democratic system, such arbitrary behaviors have been significantly limited. In contrast, these actors have played within the new institutional arrangements to secure their interests and parliament is one of the key institutions. This is because the new political arrangements provide the incentives that enable them to take advantage. By this standard,
interest alone is not sufficient to explain the problem of limited achievement in economic policy reform.

A second possible alternative explanation lies in the complexity of the political, social and economic problems before and during the Wahid administration. Cameron (1999:4), for example, predicts that given the political uncertainty and rivalry in late 1998 and early 1999, 'it is probably too much to hope that a strong and capable government with decisive economic policies will emerge'. Similarly, Barton (2001a: 33-9) argues that it is foolish to assess Wahid's performance without considering the broader social and political context including the nature of regime transition and unrealistic public expectations of his administration. Thus, Wahid's twenty-one-month administration was simply too short to bring Indonesia at least back to its pre-crisis condition, much less into the future. Such an argument is insufficient and clearly tautological since it confuses the cause and the effect. Indeed, it is not the severity of the problem but the political resources to deal with it that matter. Without constitutional protection over security of tenure and reliable partisan support, the executive could not do much. As Barton (2002b:xxv) himself later realized, Wahid simply had insufficient support in the parliament to enable him to accomplish his economic reform agenda. It was the lack of this political capital that worsened the economic condition by provoking executive-legislative relationships which then created a very uncertain political condition. At best, the gravity of the economic crisis only provides the background but not the explanation for the degree of economic policy reform achievement by any government including that of Wahid.

Another explanation hinted at the writings of other scholars points to Wahid's personal weakness including his health problem (Barton 2000; Kingsbury 2002:260-7; Sadli 2002:12; Gorjao 2003:14; Kassim 2005:148). His eccentric style of leadership provoked conflicts with the parliament which had become increasingly assertive in all policy areas. He spent most of his time and energy struggling for his survival and little on dealing with the important policy agenda toward economic recovery. Thus, he failed to provide clear guidance and visionary leadership for his ministers to deal with economic problems. Again, 45

45 The fact that Wahid survived a near-fatal stroke in early 1998 which caused a serious problem with his eyesight leads some analysts to put great doubt on his ability to lead the country. For this reason, the government passed Law 23/2003 requiring the presidential and vice presidential candidates to be mentally and physically capable of holding the responsibility of the president and vice president.
this argument ignores the policy-making context under which Wahid had to work. Mahfud (2003) and Robison and Hadiz (2004:217), for example, argue that his unpredictable behavior and bizarre leadership were worsened by and at the same time a response to the institutional obstacle he was facing, which many times compromised his reform agenda. Therefore, this alternative explanation is also insufficient and scholars must direct their attention to the wider political structure rather than focus on any idiosyncratic factors.

To extend the argument, in the first part of this chapter I will assess the achievement in economic policy reform during the Wahid administration by looking at two main areas: fiscal policy and investment-related measures. I then link this achievement to the degree of executive strength. In the final part, I will present a case study of fuel subsidy reform to provide a deeper assessment of the effects of executive strength on achievements in economic policy reform. The overall conclusion of this chapter is that achievements in economic policy reform during the Wahid administration were extremely limited and this was substantially due to Wahid's low degree of executive strength.

3.2 Economic policy reform under Wahid

When Wahid came to power, the negative effects of the 1997 economic crisis were clear. For example, in 1998, economic growth was recorded at -13.2 per cent, inflation reached 77.63 per cent, and government debt exceeded its capacity to repay as it reached 102 per cent of GDP or four times higher than the pre-crisis level (Booth 1999:12; Ministry of Finance 2000a:116-7; Ministry of Finance 2000b:31). The annual budget needed further consolidation since deficit reached -3.9 per cent of GDP in 1999. This is not to mention poverty rate which was estimated to reach around 20 per cent of the population in 1999 (Cameron 1999:12-3; Booth 1999:20) and unemployment which reached 20 per cent of the total workforces by 1998 (Ministry of Finance 2000b:27). Understandably, the government made fiscal policy reform and investment-improving measures its top priority with the main objective being to accomplish fiscal sustainability. This required immediate reform in certain key aspects. The main objective was to create economic stability while at the same
time providing stimulus for economic growth and recovery. This had to be achieved without increasing government debt or compromising fiscal sustainability.46

In trying to achieve its objective, the government had work with the IMF. To show his commitment, Wahid sent several Letters of Intent (LoI) to the IMF.47 Stabilizing macroeconomic conditions, maintaining fiscal sustainability, restructuring banking sector, and propelling privatization were among the priorities. The document incorporates performance criteria with a clear target and time schedule. The government's ability to meet its commitment would affect financial support not only from the IMF but also from other international donors as well as business sentiment.48 Given the financial constraints and unfavorable economic conditions, it was more reasonable for Wahid to commit to this document though his administration later announced its own economic recovery programs.49

Beside the Letter of Intent, the government had to also refer to the Broad Guidelines of State Policy or Garis-Garis Besar Haluan Negara – hereafter GBHN – formulated by the MPR. The executive and the DPR then detailed this policy guideline into the National Development Program or Program Pembangunan Nasional – hereafter PROPENAS.

The next section will discuss the achievements in economic policy reform under the Wahid administration, starting with fiscal policy reform, followed by investment-related measures.

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46 There is no commonly agreed safe level for government debt to GDP ratio. Through Law 17/2003, the Government of Indonesia sets the maximum level of 60 per cent of GDP, beyond which fiscal sustainability will be at risk.


48 A clear example is what happened in 1998. The IMF required Indonesia to accomplish a budget surplus in that year. However, the national budget performed poorly and again recorded a huge deficit. Many investors reacted negatively to this performance by not taking any further investment and instead moved their money abroad (see Djiwandono 2003).

49 This was announced in August 2000 after the first cabinet reshuffle. It covers ten points: to maintain macroeconomic stability with the support of the IMF, World Bank, and ADB; to reduce unemployment by creating jobs in all regions; to improve agricultural productivity and farmer's welfare; to increase non-oil export revenues, particularly in manufacturing and agro-industrial sectors; to promote domestic and foreign equity investment; to advance banking restructuring; to accelerate privatization of state-owned enterprises; to initiate comprehensive small and medium scale enterprises (SME) development program; to ensure sustainable natural resource development; and to implement economic decentralization through an orderly and phased transition (Letter of Intent, 7 September 2000).
3.2.1 Fiscal policy reform

Considering the prevailing economic conditions at that time, the first and ultimate challenge for the Wahid administration was to push fiscal policy reform. In this respect, annual budget making was extremely important. With the main objective to achieve fiscal sustainability, it incorporated several interconnected policy measures such as broadening revenue bases to increase budget revenue, targeting resources more efficiently and effectively, maintaining a low deficit, and reducing foreign sources of financing the deficit by increasing domestic sources (Ministry of Finance and JICA 2002:54).

Looking at these policy areas, it is not difficult to see a gloomy picture. Overall, the achievement of fiscal policy reform under the Wahid administration was extremely limited. The discussion begins with the revenue side of the budget. The government was required and expected to broaden its revenue bases and this was an important cornerstone for fiscal sustainability.

In trying to broaden revenue base, the most important measure planned by the executive was pushing tax reform. The PROPENAS required the government to increase the tax ratio to 11.3 per cent of GDP in 2000 and 12.3 per cent of GDP in 2001. Among the strategies to achieve this were tax extension and intensification (Ministry of Finance 2000b:164). This is related to administrative reform. A more daunting challenge was pushing tax law reform. Through a Letter of Intent in January 2000, the executive planned to revise the existing tax laws, especially the value added tax law and the tax procedure law. The objectives were to strengthen the auditing and refund procedures and broaden the tax base.\(^{50}\) The executive expected to finalize the amendment by May 2000. Despite this target, the amended laws could only be passed by August 2000, raising concern about the ability of the government to push tax reform. More important than the failure to meet the target was the scope of the amendment. Only minor revisions were made to each of these laws.\(^{51}\) This raised another concern about whether the government could achieve its target to increase the tax ratio.

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\(^{50}\) See Letter of Intent, 20 January 2000.
Another important area in fiscal policy reform was targeting spending. In this respect, the GBHN required the government to make budget expenditure more efficient and effective by reducing ill-targeted subsidies and ineffective development expenditure. Similarly, the PROPENAS laid down four-pronged strategies to improve spending policies, namely, controlling banking restructuring costs, eliminating subsidies gradually and replacing the current mechanism with a well-targeted one, controlling the increase of public personnel expenses, and focusing development expenditure on certain sectors only. The executive also expressed its commitment to accomplish these aims in the Letter of Intent sent to the IMF. However, the real practice was quite the opposite of that recommended in these documents. The executive had to balance all spending posts to respond to the DPR’s various requests making prioritizing extremely difficult.

The most difficult area for the executive to target spending was eliminating subsidies, which progressed very slowly. The area of strongest concern was fuel subsidy reform. Through the new Letter of Intent signed on 20 January 2000, the Wahid administration committed to cut fuel subsidy since 2000. Its objectives were to reduce budget deficit, maintain fiscal sustainability, target resources effectively and conserve non-renewable energy. The real practice raised further skepticism. The plan to cut fuel subsidy by April 2000 was reversed and delayed until October. When that plan was finally executed in October 2000, despite significant fuel price increase in the international market, the executive only declared a minor adjustment of 12 per cent price increase on average which was limited to certain types of fuel only. The price of kerosene for household consumption was maintained despite the fact that only 20 per cent of this subsidized fuel was consumed by this group and the rest went to the better-off people (Ministry of National Development Planning 2005a). Only in early 2001 could the executive make significant progress by applying an automatic price adjustment in line with the dynamic of fuel price in international market, though it was still limited to certain types of fuel only. Other subsidies were maintained and the government only slightly increased the electricity tariff for large and industrial users by an average of 29 per cent in April 2000. The proposal for an

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52 In Indonesian misleading budget category, expenditure was divided into routine and development posts. Routine expenditure covers government personnel expenses, goods expenses, operational costs, subsidies, and debt amortization, while development expenditure refers to infrastructure expenses for strategic sectors to directly stimulate the economy. Such formula was changed in 2004 to follow a more commonly used international standard.

electricity tariff increase for households using up to 900 VA was delayed.\textsuperscript{54} These all put strong pressure on the annual budget given that at the same time the government had to allocate a significant amount of money to cover banking recapitulation costs. Should there be no debt rescheduling, the pressure on the annual budget was likely to be stronger.

With this slow progress of reform on the budget revenue side and difficulties in prioritizing spending, controlling the budget deficit and finding resources to cover it were also difficult. Through the GBHN and PROPENAS as well as the Letter of Intent, the executive announced its target to control the deficit. For example, it set the deficit at -5 per cent for the 2000 annual budget and -3.7 per cent for the 2001 annual budget. This posed a serious challenge for finding adequate financing sources. The executive also expressed its plan to rely more on domestic than foreign sources which was critical to accomplish fiscal sustainability. For domestic sources, it planned to mobilize receipts from some bases, two of which were controversial. The first one was asset recovery and the second one was the privatization of state-owned enterprises.\textsuperscript{55} The Ministry of State-Owned Enterprises and the Indonesian Banking Restructurization Agency (IBRA) were primarily responsible for accomplishing this with the approval of the DPR.\textsuperscript{56}

During the Wahid administration, asset recovery performance was disappointing and was much lower than expected. Meanwhile, for the private enterprises taken over by the government, only BCA was divested during his administration. With these delays, the plan to push governance reform was also delayed. As for privatization, no single state enterprise was privatized under his administration. PT Kimia Farma and PT Indofarma were indeed listed on the stock market in June 2001 through a public offering. However, the shares sold were all new ones and all receipts were put back into these enterprises (Kompas 15 August 2001). The government also failed to meet its commitment to privatize PT Semen Gresik to Cemex, a Mexican company producing cement. This poor achievement contradicted the Wahid administration’s repeatedly declared commitment to push forward the agenda as

\textsuperscript{54} See Letter of Intent, 17 May 2000 Section II Paragraph 3.

\textsuperscript{55} Asset recovery came from the selling of assets from the liquidated banks. Following the economic crisis in 1997, the government froze and took over many private banks facing cash-flow problems. Then it had to put a huge amount of money through a liquidity support facility. In return, the government took over their assets and sold them to finance the deficit.

\textsuperscript{56} IBRA was established in 1998 to mainly facilitate banking restructuring and asset recovery programs. Until 2004, it has the mandate to restructure the banks which were acquired by the government. It had to recapitalize those banks and divest all the acquired assets under its control.
expressed through the Letter of Intent sent to the IMF. The main objectives were, in particular, to mobilize resources to finance the budget deficit but also to release state enterprises from political capture, encourage competition and make them more efficient and beneficial.\textsuperscript{57} This was also in line with the GBHN and the PROPENAS direction which required the government to manage SOEs to be more efficient and effective in providing public services.

The effect of this failure on the annual budget was evident. With no single state enterprise being privatized, the revenue target from privatization for the 2000 budget failed to be met. This compromised the government target of financing the deficit using more domestic sources which also implied more borrowings. The financing of the budget deficit in 2000 (-1.6 per cent of GDP) came mainly from foreign sources: 62.5 per cent (or 1 per cent of GDP) compared to 37.5 per cent (or 0.6 per cent of GDP) from domestic sources. Should the budget deficit reach -4.8 per cent of GDP as planned in the annual budget and without the oil windfall, government borrowing would have reached more than this figure. The same risk applied to the 2001 budget as no single enterprise was privatized until Wahid left office. Given this achievement, the challenge for the new administration to push privatization would be more than critical.

More important than meeting the budget target, the poor progress in privatization put serious pressure on government credibility. There was no clarity as to who decided what and this was inimical to investor confidence (Deuster 2002:11). It also compromised the prospects for financial governance reform in those enterprises. Since they were still under government control, it was difficult to go ahead with reform initiatives. For SOEs, this was very critical because most of them are cash cows for certain political elites. Moreover, under government (majority) ownership, most if not all SOEs are managed using more political than corporate principles which worsens the already notorious inefficiency and corruption. This poor performance exacerbated the already weak investor confidence (Pangestu and Goeltom 2001:147). Investor confidence declined significantly from mid 2000 until Wahid's impeachment in July 2001. Conflict with Cemex scared investors even more. The DPR's opposition to privatize the government's shares to this company despite

the commitment the government had rendered Indonesia’s investment climate highly unfavorable. 58

What can be concluded from the discussion so far is that very limited achievement occurred in fiscal policy reform under the Wahid administration. On both the revenue and spending sides of the budget, the executive was forced to accommodate what the DPR wanted at the cost of fiscal reform. The budget deficit was decided politically and the executive found it extremely difficult to finance it. Given the fiscal constraints, the privatization of state enterprises became a short-cut strategy to finance the deficit, making the prospect of genuine reform in this area less clear. These delays partly contributed to the poor fiscal performance during the Wahid administration as shown in Table 3.1. If there was one area in which he could push a reform agenda, it was tax reform though the scope of the amendments was limited. With only minor amendments, the amended laws could be adopted relatively easily.

The table shows that there were wide discrepancies between what was planned in the budget document and its actual realization. While some of the indicators such as exchange rate, oil price, and oil production were subject to factors other than the policy-making process, most were dependent on it. As will be discussed later in other section, the discrepancies were because of the executive’s inability to make a reasonable projection against opposition voices.

58 Another case in point is the selling of BCA’s assets in Sinar Mas Group. To recover the government’s recapitulation fund in BCA, IBRA finally decided to sell 25 palm oil plantations located in Sumatra, Kalimantan and Sulawesi to Guthrie Berhad Ltd, a Malaysian company. However, along with local people, business associations and NGOs, the DPR opposed this plan and requested IBRA to review its decision (DPR RI 2001:256; Kompas 25 January 2001). It based its opposition on the legal uncertainty over land ownership and the concern that Malaysia would monopolize the palm oil market. Though the process went on, Guthrie expressed its concern over the protection of property rights.
Table 3.1 Fiscal performance during the Wahid administration

<table>
<thead>
<tr>
<th>Indicators</th>
<th>2000 Budget</th>
<th>Actual</th>
<th>2001 Budget</th>
<th>Actual</th>
</tr>
</thead>
<tbody>
<tr>
<td>Growth (%)</td>
<td>3.8</td>
<td>4.9</td>
<td>5.0</td>
<td>3.4</td>
</tr>
<tr>
<td>Inflation Rate (%)</td>
<td>4.8</td>
<td>9.35</td>
<td>7.2</td>
<td>12.55</td>
</tr>
<tr>
<td>Exchange Rate (Rp to US$)</td>
<td>7,000</td>
<td>8,425</td>
<td>7,800</td>
<td>10,241</td>
</tr>
<tr>
<td>Oil price (US$/barrel)</td>
<td>20</td>
<td>28.26</td>
<td>24</td>
<td>24.6</td>
</tr>
<tr>
<td>Oil Production (thousand barrel/day)</td>
<td>1,460</td>
<td>1,400</td>
<td>1,460</td>
<td>1,300</td>
</tr>
<tr>
<td>Interest rate (%)</td>
<td>13</td>
<td>12.31</td>
<td>11.5</td>
<td>16.4</td>
</tr>
<tr>
<td>Revenue (% of GDP)</td>
<td>15.1</td>
<td>20.8</td>
<td>17.7</td>
<td>20.9</td>
</tr>
<tr>
<td>Expenditure (% of GDP)</td>
<td>20.1</td>
<td>22.6</td>
<td>21.2</td>
<td>23.7</td>
</tr>
<tr>
<td>Surplus/Deficit (% of GDP)</td>
<td>-5.0</td>
<td>-1.6</td>
<td>-3.5</td>
<td>-2.8</td>
</tr>
<tr>
<td>Domestic financing (% of GDP)</td>
<td>2.4</td>
<td>0.6</td>
<td>2.2</td>
<td>2.1</td>
</tr>
<tr>
<td>Foreign financing (% of GDP)</td>
<td>2.5</td>
<td>1.0</td>
<td>1.3</td>
<td>0.7</td>
</tr>
</tbody>
</table>


3.2.2 Investment policy reform

Besides fiscal policy reform, the Wahid administration committed to pushing the investment policy reform to increase and sustain economic growth. Since the 1997 economic crisis, economic growth had mainly been led by increased consumption and government spending while investment contribution was extremely limited (Boediono 2001:54; Athukorala 2002:148; Deuster 2002:19). Pangestu and Goeltom (2001:149) even argue that the Rupiah’s depreciation and high inflation rate which led to pessimism over sustainable recovery changed consumer consumption behavior. Some hedged their spending on durable goods in anticipation of inflation. Meanwhile, the export surge could not be sustained as the government aimed to bring Rupiah depreciation down to a reasonable level.
With unsustainable consumer consumption and export revenue, the trigger for higher growth was expected to come from investment. By the end of 2000, the level of investment was only 59 per cent of the pre-crisis level (Bird 2001:48). As for foreign investment, the average proposal had declined from nearly US$ 50 million during the 1994-1997 period to only around US$ 9 million in the 1998-2001 period. Moreover, foreign direct investment was only US$ 15 billion on average for the period of 1999 to 2001 compared to US$ 30 billion on average prior to the 1997 crisis (Pangestu and Goeltom 2001:148). Therefore, the Wahid administration planned to push reform in the investment area. To this end, the executive expressed its commitment to maintaining a liberal trade regime. Removing tariff and non-tariff trade barriers, eliminating export restrictions, and inducing competition in the energy sector were among the policy measures. The first two performed relatively well and the executive adopted several reform measures. Clear examples were the removal of all non-tariff import restrictions on rice and sugar. This is because the executive could simply execute the removal without the DPR approval and Indonesia had adopted a relatively liberal trade regime since the 1980s. Discussing this is outside the focus of this thesis. The following discussion will focus on how to inducing competition in the energy sector where progress was less certain.

To push reform in the energy sector, the executive maintained its priority on the oil, gas and electricity sectors as expressed several times since the first Letter of Intent to the IMF in January 2000. For the oil and gas sector, despite the huge potential, the investment in these areas had declined significantly since the start of the 1997 economic crisis. Among the reasons for this decline was the lack of competition due to the existence of the state monopoly. Therefore, besides restructuring PERTAMINA – Indonesia’s state-owned enterprise responsible for fuel production and distribution – the executive also planned to revise Law 8/1971 to better reflect the current economic dynamics. Its main objective was to endorse private sector participation in both upstream and downstream activities. Under this scheme, the government would still control the resources but its management could be shared with or transferred to the private sector which was assumed to be more professional and efficient. When Wahid left office, the new law had not yet been enacted.

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The same story also applies to the electricity sector. The executive planned to push reform in this area given its worrisome performance. There have been complaints among Indonesians and business sectors about the poor service quality in this sector, especially the inadequate power supply (Alisjahbana and Manning 2002:297). The main explanation for this problem is the fact that the state-owned electricity company, the PLN, still holds the monopoly. Due to this monopoly, it acts as both the regulator and the provider. This discourages competition which leads to poor service quality. Therefore, through the Letter of Intent to the IMF in January 2000, the Wahid administration maintained its commitment to push reform in this area with the objectives of restoring commercial viability, improving efficiency and attracting private investment. Part of the plan was to revise Law 15/1985 which was seen to be outdated given the many significant developments in this area. Measures to support this plan had actually begun in 1998. In 2000, the executive submitted its draft to the DPR. As in the case of the oil and gas bill, it had not been enacted by the time Wahid left office.

What I can conclude from the discussion on investment-related reform measures is that the Wahid administration failed to adopt the planned reforms. This is contrary to the targets or commitment it had made, especially through the Letter of Intent to the IMF. Together with the poor performance in the fiscal policy area, this forced the IMF to become even more deeply involved in pushing economic policy agenda with more coercive micromanagement approach (Pangestu and Goeltom 2001:146; Martinez-Diaz 2006:407).

Why was the achievement in economic policy reform extremely low under the Wahid administration? The following section will address this question.

3.3 The effect of executive strength

To understand the lack of achievement in economic policy reform under the Wahid administration, the context of policy-making during Wahid's period needs to be understood. This thesis argues that while opposition to reform initiatives is important, it is the inability of the executive to deal with opposition that matters most for achievements in economic policy reform. This inability was related to the degree of executive strength
coming from a president’s constitutional powers and partisan support. Therefore, the fact that the Wahid administration only adopted very limited economic policy reform is significantly explained by Wahid’s low executive strength. This lack of institutional underpinning prevented Wahid from governing effectively while at the same time creating policy space for the DPR to play on populist and nationalist sentiments. The following paragraphs will extend this argument by first looking in detail at the degree of executive strength under the Wahid administration.

3.3.1 Executive strength under Wahid

As briefly discussed in Chapter 2, in the constitutional aspect, Wahid had no protection over security of tenure. Indonesia’s constitution until the late 2001 gave power to the MPR as an electoral college to elect the president and vice president and also to remove them from office. There was consequently no protection over the executive’s security of tenure. This is a serious liability for a president wishing to adopt politically difficult economic policy reform. The absence of such protection is consequential given that Wahid - as well as other post-Suharto presidents - had only limited legislative powers. He had insufficient veto and or decree powers to push his own agenda. Wahid was therefore a constitutionally weak president.

Wahid’s weak position was also evident in the first and second constitutional amendments in the late 1999 and 2000, through which the MPR removed many of the president’s powers and prerogatives and transferred them to the DPR. For example, the president no longer has power over making legislation;\(^60\) this is now under the DPR’s control and the president can only propose bills with a privilege over budget bill introduction. Consultation with the DPR is even required for almost all areas under the executive’s prerogative such as establishing diplomatic relations, giving clemency, making international treaties, and declaring war. While its initial purpose was to enhance executive-legislative checks and balances, constitutional amendments up to 2000 had in fact limited the president’s power significantly while at the same time empowering the DPR. Gorjao (2003) cynically argues

\(^60\) Indonesia’s original constitution stipulates that the president has the authority to make laws with the approval of the DPR.
that the constitutional amendment actually prepared the way for Wahid's removal from office.

With limited constitutional powers, Wahid had to establish a legislative majority to survive and govern effectively. As also discussed in Chapter 2, even a weak president can govern successfully as long as he or she has strong partisan support in parliament. For Wahid, this was mandatory considering the coming of multiparty system resulting from the 1999 election (see Appendix 1). Establishing a coalition was more a necessity than a choice given the high fragmentation of power in both the DPR and the MPR with as many as ten fractions (see Table 3.2). Moreover, he came from a minor party, PKB, with only 10.2 per cent of seats in the DPR and only 8.2 per cent of seats in the MPR (Mietzner 2001:31). Even with the support of his Central Axis allies,\(^6\) his legislative contingent was still far from sufficient to achieve a legislative majority in parliament (only 30 per cent). Therefore, Wahid then established a grand coalition cabinet involving all major parties.

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\(^6\) The Central Axis is a loose coalition among Islamic parties such as PAN, PBB, PPP, and PK which engineered Wahid's election. One of its leading figures is Amin Rais who then became the Speaker of the MPR.
### Table 3.2 Composition of the DPR and MPR, 1999-2004

<table>
<thead>
<tr>
<th>Fractions</th>
<th>DPR seats (number)</th>
<th>DPR seats (%)</th>
<th>Regional Delegates (number)</th>
<th>MPR seats (Number)</th>
<th>MPR seats (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>A</td>
<td>B</td>
<td>C</td>
<td>A + C</td>
<td>D</td>
</tr>
<tr>
<td>PDIP</td>
<td>153</td>
<td>30.6</td>
<td>32</td>
<td>185</td>
<td>26.61</td>
</tr>
<tr>
<td>GOLKAR</td>
<td>120</td>
<td>24</td>
<td>62</td>
<td>182</td>
<td>26.18</td>
</tr>
<tr>
<td>PPP</td>
<td>58</td>
<td>11.6</td>
<td>12</td>
<td>70</td>
<td>10.07</td>
</tr>
<tr>
<td>PKB</td>
<td>51</td>
<td>10.2</td>
<td>6</td>
<td>57</td>
<td>8.20</td>
</tr>
<tr>
<td>Reformasi (PAN + PK)</td>
<td>41</td>
<td>8.2</td>
<td>7</td>
<td>48</td>
<td>6.90</td>
</tr>
<tr>
<td>PBB</td>
<td>13</td>
<td>2.6</td>
<td>1</td>
<td>14</td>
<td>2.01</td>
</tr>
<tr>
<td>KKI (PKP + 7 smaller parties)</td>
<td>12</td>
<td>2.4</td>
<td>2</td>
<td>14</td>
<td>2.01</td>
</tr>
<tr>
<td>PDU (PNU + 4 smaller parties)</td>
<td>9</td>
<td>1.8</td>
<td>-</td>
<td>9</td>
<td>1.29</td>
</tr>
<tr>
<td>PDKB</td>
<td>5</td>
<td>1</td>
<td>-</td>
<td>5</td>
<td>0.71</td>
</tr>
<tr>
<td>TNI/POLRI</td>
<td>38</td>
<td>7.6</td>
<td>-</td>
<td>38</td>
<td>5.46</td>
</tr>
<tr>
<td>Societal</td>
<td>-</td>
<td>-</td>
<td>65 UG + 8</td>
<td>73</td>
<td>10.50</td>
</tr>
<tr>
<td>Delegates (UG)</td>
<td></td>
<td></td>
<td>UD</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>500</td>
<td></td>
<td></td>
<td>195</td>
<td>695</td>
</tr>
</tbody>
</table>

Source: Adapted from [www.dpr.go.id](http://www.dpr.go.id) and [www.mpr.go.id](http://www.mpr.go.id)

Due to his vulnerability to dismissal, Wahid had to accommodate what the MPR wanted in establishing his cabinet. He consulted with leaders of major forces through backdoor negotiations in distributing cabinet posts: Megawati from PDIP, Akbar Tanjung from GOLKAR, Amin Rais from PAN as well as Central Axis, and Wiranto from the ABRI faction.\(^{62}\) They acted as guarantors for the nominees in cases of misconduct (Slater 2004:71).\(^{63}\) Worse than that, most of the figures included in the cabinet were imposed on him by major forces in the parliament which he could only accept given his vulnerable position. Understandably, his cabinet was dominated by figures with political affiliation. Of special concern was the composition of the economic team. It was ‘drawn from very different backgrounds and may have divergent views on both the content and the conduct of economic policy’ (Booth 1999:34). Harmony among cabinet ministers soon disappeared.

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\(^{62}\) Hamzah Haz was not involved despite PPP’s large share of parliamentary seat, 11.6 per cent, because it had joined the Central Axis which was represented by Amin Rais.

\(^{63}\) One leading newspaper cynically dubbed the Wahid cabinet as a “Toshiba Cabinet”, a cabinet with a guarantee as for electronic products such as Toshiba (Tempo 01-07 November 1999).
replaced by internal strife (Booth 1999:33-4; Fane 1999:20; Haggard 2000:124; Mietzner 2000:39; Ramstetter 2000:5; van Dijk 2001:497). As shown in Table 3.3, of 35 cabinet members, 77 per cent were politically connected, either with parties (60 per cent) or the military (17 per cent), and only 23 per cent were non-partisan professionals. Moreover, his coalition had as many as 95.6 per cent of DPR seats, involving all major parties as well as tiny parties such as PK, PBB, and PKP, leaving no space for opposition.

<table>
<thead>
<tr>
<th>No</th>
<th>Affiliation (party/other)</th>
<th>Total vote (%)</th>
<th>Total seat (%)</th>
<th>Cabinet portfolio (number)</th>
<th>Cabinet portfolio (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>PDIP</td>
<td>33.7</td>
<td>30.6</td>
<td>4</td>
<td>11.4</td>
</tr>
<tr>
<td>2</td>
<td>GOLKAR</td>
<td>22.4</td>
<td>24</td>
<td>4</td>
<td>11.4</td>
</tr>
<tr>
<td>3</td>
<td>PKB</td>
<td>12.6</td>
<td>10.2</td>
<td>4</td>
<td>11.4</td>
</tr>
<tr>
<td>4</td>
<td>PPP</td>
<td>10.7</td>
<td>11.6</td>
<td>2</td>
<td>5.7</td>
</tr>
<tr>
<td>5</td>
<td>PAN</td>
<td>7.3</td>
<td>6.8</td>
<td>4</td>
<td>11.4</td>
</tr>
<tr>
<td>6</td>
<td>PBB</td>
<td>1.8</td>
<td>2.6</td>
<td>1</td>
<td>2.9</td>
</tr>
<tr>
<td>7</td>
<td>PK</td>
<td>1.3</td>
<td>1.4</td>
<td>1</td>
<td>2.9</td>
</tr>
<tr>
<td>8</td>
<td>PKP</td>
<td>1.03</td>
<td>0.8</td>
<td>1</td>
<td>2.9</td>
</tr>
<tr>
<td>9</td>
<td>ABRI</td>
<td>-</td>
<td>7.6</td>
<td>6</td>
<td>17.1</td>
</tr>
<tr>
<td>10</td>
<td>Non-partisan</td>
<td>-</td>
<td>-</td>
<td>8</td>
<td>22.9</td>
</tr>
<tr>
<td></td>
<td>Total</td>
<td>90.83</td>
<td>95.6</td>
<td>35</td>
<td>100</td>
</tr>
</tbody>
</table>

Note: The total seat for each party is different from the one in Table 3.1 since I calculate the total number of seat in parliament which includes ABRI.

Source: Author's calculation from various publications.

This cabinet inclusiveness is important for two main reasons. No less important than securing his tenure, it provided him with a legislative majority to enable him to win the legislative agenda in the DPR. Given policy challenges he had to face at that moment on the one hand and a fragmented parliament on the other hand, Wahid had to have a legislative majority to be able to govern effectively. Additionally, the nature of the policymaking process implies that only with the support of the majority fractions in the DPR

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64 A clear example was conflict between Kwik Kian Gie and Sofyan Wanandi. Moreover, besides the economic team in the cabinet, he appointed at least four auxiliary bodies, namely, National Economic Council, National Council for Business Development, Assistance Team, and Monitoring Team.

65 The other subsidiary motives behind Wahid's grand coalition cabinet were a matter of pay back, that is, to 'return favors to those who had made his own election possible' (van Dijk 2001:467; see also Kingsbury 2002:254-5) and to 'to accommodate all the main parties and thus to reduce the tensions that were aroused by the struggle over the presidency in order to avoid risking any exacerbation of unrest' Mackie (1999:154).
could he move forward with any policy agenda, especially for politically difficult agenda. Having a legislative majority was also important given the president’s limited legislative powers. As shown in Table 3.4, he included eight major fractions in the DPR with the total share of 486 out of 500 DPR seats or 97.2 per cent. Only two tiny fractions with insignificant share of seats, 2.8 per cent, were excluded. They are far from sufficient to be an effective opposition, if they can be called an opposition at all.

Table 3.4 Fractions in Wahid’s coalition cabinet

<table>
<thead>
<tr>
<th>No.</th>
<th>Fractions</th>
<th>DPR seats (number)</th>
<th>DPR seats (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>PDIP</td>
<td>153</td>
<td>30.6</td>
</tr>
<tr>
<td>2</td>
<td>GOLKAR</td>
<td>120</td>
<td>24</td>
</tr>
<tr>
<td>3</td>
<td>PPP</td>
<td>58</td>
<td>11.6</td>
</tr>
<tr>
<td>4</td>
<td>PKB</td>
<td>51</td>
<td>10.2</td>
</tr>
<tr>
<td>5</td>
<td>Reformasi</td>
<td>41</td>
<td>8.2</td>
</tr>
<tr>
<td>6</td>
<td>PBB</td>
<td>13</td>
<td>2.6</td>
</tr>
<tr>
<td>7</td>
<td>KKI</td>
<td>12</td>
<td>2.4</td>
</tr>
<tr>
<td>8</td>
<td>TNI/POLRI</td>
<td>38</td>
<td>7.6</td>
</tr>
<tr>
<td>Total</td>
<td></td>
<td>486</td>
<td>97.2</td>
</tr>
</tbody>
</table>

Source: Author’s calculation from www.dpr.go.id

This grand coalition should have given Wahid consolidated support which would help him achieve his legislative agenda. This was not the case, however. Since his survival depended on parliamentary support, he could not maintain consolidated legislative support. On the contrary, Wahid had to desperately craft legislative support without a sense of freedom as the first democratically elected president. Those included in his grand coalition were also those who mounted opposition to him and in the end engineered his removal from office. The opposition to him was even stronger following the first cabinet reshuffle and thereafter, through which he reduced party involvement significantly (see Appendix 3). The root of the problem lays in the institutional arrangements he was working with. The absence of constitutional protection over the executive’s security of tenure due to the power of the MPR to remove the executive from office proved very costly for the president. Without this

66 The cabinet reshuffle or “restructurization” in Wahid’s terms indicates that he wanted to distance himself from political parties and maintain a sense of independence from the parliament. It is clear that Wahid considered coalition unworkable (Gorjao 2003:33). Therefore, he first reduced the number of cabinet members from 35 to 26 posts with 3 additional advisory posts of minor significance. He also changed the composition of the cabinet by giving more portfolios to non-partisan figures (34.5 per cent).
protection, Wahid could not consolidate partisan support from his inclusive coalition. His effort to consolidate power by distancing himself from his coalition allies only justified the latter in removing him from office.

Looking at the combination of constitutional powers and partisan support, I conclude that Wahid was a weak president. His executive strength was extremely low. This lack of institutional underpinning is a serious liability to effective policy-making. Due to the lack of independence from the parliament, in most policy initiatives, Wahid and his economic team had to accommodate what the DPR wanted. Moreover, the members of the DPR were also the very members of the MPR who had the power to remove him from office. Since the DPR had a tendency to favor populism over good policy, economic policy reform became much more difficult to advance. This was especially true for policy reform in areas with political significance such as fiscal reform, privatization, fuel subsidy, and investment-related measures. DPR opposition to these initiatives had almost definitely brought Wahid’s reform agenda to an end. Wahid led the government but failed to govern effectively (Sadli 2001:485). The decision-making process thus became a competitive territory between the president and DPR with the first becoming more dependent on the latter (Kingsbury 2002:265). Worse than that, DPR approval was mandatory for any policy initiative even in areas under the executive’s domain (DPR RI 2000; DPR RI 2001; Mulyani 2001). Due to these very practices, some analysts expressed concern about the danger of DPR tyranny (Bayhagi 2001; Karman 2001; Suwarno 2001). Lubis (2001) even dubbed Indonesian politics under Wahid as ‘government by legislature’ while Muhammad (2002:155) cynically calls all political maneuvers in the Wahid era a ‘game without rules of a game’. 67

These institutional arrangements created policy uncertainty and widespread confusion with noisy economic policy-making (Mulyani 2001). Moreover, having spent most of his energy and time struggling for his survival, Wahid failed to act as an independent and visionary leader to provide clear guidance for his economic team on how to deal with the issues at hand. Even his ministers were trapped in his conflict with the parliament making them less

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67 Due to this reason, many reform-minded politicians, including those from the PKB, mobilized support in the MPR to undertake a more substantive constitutional amendment to give the executive more sense of independence as under a pure presidential system so that it could balance the parliament.
able to concentrate on upholding their jobs (Sadli 2002:12). Had Wahid had constitutional security of tenure and been able to craft consolidated coalition, the situation could have been totally different.

The next sections assess the effect of Wahid's low executive strength on the adoption of economic policy reform. Considering the complexity of the issues, I divide this section into three parts: fiscal policy reform, privatization, and investment policy reform.

### 3.3.2 Fiscal policy reform

In pushing fiscal policy reform, the most difficult job for the Wahid administration was the formulation of the annual budget. The main objective was to accomplish fiscal sustainability. Here, the executive had to set certain targets such as economic growth, inflation rate, interest rate, Rupiah exchange rate, revenue and expenditure rate, and deficit and its financing. Some items on the policy reform agenda were also tied to the budget document such as tax reform, subsidy reform, and privatization as well as investment-related measures. As budget making did not directly affect certain interests and dealt generally with the national agenda, a compromise between the executive and the DPR was relatively easier to reach, except in areas where further legislative process was needed. This was because the executive and the DPR shared similar views on propelling fiscal sustainability and economic recovery in general and, under the economic conditions at that time, government intervention through the annual budget was extremely important. Table 3.5 summarizes the results of such compromises for the 2000 and 2001 annual budgets.
### Table 3.5 Key indicators for the 2000 and 2001 annual budgets

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Growth (%)</td>
<td>4-5</td>
<td>3.8</td>
<td>3.8</td>
<td>4.5-5.5</td>
</tr>
<tr>
<td>Inflation Rate (%)</td>
<td>7-9</td>
<td>4.8</td>
<td>4.8</td>
<td>6-8</td>
</tr>
<tr>
<td>Exchange Rate (Rp to US$)</td>
<td>7,000-8,000</td>
<td>7,000</td>
<td>7,000-8,000</td>
<td>7,300</td>
</tr>
<tr>
<td>Oil price (US$/barrel)</td>
<td>-</td>
<td>18</td>
<td>20</td>
<td>-</td>
</tr>
<tr>
<td>Oil Production (thousand barrel/day)</td>
<td>-</td>
<td>1,460</td>
<td>1,460</td>
<td>1,460</td>
</tr>
<tr>
<td>Interest rate (%)</td>
<td>12</td>
<td>13</td>
<td>13</td>
<td>11.2</td>
</tr>
<tr>
<td>Revenue (% of GDP)</td>
<td>19.4</td>
<td>15.1</td>
<td>16.8</td>
<td>17.3</td>
</tr>
<tr>
<td>Expenditure (% of GDP)</td>
<td>22.8</td>
<td>20.1</td>
<td>21.6</td>
<td>21.0</td>
</tr>
<tr>
<td>Deficit (% of GDP)</td>
<td>-3.4</td>
<td>-5.0</td>
<td>-4.8</td>
<td>-3.7</td>
</tr>
<tr>
<td>Domestic financing (% of GDP)</td>
<td>1.7</td>
<td>2.5</td>
<td>2.7</td>
<td>2.3</td>
</tr>
<tr>
<td>Foreign financing (% of GDP)</td>
<td>1.7</td>
<td>2.5</td>
<td>2.1</td>
<td>1.4</td>
</tr>
</tbody>
</table>


Despite these compromises, a closer look into the process of the budget making will reveal that the formulation of the annual budget was predominantly dictated by political logic. In this the DPR played a significant role rather than following a more rational, technocratic process. Indonesia’s constitution does provide the executive with the authority to propose the annual budget. However, this bill had to be approved by the DPR to become law and there is no single stipulation on the extent to which the DPR can revise it. Therefore,
despite the lack of expertise in the area of budget making, or 'economic literacy' as Bird et al. (2007:10) might call it, the DPR actively criticized the executive's budget proposal and opposed some measures employing populist and nationalist sentiments. It simply wanted to show that it was no longer the executive's rubber stamp and had the power to involve in the budget making with a much empowered budgetary right. Moreover, it realized that the survival of the president depended on it. This trend was even stronger when the president took some controversial measures which triggered executive-legislative tension, especially the sacking of some ministers from political parties.69

The assertiveness of the DPR in the budget making process even started with the setting of macroeconomic targets such as economic growth, Rupiah exchange rate, inflation, interest rate, international oil price and the volume of oil production. This was a critical job for the government as it would show how the country's economy would look in at least the next year and whether or not it would be promising and secure for the business community to carry out its activities. A careless projection could lead to a wide gap between the plan and achievement and this would only create further uncertainty for these actors. It would not only fail to bring economic recovery but also compromise it at worst. Amidst this concern, the DPR involved very actively, rendering the process politically dictated. In this context, the new DPR was a real political obstacle.70 Whatever targets the executive set, the DPR always criticized and requested the executive to revise them. For example, if the executive projected a relatively high economic growth, the DPR criticized it as unrealistic or too optimistic and, therefore, would compromise investor's confidence once it failed to be achieved. On the other hand, if the executive set a lower target for economic growth, the DPR also criticized it for lacking direction, being pessimistic or having no sense of mission to bring about economic recovery (see for example GOLKAR 2000a; GOLKAR 2000b;

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69 Though Wahid sacked several ministers, the removal of Laksamana Sukardi and Yusuf Kalla in April 2000 was the most fatal one since it involved two largest parties in parliament, PDIP and GOLKAR (NDI 2001:6; Mietzner 2001:32; Barton 2002a:302; Mahfud 2003:94), which then initiated interpellation to summon the president regarding his decision. The removal of Hamzah Haz (PPP) in November 1999 and the resignation of General Wiranto (ABRI) in May 2000 and Kwik Kian Gie (PDIP) in August 2000 only complicated the game. His desperate moves to replace some key ministers after the second cabinet reshuffle made executive-legislative relationships even worse. See Muhammad (2002) and Simanjuntak (2003) for more extensive discussion on this matter.

70 This is not to say that the DPR was the only factor which prevented the executive from making a reasonable projection. Other factors were also important such as the performance of the world economy as well as Indonesian neighbors' economy and the mood of the business community, all subject to change.
The end result was a political compromise regardless of how poorly-formulated it was. Its implication for the whole budget was undeniable.

A more daunting task in the annual budget making was when the executive and the DPR debated budget revenue, expenditure, deficit target and how to finance the deficit. These were critical issues since they provided the policy cornerstone for achieving fiscal sustainability and, therefore, set the benchmark for related actors especially investors to make any decision. As mentioned earlier, the executive had laid down several strategies for fiscal reform toward fiscal sustainability such as consolidating the state budget, expanding revenue bases, targeting expenditure, implementing good governance in the public sector, and building up the domestic bond market. In putting these strategies in place, expanding revenue bases and targeting resources are of special interest since they deal directly with economic policy reform. Any policy measure to change the status quo in these two areas required the approval of the DPR. Worse than that, the executive had to face the very reality that the DPR always demanded more spending regardless of budget revenue. It even opposed the executive’s reform proposal to target expenditure efficiently and effectively and to mobilize extra resources from tax and or privatization receipts. Given Wahid’s limited political resources, he encountered difficulties in pushing reform in these areas.

On the revenue side, tax receipts were still the main source of budget revenue. Another source was non-tax receipts. A target was also set to increase tax receipts more than non-tax revenue. This was to be achieved by raising the tax ratio and tax coverage. While the president and the DPR had agreed on these targets, they held different opinions about how to achieve them. For example, for the 2000 annual budget, the Budget Committee requested the executive to increase revenue by raising the tax ratio from the proposed 10.1 per cent of

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71 In setting macroeconomic projections, the executive employed certain methods and considered many factors with potential or real effects on the economy. This was to make budget projection more reasonable. In setting economic growth target, for example, the executive considered the trend from previous year in both domestic and international economy, relevant social and political development, and the need for certain stimulus for economic growth. This also applied to other targets. Fortunately, there was no room for the DPR to play with inflation and interest rates as these are under the authority of an independent central bank (see for example Ministry of Finance 2000a; Ministry of Finance 2000b; Ministry of Finance 2004; Ministry of Finance 2007).
GDP and tax coverage which covered only 66.33 per cent of overall potential tax payers (DPR RI 2000b:209). The non-tax revenue had to be increased as well from the proposed 4.4 per cent of GDP by boosting revenue from oil, gas, and other natural resources as well as dividend from the state-owned enterprises. Such concerns were also raised by PDIP (2000a), GOLKAR (2000a), PPP (2000a), Reformasi (2000a), and TNI/POLRI (2000a). In general, as requested by PDIP (2000a), TNI/POLRI (2000a) and PBB (2000a), budget volume had to be increased to be able to serve as a stimulus instrument for economic growth at least in the short run. However, the DPR was against the plan to raise tax revenue by 38.7 per cent through increasing 74 per cent of income tax and 100 per cent of levies as it could compromise the prospects for economic growth and trade liberalization. The same opposition was expressed during the 2001 budget debates. The DPR again requested the executive to increase tax revenue. However, it was against the plan to increase value-added taxes by 12.5 per cent (Abimanyu 2003:271). All it asked was for the executive to improve tax and non-tax administration, considering the widespread practices of corruption, collusion, illegal mining, illegal logging and illegal fishing.

In response to the DPR’s request, the executive had to give up many of its plan for further tax reform and could only revise the existing tax laws with the emphasis on improving tax administration. This was politically acceptable since tax reform is a politically sensitive measure and the executive would not risk its already vulnerable position by pushing this agenda. Even if the executive insisted on pushing reform in this area, the opposition from the DPR would almost certainly block it. Therefore, only limited progress was made in this area. In April 2000, the executive proposed new drafts to revise the existing laws on income tax, value-added tax, tax procedure, tax collection by force, land and building excises, and local taxes. Among the proposed changes were increasing the penalty for recalcitrant tax payers, clearer legal sanctions for tax evasion, broadening tax coverage with

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72 The exact number of tax payers in Indonesia is not known. The DPR always maintains that it covers only 40 per cent of the eligible tax payers while the executive states that more than 60 per cent of the tax payers are already covered. The Ministry of Finance reports that in 2001, it covered only 1.9 million people out of more than 200 million of the population. This was planned to be increased to 3.5 million people in 2002 and 9 million people in 2004 (Ministry of Finance and JICA 2002:56). Poor tax administration is still a serious concern.

73 GOLKAR even proposed that revenue from forestry sector had to be increased from the proposed Rp 1.2 trillion to Rp 6 trillion. This is a more-than-four-times increase. For this party, this is a reasonable request and achievable insofar the executive can combat illegal mining, illegal logging and illegal fishing.

74 The Reformasi fraction suggested that revenue from SOEs be increased from the proposed Rp 4 trillion to Rp 8 trillion. The executive had to improve the performance of all SOEs.
much clearer stipulation of tax subjects and objects, tax exemption such as for religious donations (zakat) and profit for small-scale enterprises involved in any joint venture, increasing the non-taxable income rate, reducing the taxable income tax rate with a higher and wider range, and still many others. The overall objectives were to create legal certainty and improve tax administration which was expected to enhance tax compliance while at the same time stimulating economic growth. The DPR – as well as other tax stakeholders – expressed a negative response to these drafts arguing that such measures were insufficient to boost tax revenue. It argued that under existing economic conditions, such initiatives would only put an additional burden on tax payers since indirect taxes such as value-added taxes were still dominant (Kompas 23 June 2000; Kompas 07 July 2000). The DPR instead succeeded in pushing its populist agenda by offering special treatments in the revised laws.\textsuperscript{75} Thus, no significant change was achieved in tax policy. Even without a major amendment, the executive was forced to wait until August 2000 before the DPR approved the laws, quite a long delay for the executive’s target of passing them by May 2000.

A more daunting challenge came from the DPR when debating budget spending. Given that the executive had limited resources and the DPR opposed the plan to increase tax rates, there was a compelling need to push reform toward targeting resources more efficiently and effectively. Cutting ill-targeted subsidies and less important posts were among the main strategies. Compared to revenue measures, these were all politically difficult since they directly removed certain allocations to certain groups and contained certain redistributive elements by taking something from certain segments of society and giving it to the others. Given the weak executive strength in both constitutional and partisan aspects, Wahid also faced difficulties in dealing with opposition in this area. The discussion will now focus on issues other than the fuel subsidy which will be assessed in the last section of this chapter.

Though the DPR agreed with spending strategies, it was against the executive’s plan to implement them. Instead, the DPR again employed populist slogans. In debating the 2000 budget, for example, the Budget Committee argued that the national budget was at risk since routine spending alone had exceeded domestic revenue. However, it requested the

\textsuperscript{75} Clear examples are the exemption of religious donation and profits from small-scale enterprises as taxable objects. Moreover, while the tax range was increased, tax rate was reduced significantly. For a deeper assessment, see Law 16/2000, Law 17/2000, Law 18/2000, Law 19/2000, and Law 20/2000.
executive to thoroughly recalculate and then increase personnel expenses to at least cover minimum living expenses. As if to confirm its populist stand, the DPR also opposed the executive’s plan to spend a huge amount of money to cover banking recapitulation costs which could put the national budget into difficult position. Moreover, the DPR requested the executive to recalculate subsidy expenses so that a fuel price increase would not burden the people (Budget Committee 2000b:3).

Following this, all fractions in the DPR raised criticisms. In the draft budget, the executive’s proposal for the composition of routine and development allocations was 78.5 per cent and 21.5 per cent, respectively. The DPR required the executive to revise this by at least 60 per cent and 40 per cent or 65 per cent and 35 per cent, respectively. Such criticism came from the GOLKAR (2000b), PKB (2000b), PBB (2000b), Reformasi (2000b), and TNI/POLRI (2000b) fractions. They also questioned the executive’s commitment to the people since the allocation for both the education and agriculture sectors declined by 50 per cent each. Moreover, the DPR opposed the executive’s plan to allocate almost half of the routine spending or one-third of total spending to debt interest payment since it was against the fairness principle. The maximum allowable allocation was 20 per cent of the budget (PDIP 2000b:4). Members of the DPR even expressed their opposition to the executive’s plan to increase fuel and electricity prices which was planned to be implemented in April 2000.

This criticism was also expressed when debating 2001 budget. The executive’s proposal to reduce government debt by increasing the budget allocation to 5.5 per cent of GDP or 39 per cent of the total expenditure for debt payment was rejected by the DPR as it was far above development expenditure which accounted for only 2.4 per cent of GDP or 13 per

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76 The government had spent about Rp 650 trillion to cover recapitulation costs and had to pay around Rp 60 trillion annually from the state budget for the interest, subject to the interest rate (Subianto 2004:114-32).
77 During the pre-crisis years, the government used to spend at least 6 per cent of GDP for capital or development expenditure. This figure had reduced to only around 3 per cent of GDP after the 1997 economic crisis (Abimanyu 2003:276-7).
78 There was and is strong sentiment among legislators regarding government debt. Some legislators asked the government to abolish this debt which was incurred during the Suharto era on the grounds of ‘odious debt’. For them, it is against the fairness principle that the current government had to pay for the wrongdoings of the previous government and the people had to bear the burden caused by Suharto’s New Order regime.
79 World Bank (2001b:2) reports that government debt service payment accounted for one third of government revenue in 2000 and around 40 per cent in 2001.
cent of the total expenditure. The latter was even far lower than routine expenditure (87 per cent). The DPR was also against the plan to cut the fuel subsidy.

In response to these criticisms, compromises were reached between the executive and the DPR at the cost of reform prospects. Except for debt amortization which was tied to other multilateral agreements such as the CGI,\textsuperscript{80} the World Bank, the IMF and the Paris Club,\textsuperscript{81} the executive had to balance all posts in response to DPR’s criticism making resource targeting an absolutely difficult job. For example, development expenditure was increased in both the amount and percentage relative to routine expenditure. So did personnel expenses. Initially the executive proposed only a 20 per cent of base wage increase. During the debate, the DPR instead decided to increase it by 30 per cent, divided into two stages: 15 per cent in April 2000 and another 15 per cent in October the same year.\textsuperscript{82} These affected government plans to accomplish fiscal sustainability by cutting the budget deficit and reducing the government-debt-to-GDP ratio unless the executive could increase budget revenue significantly. In the 2000 budget, the executive proposed a deficit of -5.0 per cent of GDP. Taking DPR’s criticism into account, it then reduced the target to -4.8 per cent of GDP. For the 2001 annual budget, while the executive proposed budget deficit of -3.7 per cent of GDP, the DPR instead approved a lower deficit of -3.5 per cent of GDP. Whether the government could accomplish this target was of great concern since it also depended on the success in related reform measures. With the slow progress of reform in both revenue and expenditure aspects, especially tax and subsidy reform, such a target could only be a distant dream. As proven later, the government could bring the deficit down to a promising level of -1.6 per cent of GDP in 2000, thanks to the increasing oil prices in international market. However, this again increased to -2.8 per cent of GDP in the 2001 fiscal year (Ministry of Finance 2002; Ministry of Finance 2003). Though it was below the set target of -3.5 per cent of GDP, this clearly raised concerns about the uncertainty of

\textsuperscript{80} CGI (Consultative Group on Indonesia) was established in 1992. It is a consortium of 30 donor countries and multilateral institutions providing loans to Indonesia, set up by the Indonesian government and the World Bank. Before that, its role was played by the Inter-Governmental Group on Indonesia (IGGI) which provided multilateral development aid for Indonesia since 1967. President Suharto dismissed it following conflict with one of its members, the Netherlands, regarding massacre in East Timor in 1991.

\textsuperscript{81} The Paris Club is an informal group of financial officials from 19 of the world’s richest countries, which provides financial services such as debt restructuring, debt relief, and debt cancellation to indebted countries and their creditors. Debtors are often recommended by the International Monetary Fund after alternative solutions have failed (www.wikipedia.com).

\textsuperscript{82} See Letter of Intent, 17 May 2000.
macroeconomic management. The effect of good budget policy and management was far from expected.

Meanwhile, government debt to GDP ratio had declined significantly, thanks to the increase of GDP growth and the pressure from donor institutions. It had reduced from 101.2 per cent in 1999 to 98 per cent in 2000 and 86 per cent in 2001. This achievement is in line with PROPENAS target. However, this was due more to nominal GDP increase and Rupiah appreciation right on the due date than good policy management (World Bank 2002b:5-6). There was almost no contribution from debt policy measures since the DPR was against the executive's proposal to allocate a significant amount for debt amortization. The DPR even requested the executive to negotiate debt rescheduling which would burden the next administrations.

What I can conclude from the achievement in revenue and spending reform initiatives is the prominence of political compromise in the budget making process though this meant a further delay of reform targets. The whole process indicates the inability of the executive to cope with DPR opposition. Wahid's low executive strength prevented the executive from dealing with this opposition and it principally followed what the DPR wanted.

Pushing policy reform in financing the budget deficit was no less difficult. Government had maintained its commitment to rely on domestic sources. Of the main domestic sources, asset recovery and privatization of state-owned enterprises were of special concern. As discussed in the previous section, asset recovery progressed only slowly. Most of the problems lied on law enforcement and IBRA was trapped within the corrupt Indonesian legal system. DPR opposition to IBRA's asset recovery targets had complicated the picture even more (Ramstetter 2000:18; World Bank 2001a). The DPR involved actively in every stage of the process, making IBRA highly politicized and less independent. For example, to recover government's recapitulation cost in BCA, IBRA planned to sell some of its properties. Included among these were 25 palm oil plantations in Sumatera, Kalimantan and Sulawesi. After a long bidding war, IBRA finally approved selling them to Guthrie Berhad Ltd, a Malaysian company. However, along with local people, business association and NGOs, the DPR opposed this plan and requested IBRA to review its decision (DPR RI 2001:256; Kompas 25/01/2001). Its reason was due to legal uncertainty over land
ownership and the concern that Malaysia would monopolize palm oil market. Opposition such as this not only compromised the budget target but, more importantly, rendered the business climate very unfavorable for potential investors as there was no protection over property rights.

In response to this opposition, IBRA sometimes had to review decisions it had already made. Since the survival of the executive depended on the DPR, it had to really consider what the DPR requested and this significantly explained its low performance. Together with privatization, this compromised the government's targets for accomplishing fiscal sustainability.

3.3.3 Privatization

In privatization area, no single state-owned enterprise was privatized during the Wahid administration despite its repeatedly-declared plan to push this agenda. The main explanation for this poor achievement was not the opposition from the DPR as some might argue (Hendrawan 2001; Bari 2005; Prasetiantono 2005) but rather the president's inability to face that opposition. Since privatization is a politically sensitive agenda involving both winners and losers, it needs a strong hand. The losers come mainly from political elites who in the past enjoyed privileged benefit. The fact that potential winners could be foreigners makes these initiatives even more difficult. The adoption of a family-based economic system as stipulated in the constitution makes the issue even more complicated and the DPR uses this to articulate its populist and nationalist policy preference. Wahid had no political resource to push this agenda forward especially, the constitutional protection over security of tenure and adequate partisan support. His already vulnerable position could be in danger if he insisted on pushing his reform agenda amidst DPR's opposition. Even if he was ready to take such a risk, he could not push the privatization agenda without DPR approval. DPR opposition almost always blocked this agenda.

The main reason for DPR's opposition was that since the state-owned enterprises touch the public interest as stipulated in Article 33 of the Constitution, it must supervise and approve each privatization process on a case-by-case basis. Unfortunately, the parties had no clear
platform on this issue, except GOLKAR which required government ownership of a minimum 50 per cent in those enterprises (Hendrawan 2001:16). This made it extremely difficult for the executive to push the privatization agenda forward. Moreover, Wahid’s confrontation with the DPR had only provided additional justification for the DPR to frustrate the executive by blocking its reform initiatives and becoming involved so deeply in the executive’s business (Mulyani 2001). Though the DPR had approved the privatization target through the budget bill, it always blocked the executive’s plan to execute it. For every single enterprise to be privatized, the executive had to firstly get “principal approval” from the DPR and then discuss it in detail, case by case.\footnote[83]{Known as “\textit{ijin prinsip},” this rule simply means that the executive must firstly get general approval from the DPR on the whole plan of privatization. After that, it has to discuss the plan in detail, case by case. Among the issues to be approved are how much of government share shall be sold, who is the potential buyer, the proper time to sell it, and even the price of share. Due to this rigid rule and combined with low executive strength, the DPR had more opportunities to dictate to the executive so that privatization progressed very slowly under Wahid administration.} For this purpose, the DPR even established a special committee for each case. The committee had the responsibility not only to oversee the process but also to become involved in all the stages including giving approval to the winning investor. The practice was legalized through the DPR’s internal mechanism and the executive had to comply with it though the technicalities of privatization were still under the executive’s domain. Due to this very practice, the executive sometimes had to reverse decisions it had already made with foreign investors such as in the case of Cemex (discussed below).

In trying to push the privatization agenda, the first challenge for the Wahid administration was the divestment of BCA during the last quarter of 1999 and PDFCI and Tiara in early 2000.\footnote[84]{This was based on the agreement made by the Habibie administration with the IMF before he left office.} Then, on 20 January 2000, Wahid signed the government’s first Letter of Intent with the IMF. One of the most important points in this document was the government’s plan to raise domestic funds to finance the budget deficit by privatizing some of the SOEs. The focus was on enterprises operating in competitive markets and where there was no compelling need for government ownership or public service obligation. PT Telkom and PT Indosat – both telecommunication enterprises – were included in the plan. This was expected to raise as much as Rp 5.9 trillion for the 2000 fiscal year (Kompas 24 January 2000). There was no further specification as to the extent to which these enterprises would be privatized. This was again changed by the signing of another Letter of Intent in May
2000 when the government increased the target to Rp 6.5 trillion and Telkom and Indosat were again the main targets.

After that, in February 2001, the executive again planned to privatize as many as 16 SOEs from May to December 2001 as shown in Table 3.6. This was to raise extra resources of at least Rp 6.5 trillion for the 2001 budget. This would come from, among other, the privatization of 10 per cent of PT Indosat (Rp 1.2 trillion), 10 per cent of PT Telkom (Rp 3 trillion), and 20 per cent of PT Pupuk Kaltim (Rp 1.4 trillion) and from other SOEs to cover the rest (Kompas 20 April 2001). Whether government could meet its target was a big question and the following discussion will discuss its achievement.

Table 3.6 List of state-owned enterprises to be privatized in 2001

<table>
<thead>
<tr>
<th>State enterprises</th>
<th>Field of business</th>
<th>Divested (%)</th>
<th>Method*</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sarinah</td>
<td>Department store</td>
<td>up to 100</td>
<td>SS</td>
</tr>
<tr>
<td>Bank Mandiri</td>
<td>Commercial bank</td>
<td>49</td>
<td>IPO</td>
</tr>
<tr>
<td>Krakatau Steel</td>
<td>Steel</td>
<td>49</td>
<td>SS/IPO</td>
</tr>
<tr>
<td>Angkasa Pura II</td>
<td>Airport services</td>
<td>49</td>
<td>SS</td>
</tr>
<tr>
<td>Pupuk Kaltim</td>
<td>Fertilizer</td>
<td>10-49</td>
<td>SS/IPO</td>
</tr>
<tr>
<td>Indofarmera</td>
<td>Pharmaceutical</td>
<td>10-49</td>
<td>IPO</td>
</tr>
<tr>
<td>Wisma Nusantara Internasional</td>
<td>Property</td>
<td>up to 42</td>
<td>SS</td>
</tr>
<tr>
<td>Kimia Farma</td>
<td>Pharmaceutical</td>
<td>10-35</td>
<td>IPO/SS</td>
</tr>
<tr>
<td>Perkebunan Nusantara III</td>
<td>Plantation</td>
<td>10-35</td>
<td>IPO/SS</td>
</tr>
<tr>
<td>Tambang Batu Bara Bukit</td>
<td>Coal mining</td>
<td>10-35</td>
<td>IPO/SS</td>
</tr>
<tr>
<td>Asam</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Succofindo</td>
<td>Import procedure surveyor</td>
<td>15-20</td>
<td>SS</td>
</tr>
<tr>
<td>Socfindo</td>
<td>Agroindustry</td>
<td>..</td>
<td>..</td>
</tr>
<tr>
<td>Indocement Tunggal Perkasa</td>
<td>Cement</td>
<td>..</td>
<td>..</td>
</tr>
<tr>
<td>Semen Gresik</td>
<td>Cement</td>
<td>..</td>
<td>..</td>
</tr>
<tr>
<td>Telkom</td>
<td>Telecommunication</td>
<td>14</td>
<td>RES</td>
</tr>
<tr>
<td>Indosat</td>
<td>Satellite &amp; communication</td>
<td>14</td>
<td>RES</td>
</tr>
</tbody>
</table>

* SS = Strategic Sales; IPO = Initial Public Offering; RES = Restructuring


The divestment of BCA found no easy way. By the end of 1999, the government’s deadline to complete the sale of IBRA’s stake in this company had passed. Later, the DPR decided that IBRA could only sell its shares in BCA for a maximum of 30 per cent of its shares at a minimum price of Rp 1,350/share (DPR RI 2000:214). It was against the “fire sale”
approach when the share value is low. When IBRA finally launched the public offering in May 2000, the market response was so low that it could sell only 22.5 per cent of the shares. Its contribution to the 2000 budget was far from expected since it could only raise Rp 900 billion out of the planned Rp 3 trillion or less than 30 per cent of the target (McLeod 2000:24). Many observers criticized the government for its slow decision in this case. They argued that postponing divestment would not guarantee a better price or greater revenue but only raised more doubts in the market, especially among foreign investors interested in such businesses. Moreover, in line with the experience from other countries, the longer the government holds such assets, the greater the depreciation of asset value and the larger the opportunity cost for the government will be (Bird 2001:58). As if to ignore such concerns, the DPR said it would oppose the plan if the divestment to new owners proceeded without paying all recapitulation costs the government had spent.

In 2001, the executive again planned to divest BCA by selling 40 per cent of its share: 30 per cent through strategic sales and 10 per cent through public offering. Both had received a good response from the domestic and international market. However, the DPR opposed the plan on the grounds that it needed more time to establish a more comprehensive scheme especially regarding the timing and pricing (Tempointeraktif 06 February 2001). This also applied to Bank Niaga. When Wahid left the office, this plan was still underway (Tempo 08 July 2001).

In the meantime, the privatization of PT Telkom and PT Indosat encountered the same opposition. The DPR agreed with the executive that these two enterprises had to be privatized by opening more room for private sector involvement. However, given the internal condition of these enterprises at that time, the DPR only gave the green light for the executive to restructure them (DPR RI 2001:261-2). Given this opposition, the executive could not move forward though it had declared these two enterprises to be the main targets of privatization in 2000 to at least cover the budget deficit. Its attempts to push the privatization of these enterprises again in 2001 only embarrassed itself since the DPR again opposed the plan.

With the failure of the PT Telkom and PT Indosat privatization and given the targets to mobilize more domestic resources to cover budget deficit, the executive then tried to
privatize other state enterprises. One such target was PT Perkebunan. However, when the executive was about to privatize PT Perkebunan Nusantara III and PT Perkebunan Nusantara IV in June 2000, the DPR again showed its opposition. The reason was that these enterprises had to accomplish internal improvement before being sold to strategic partners. This was to avoid the image of a fire sale simply to mobilize extra resources for the national budget. Such improvements were important to boost the market value of the enterprise, so it argued. Moreover, they needed to wait for favorable market conditions so that the shares could be sold at a higher price (DPR RI 2000:132; Kompas 13 June 2000). However, when the executive submitted a report showing improved performance of PT Perkebunan Nasional III in September 2000, the DPR held to its opposition. It argued that the privatization of this company could only be allowed if undertaken according to the law, transparently, free from corruption, collusion and nepotism, and in line with a business development plan, and if it would improve the welfare of the local people (DPR RI 2000:230). Considering this opposition, the executive finally decided to postpone the plan. This is a clear example of how the DPR compromised the executive’s targets by using exceptionally inconsistent arguments. However, given Wahid’s weak position, the executive could only follow it.

With the failure to privatize PT Perkebunan, the executive then turned its target to fertilizer enterprises. As for other enterprises, its plan also found opposition from the DPR. One case in point was PT Pupuk Kaltim. Through its Commission IX, the DPR strongly opposed the plan to privatize this enterprise. It argued that this enterprise was under no circumstances to be privatized given its improved financial performance (DPR RI 2000:134). This position changed slightly in 2001 when the DPR approved the plan to privatize it. However, it could only proceed under three conditions: (1) the government would still maintain a majority share ownership; (2) privatization would produce a high sale price; and (3) fertilizer could

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85 There were 14 PT Perkebunan Nasional operating throughout Indonesia in different plantation businesses such as rubber, tea, palm, and coffee.

86 The privatization of PT Perkebunan Nasional faced another problem. Wahid once said that 40 per cent of its land belongs to the local people and therefore had to be returned to them. This provoked waves of reclaim and occupation by local people even when the government had sold the land to investors. This led to the problem of security and legality of ownership. Under such circumstances, potential buyers would not touch it.

87 This was a confusing argument since every step the executive took had actually referred to the law. It was even unclear to the executive which law the DPR asked it to comply with and that it had broken.
be secured for domestic needs (DPR RI 2001:268). Given these tight conditions, the executive again had to give up its plan.

Another case was the privatization of PT Semen Gresik. In 1998, the government had reached an agreement with Cemex, a Mexican cement company, over the acquisition of extra shares in Semen Gresik. The execution of this agreement faced opposition from Semen Gresik's two subsidiaries, PT Semen Tonasa and PT Semen Padang, each located in South Sulawesi and West Sumatra. To respond to regional opposition, the DPR opposed the executive's put-option proposal since it was against Article 33 of the Indonesian constitution. It could only approve the proposal if the executive used a spin-off strategy to Semen Gresik's two subsidiaries (DPR RI 2002:320). Due to this opposition, Cemex reacted by threatening to move out of Indonesia since the government had broken its initial agreement. This case again confirms a strong nationalist sentiment in relation to foreign ownership, making privatization more and more uncertain in the future (Pengestu and Goeltom 2000:164; Siregar 2001:296). In the end, this had created an inimical investment climate resulting in the ineffectiveness of both the public offering and strategic sales as well as causing poor investment performance as a whole.

A similar case where nationalist sentiment was manipulated by the DPR to block privatization was PT Angkasa Pura II. This enterprise provides services for Jakarta Soekarno-Hatta International Airport. The argument for the DPR was that this enterprise performed well financially. Under these conditions, there was no acceptable reason for privatization (Angkasa 27 February 2001). Moreover, as its service was related to internal security concerns, the DPR rejected the plan. This opposition again prevented the executive from moving forward with its reform agenda. Given the president's weak position, the executive could not push this agenda any further.

What I can conclude from the case of privatization in general is the inability of the Wahid administration to push forward its reform agenda despite its strong commitment to do so. Above any other explanation, it was Wahid's low executive strength which was the primary

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88 Cemex finally sold its hares in PT Semen Gresik to PT Rajawali Corporation in July 2006 since it only had a minor share in that company. It brought its conflict with the Indonesian government to the International Center for Settlement of Investment Disputes (ICSID) in Washington but then withdrew it later (Tempointeraktif 25 July 2006).
reason for this. Without constitutional protection over his tenure and the lack of partisan support in the DPR, his team could do nothing but accommodate to what the DPR wanted. When the latter showed its strong opposition, the executive had to give up its agenda. Had Wahid been in a safe position and had sufficient partisan support, he would have been able to face the DPR opposition and push this agenda, given the limited choices he had at that time.

3.3.4 Investment policy reform

This section will discuss investment policy reform under Wahid. Of special concern is the energy sector, and the Wahid administration prioritized the pushing of reform of the management of national oil and gas and electricity. However, Wahid failed to achieve this aim before he left office. The reason for this is clear. Reforming these two areas means disturbing many established interests, especially in PERTAMINA and PLN and their cronies. As in other cases, the DPR also posed strong opposition using anti-market and nationalist sentiments and citing the protection of the people as the reason, as mandated by Article 33 of the 1945 Constitution. Considering their nature, reform in these areas would have required strong political capital and the executive’s freedom from political opposition would also be especially important. Wahid had no such capital because of the absence of protection over security of tenure and consolidated partisan support. Therefore, the executive had to give up this proposal despite a long process of preparation from 1998 onwards (Media Transparansi 07 April 1999).

The discussion so far shows how powerless the executive was to cope with DPR’s opposition in pushing economic policy reform, especially where the DPR held a different interest or priority. Wahid’s vulnerable position left him with limited choice but to follow what the DPR wanted. Moreover, realizing its stronger position, the DPR showed strong opposition even to jointly-approved targets and was actively involved in policy areas under the domain of the executive such as privatization. This was against the principle that it is the executive which is responsible for executing privatization since the president and the DPR have jointly approved the set revenue targets from privatization to financing budget deficit. Wahid’s hostile confrontation with the DPR triggered the latter to become more
deeply involved in managing the economy despite its lack of expertise. Worse than that, the DPR manipulated populist and nationalist sentiments to block the executive's reform initiatives as in the case of privatization and energy sector reform. Most of the already announced reform targets were unmet, pushing government credibility down in the eyes of the business community. The IMF and other donor agencies such as the World Bank and the Asian Development Bank even felt the need to postpone their financial support for economic recovery until the government improved its performance.89

3.4 Fuel subsidy reform

This section presents a case study of fuel subsidy reform. The case is important for two reasons. First, it traces in detail the effect of executive strength on economic policy reform and second, it provides a common policy challenge that can be compared across administrations.

With low executive strength in both constitutional and partisan aspects, Wahid bore the burden of initiating the fuel subsidy reform. As in the previous section, my argument is that his vulnerability to dismissal by parliament and the lack of legislative support prevented him from pushing reform in this politically sensitive area. At best, he could not pursue fuel subsidy reform unless the DPR approved it. As the latter took a populist stance at the cost of good policy in this even more sensitive issue, the progress of reform in this area was extremely limited.

The decision to reform the fuel subsidy is made annually through the annual budget deliberation between the executive and the DPR. The executive is usually represented by the Ministry of Mining and Energy,90 the Ministry of Finance, and supported by the Ministry of National Development Planning (Bappenas), the Bureau of Statistics, and the Central Bank. Once it is agreed, the president will proceed by issuing a Presidential

89 The last Letter of Intent was sent to the IMF on September 2000. After that, for around one year, the IMF postponed all its financial commitment due to political uncertainty. Other international donors took this as a strong signal of economic uncertainty and followed the IMF's move.
90 In August 2000, the government changed the name of this ministry to the Ministry of Energy and Mineral Resources. This is still the case.
Decision (Keputusan Presiden or Keppres). This means that the Keppres must refer to the Annual Budget Bill (UU APBN), ignorance of which will provoke conflict with the DPR.

When proposing the draft of the 2000 budget, the executive presented several key points regarding the subsidy (Ministry of Finance 2000b). Firstly, the fuel subsidy together with other subsidies needed at least Rp 26.7 trillion (or 2.9 per cent GDP). From this amount, 18.3 trillion or 68.5 per cent was for fuel subsidy (or about 1.98 per cent of GDP) and the remainder was for electricity, food, and credit interest subsidies. Secondly, while this allocation burdened the state budget, the subsidy was still necessary to trim down the people’s economic burden in coping with the impacts of the economic crisis. Thirdly, along with this measure, government would restructure PERTAMINA to overcome inefficiency in fuel provision which caused increasing subsidy allocation. Fourthly, the executive planned to increase fuel prices in line with the rise in oil prices in the international market which had caused a rise in fuel subsidy allocation. This increase would be different from one type of fuel to another considering the different purchasing power of the people. In addition, government would still provide a targeted subsidy for poor and vulnerable people.

In its proposal, the executive also argued that given budget constraints, continuing the fuel subsidy potentially distorted the economy by triggering negative effects such as unreal production costs, energy wasting,91 and fewer incentives for energy conservation and diversification. Moreover, the fuel subsidy had triggered widespread smuggling to neighboring countries due to the wide price gap (Ministry of Finance 2000b:266).92

In consideration of these factors, the president then proposed to allocate Rp 18.3 trillion to the fuel subsidy while at the same time increasing the fuel price by 19 per cent on average.

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91 The low fuel price has triggered wasteful energy consumption and this is measured by both energy elasticity and energy intensity. Indonesia’s energy elasticity lay somewhere between 1.04 and 1.35 during the period of 1985-2000. This is more than double that in developed countries which reached 0.55 to 0.65 during the same period. While in terms of energy intensity, it is four times higher than Japan (400:100), twice as high as OECD countries (400:200), and still higher than North America (300) and Thailand (350). This is in contrast with fuel oil reserve which is predicted to vanish in the next ten years (Ariati 2004; Elyza and Hulaiyah 2005).

92 For comparison, the petrol price was only US$ 0.124 compared to US$ 0.318 in Malaysia, US$ 0.872 in Singapore, US$ 0.403 in Thailand, US$ 0.279 in the Philippine, and US$ 0.307 in Brunei. Meanwhile, diesel fuel price is only US$ 0.055 compared to US$ 0.185 in Malaysia, US$ 0.387 in Singapore, US$ 0.350 in Thailand, US$ 0.291 in the Philippine, and US$ 0.181 in Brunei (Tempo 01 October 2001; OPEC 2005).
These two related measures were part of the executive’s effort to fight the deficit and enhance fiscal sustainability. This effort was actually critical given that the amount spent on the fuel subsidy in the 1999/2000 annual budget had exceeded its initial allocation by as much as 300 per cent even before the end of the fiscal year. This was due to the rise in oil prices in international market and the depreciation of the Rupiah exchange rate at the same time (Ministry of Finance 2000b:198).

Responding to this proposal, the DPR’s Budget Committee requested the executive to really carefully calculate the price increase so as not to place an additional burden on the people. The PDIP fraction questioned the readiness of the executive to target the subsidy to the eligible group. While the subsidy had increased by 83 per cent above the previous annual budget (1999/2000) or around 144 per cent over a period of nine months (April-December 2000), for this fraction, subsidy targeting was still a big concern as around 40 per cent of the funds went to the wrong target (PDIP 2000b). Similarly, the GOLKAR fraction emphasized that the subsidy had to be based on the principle of fairness: only the poor, vulnerable and low income people were eligible and not the better-off people. It requested the executive to establish a new scheme. Moreover, unless the executive was able to tackle corruption, collusion and inefficiency in production, transportation and distribution process in PERTAMINA as well as establishing a new subsidy policy scheme, GOLKAR would reject any plan to increase the fuel price (GOLKAR 2000b).

The recommendation for the executive to establish a new scheme for the fuel subsidy also came from other fractions, such as Reformasi (2000b), TNI/POLRI (2000b), KKI (2000b), PKB (2000b), and PDKB (2000b). The underlying reason was also similar. While the fuel subsidy touched the majority of the people, the current subsidy scheme was so poorly designed that those not eligible also enjoyed the benefits. Continuing this scheme would not only be ineffective and against the principle of fairness but would also simply waste public money.

The other leading fraction, PPP, was no less critical of the plan. For PPP, this measure contradicted the very economic situation the people were facing. Considering that the people’s purchasing power was decreasing due to the economic crisis, increasing the fuel
price would only put an additional burden to them. Therefore, the executive was requested to revoke its plan (PPP 2000b).

Besides all these criticisms, the DPR had set up a special task force to assess the feasibility of an electricity and fuel price increase.\(^{93}\) Among its recommendation were: (1) to selectively and gradually cut the subsidy based on economic activity, social status, and geographical location; (2) to review the current subsidy scheme; (3) to provide direct cash transfers to the eligible; and (4) to endorse energy conservation and diversification (DPR RI 2000:202).

Taking the DPR’s feedback into account, the executive finally agreed to increase the fuel subsidy allocation to Rp 22.5 trillion. The increase placed serious pressure on spending and, therefore, on the budget deficit. Consequently, a price increase had to be applied as well. However, it had to give up its initial plan to increase the fuel price by 19 per cent on average. This plan required DPR approval and the Commission VIII and IX had to be consulted.\(^{94}\) Realizing the country’s precarious financial situation, the DPR did not oppose the plan. However, considering the people’s social and economic conditions, it only allowed the executive to increase the fuel price by no more than 10 per cent (and 20 per cent for the electricity price). A compromise was finally reached to increase the fuel price by 12 per cent on average. In addition, the DPR requested the president to undertake a thorough investigation of PERTAMINA’s corruption indications. It also demanded the Ministry of Mining and Energy ensure that the fuel price would remain low for public transportation and to protect low-income families. The president and the Minister of Mining and Energy responded to such requests by announcing that 17 million poor households would receive special coupons to buy fuel products at existing price and public transport would receive a special subsidy from the government. For these purposes, the president planned to allocate Rp 1.3 trillion by distributing fuel coupons. Later, the president cancelled the plan given the complexity of its delivery system and instead provided direct cash transfer to the poor and to public transport companies (Ministry of Energy and Mineral Resources 2001:4; van Dijk 2001:516-7).

\(^{93}\) This task force was named the Assessment Team for Electricity and Fuel Price Increase (or Tim Pengkajian Kenaikan Tarif Dasar Listrik (TDL) dan BBM).

\(^{94}\) The Committee VIII dealt with the science, technology and environmental affairs while the Committee IX dealt with the finance and development planning affairs.
As time passed, economic conditions changed. In early 2000, the president maintained that reducing the fuel subsidy or increasing the fuel price was unavoidable given the current economic conditions and the conditions of the IMF package (Kompas 22 February 2000). On the contrary, through the Committee VIII, the DPR requested the executive to cancel the plan. Its reasons were its likely contagious effect on the whole economy and the people on one side and the executive’s indisposition to tackle this effect and to deliver cash compensation on the other side. This was against its own initial agreement made through budget deliberation with the executive (Kompas 31 March 2000). Wahid finally announced on 31 March 2000 that he had canceled the plan to increase the fuel price. This is substantially explained by his inability to cope with opposition from the DPR. At that time, conflict between the president and the DPR had just started, triggered by the dismissal of some ministers based on unclear allegations. Therefore, his already vulnerable position would be at risk if he insisted on the plan. In addition, people’s possible anarchic reactions could not be underestimated as had happened to Suharto (Ministry of Energy and Mineral Resources 2001:2). Worse still, such an unpopular decision could be engineered by the parliament to remove him from office.

Up to this point the DPR’s inconsistencies in the policy-making arena could be seen. It even betrayed decisions it had itself approved. To make things worse, the executive could do nothing but to follow it. Should Wahid have been in a secure enough position, he would have been able to push this agenda since it had already been approved by the DPR even when the latter withdrew its approval. What happened was the political game played by the DPR to frustrate the president on populist grounds especially when there was a strong indication that the president was trying to consolidate his power and keep his distance from the political parties. This should have provided a strong enough message to Wahid to be more careful in taking his next steps if he wanted to maintain DPR’s support.

The delay of the price increase in March was the beginning of the problems. The Rupiah had depreciated relative to the US Dollar from Rp 7,100/US$ in December 1999 to almost Rp 8,000/US$ in April 2000. To make things worse, international oil prices had also

95 In a very diplomatic way, the executive argued that it “full implementation has been delayed in order to better prepare the people for this increase as well as to finalize measures to protect the poor” (Letter of Intent 17 May 2000). This only sent negative signal to investors of how unpredictable policy direction was in Indonesia.
increased at the same time. Both changes caused the fuel subsidy allocation to increase quite significantly and the government had to take immediate action. Further delay could force the deficit to increase significantly unless the government cut its expenditure. Increasing the fuel subsidy allocation was simply unrealistic given the current budget constraint. However, the president could only make new decisions on the fuel price increase after he presented the semester-one budget performance and this required the approval of the DPR. By this time, the fuel subsidy had far exceeded the allocated amount since the fuel price was kept at the current rate.

After a long delay, Wahid finally announced the fuel price increase on 1 October 2000 through Presidential Decision No.135/2000. This time, due to the Rupiah’s depreciation and increased international oil price, fuel subsidy allocation had increased from Rp 22.5 trillion to Rp 44 trillion. The budget deficit and fiscal sustainability were under real threat. Despite this huge increase, the DPR only approved a price increase for all fuel products by 12 per cent on average. This could only reduce the fuel subsidy allocation to Rp 43.2 trillion. The freeing up fund, Rp 800 million, was then allocated to compensation programs consisting of cash transfers, revolving funds and infrastructure development which had to be accomplished within three months (October-December 2000). Of these three components, the cash transfer was the most complicated one since the government had to distribute Rp 10,000 to 6,666,667 poor families (or 47 per cent of total poor households) each month in 321 districts throughout the country (Rahayu et al. 2001:iv).

Despite the miniscule increase, this time the executive succeeded in convincing the DPR to increase the fuel price. This was also a critical moment to test the extent of public reaction which was proven still under control. Given the doubling of the fuel subsidy allocation, the executive should have at least doubled the fuel price to ease the budget constraint. However, the DPR’s opposition prevented such a significant change, which the president could only accept. Thanks to the oil windfall, the budget deficit could be brought down to -1.6 per cent of GDP, much lower than the target set in annual budget of -4.7 per cent of GDP. However, the fuel subsidy allocation had increased significantly. Even government attempts to revise the annual budget by allocating Rp 51 trillion were simply not enough to face the pressure from the Rupiah depreciation and the international oil price hike. By the end of 2000, the fuel subsidy allocation had finally increased to as much as Rp 62.7 trillion,
more than three times higher than the initial allocation. The budget deficit would have reached more than -4.7 per cent of GDP if there had been no adjustment at the end of 2000 fiscal year. The fuel subsidy alone reached 5.4 per cent of GDP, making it difficult for the government to cut overall subsidies in that year by only 5.5 per cent of GDP as set in the PROPENAS.

Learning from the experience of 2000, the executive planned to continue further changes in 2001. The process of policy-making for the fuel subsidy reform in 2001 and its institutional arrangements were still the same. It proposed Rp 36.4 trillion or 2.6 per cent of GDP for the fuel subsidy allocation, higher than the allocation for development expenditure of only 2.4 per cent of GDP. This contributed to -3.7 per cent of GDP of the deficit. Therefore, the executive planned to undertake further reform by increasing the fuel price by at least 20 per cent on average (Ministry of Finance 2000a).

Responding to the executive’s budget draft, the DPR again mounted its populist-based opposition. The Budget Committee posited that while a subsidy reduction was a must, it also had to ensure fairness for the people. However, it also brought to mind that one had to be careful not to hastily assume that the fuel subsidy actually went to the poor. It mostly benefited the middle class and better-off people who had much better economic capacity to afford the higher fuel prices. The poor households only consumed 20 per cent of the kerosene while the rest went to the industrial sector. The Budget Committee also requested the executive to establish a better strategy to reduce the subsidy with a more systematic awareness raising – or socialization as it is known in Indonesia – approach so that the people could understand, accept and finally support this measure. The committee also requested the executive to develop an appropriate measure to cope with the unexpected impacts of the price increase. It then recommended the executive continue providing the fuel subsidy, not through price subsidy but through direct cash transfer to those eligible.

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96 This was especially related to the huge allocation for government debt amortization. The government had to allocate 40 to 60 per cent of routine spending to debt amortization. This triggered negative reaction from all legislators when discussing annual budget. However, it had no alternative but to pay it. Otherwise, it would only worsen business climate and donor agencies would stop providing financial support which Indonesia desperately needed to overcome economic crisis.

97 In fact, 40 per cent of lowest income households consumed only 18 per cent of fuel oil and 25 per cent of kerosene. The rest was consumed by middle and top income households with 20 per cent of highest income group consumed 43 per cent of fuel oil and 31 per cent of kerosene (Ministry of National Development Planning 2005a).
The executive also needed to supervise and control fuel distribution to avoid smuggling (Budget Committee 2000a).

This was just an invitation for all the fractions in the DPR to mount their opposition. First, the TNI/POLRI fraction criticized the executive for its inability to set a priority. This was because the fuel subsidy allocation was higher than other subsidies which contradicted government priorities and the economic recovery programs. The TNI/POLRI also requested the executive to revise the existing policy scheme. Should the executive insist on the plan to increase fuel price, it had to prevent disproportional price rises in other products, conduct systematic socialization for the people to understand and accept the measure, and keep up subsidies for certain segments in society (TNI/POLRI 2000a).

The PBB fraction also raised a similar point. For this fraction, spending on the subsidy as proposed in the draft budget was too high since it almost equaled the revenue derived from the oil and gas sectors and was even higher than the spending for government personnel (PBB 2000a). Similarly, the KKI fraction reminded the executive to reduce the fuel subsidy carefully and it would only approve the plan if the executive could effectively control the social and political costs. More importantly, such a measure had to be able to improve the people’s welfare, not compromise it. The KKI fraction also requested that funds saved be reallocated to development programs such as improving access to education through mandatory but free nine-year-education (from primary school to high school), subsidizing transportation to stabilize transportation costs, reducing poverty, creating employment, boosting the development of certain regions lagging behind others, and supporting the implementation of special autonomy in West Papua and Aceh (KKI 2000a).

The PDKB fraction took a similar position. As any subsidy reduction was always accompanied by social protest, demonstration and riots, it suggested the executive (1) establish a special campaign team to explain and socialize the idea of fuel subsidy elimination to the people and to prevent certain groups from manipulating the situation; (2) use the fund from the subsidy for rural development programs; and (3) take strict action to punish the provocateurs and riot triggers who manipulated the conditions when the fuel price was increased. The executive also had to relentlessly persuade the people that the existing fuel subsidy scheme only benefited groups other than the poor people (PDKB
These concerns were also expressed by the Reformasi fraction which required government to set a well-targeted subsidy strategy to avoid social unrest (Reformasi 2000a).

In line with these criticisms, the GOLKAR fraction emphasized its support to continue providing the fuel subsidy. For GOLKAR, this was important to maintain fuel price stability which affected the price of other products. This would also help maintain the inflation rate at a reasonable level. However, it pushed the government to take any necessary action to accomplish efficiency and effectiveness in oil management and use for the sake of national energy sustainability (GOLKAR 2000a). The PDU fraction also shared this criticism. While realizing the burden of the subsidy on the national budget, it supported the continuation of fuel subsidy provision. It called on the executive to work harder to generate more revenue from oil and gas income, privatization, and asset recovery and to push down expenditure in less productive and urgent sectors outside the spending for government officers and debt payment (PDU 2000a).

To more articulate the previous criticisms, the PPP fraction argued that the large amount of allocation to the subsidy marked an inefficient economic resource allocation which in the long run could put the national economy into deeper crisis. It requested the executive to examine more deeply whether the subsidy could be gradually eliminated and reallocated to other important sectors such as free health services and mandatory nine-year-education. The executive was also exhorted to ensure that the subsidy went to the eligible and would combat smuggling (PPP 2000a).

Unlike other fractions, the PDIP fraction stated that it could understand the executive's proposal to gradually reduce the fuel subsidy. For PDIP, this was an important measure to conserve energy resources and make energy use more efficient and sustainable. It criticized the current subsidy scheme as being against market principles and requested the executive to reallocate the subsidy to empower the poor. However, it could only approve removal of the subsidy if the executive could control inflation and social unrest as well as establish more concrete steps to set up and employ a compensation fund to improve people's welfare, create employment opportunities, and help the poor and destitute children (PDIP 2000a).
During this process, it was only the PKB fraction which raised no criticism. The other nine fractions all expressed their opposition to the executive’s plan or supported it but with strict conditions. Some suggested the executive continue providing the subsidy but under a new, more well-targeted, effective, and fair scheme. The other suggested canceling this measure and instead to reallocate the compensation fund for other more productive and urgent purposes such as health services, free education up to high school, and rural development.

If there was something they shared in common with the executive, it was the difficulty of dealing with the fuel subsidy under circumstances marked by the economic crisis and the decreasing purchasing power of the people. All they could suggest to the executive was the need to be really careful in formulating whatever measures to be taken, especially if the fuel subsidy had to be cut.

This type of opposition from the DPR also shows how weak the executive’s partisan support was in the parliament. It was only PKB which stood behind the executive. The opposition was politically understandable because late 2000 – when the executive and the DPR debated the 2001 budget – was also the moment when executive-legislative relationships were deteriorating triggered by Wahid’s move to distance himself from the parties. Given the complexity of the conditions raised by the DPR, it was very difficult to push reform in this area unless the executive could find a better solution. Even if the executive could push reform in this area, it would be gradual and slow.

Considering the DPR’s opposition, the president and his team again had to put forward a more concrete plan. Fuel subsidy allocation was increased to Rp 41.3 trillion, much higher than the executive’s proposal. Even at this level, the fuel price had to be increased. The challenge for the executive was to determine the rate of increase. Given his hostile political surroundings, Wahid and his team could only focus on fuel type which went to a small segment of better-off groups in society. On 29 March 2001, Wahid finally issued the Presidential Decision No.45/2001. It maintained the existing kerosene price for poor households and small-scale enterprises as well as diesel fuel and premium fuel for public transportation, the national electricity company (PLN), and small-scale enterprises. On the other hand, it applied 50 per cent of market price to fuel products used by industrial and other sectors. In addition, the decision applied 100 per cent market price for fuel products used by mining sectors, foreign vessels, and fleets with international destinations. Herein,
market price referred to Mid Oil Platts Singapore (MOPS) in which the price would be increased every month based on the average price of the previous month plus 5 per cent increase.

This was an initial smart move by the executive, and occurred thanks to Minister Yusgiantoro. The adoption of an automatic adjustment by tying the fuel price partly to the international fuel price enabled the executive to change the fuel price almost every month, especially when the fuel price in international market increased significantly. By this strategy, the executive took part of fuel subsidy reform out of the political arena, a move which the DPR realized later and tried to bring back in. Opposition from the people was also not as strong as predicted. This was partly because the kerosene price was not increased.

However, this smart move was not sufficient to ease the budget constraint and fiscal sustainability was still under real pressure given worsening macroeconomic conditions, especially the Rupiah exchange rate. The executive then submitted the draft budget revision to the DPR; it was approved in mid June. This time, the fuel subsidy allocation increased to as high as Rp 60.9 trillion or 4.1 per cent of GDP, pushing the budget deficit up to -2.8 per cent of GDP (Pengestu and Goeltom 2001:159). Wahid’s quick response to push fuel subsidy reform was therefore extremely important. He issued Presidential Decision No.73/2001 on 15 June 2001 to continue the application of the automatic adjustment scheme as in March. This was also close to the end of his tenure when executive-legislative antagonism was reaching its peak. This would not be possible should the executive follow normal procedure. Based on this mechanism, fuel price was then increased by 30 per cent on average.

This time the DPR showed no opposition, in face of a much worsening budget constraint due to the Rupiah’s depreciation and international oil price hikes which caused a significant increase in subsidy allocation.98 Moreover, the central government no longer enjoyed the benefits from the oil windfall as in previous years, due to the implementation of

98 Since the sacking of Jusuf Kalla and Laksamana Sukardi in April 2000, Rupiah showed a weakening trend. It got worse by the issuance of DPR memorandum to the president in February 2001 and reached its peak at Rp 11,675/US$ in April 2001. This was also the moment when the DPR passed its second memorandum to the president. This weakening trend sustained until July 2001 when Wahid was finally impeached.
decentralization (World Bank 2001a). Unless immediate action was taken, the national budget would suffer a real pressure. Considering this, even kerosene for poor households and small-scale enterprises was increased by 14.2 per cent while the premium and diesel fuel prices for public transportation and small-scale enterprises was increased by 26.1 per cent and 50 per cent respectively. At the same time, fuel price for industries, small-scale enterprises and other sectors was also brought up to 50 per cent of the market price. In addition, a pure international market price was applied to the mining sector, foreign vessels, and fleets with international destinations as in the previous decision. With this increase, the government could save Rp 7 trillion from the subsidy allocation. From this amount, Rp 2.2 trillion was reallocated to compensation programs in food security, health, education, public transportation, micro enterprise funding, fishermen empowerment, and water sanitation infrastructure development (World Bank 2001b:6). This decision triggered public protests but not at the level that many people had feared. With this measure, government could only reduce the fuel subsidy from 5.4 per cent of GDP in 2000 to 4.6 per cent of GDP in 2001. At this level, it was clear that government had failed to meet the target set in the PROPENAS to reduce overall subsidy to 3.4 per cent GDP by 2001 (Ministry of Finance 2001; Ministry of Finance 2002).

What I can conclude from this case study is how limited was the progress of fuel subsidy reform under the Wahid administration in the light of its commitment to reducing it significantly. His plan to increase the fuel price in March 2000 was reversed and then delayed. In late 2000, his administration could only slightly increase the fuel price by 12 per cent on average, despite the huge increase in the fuel subsidy allocation. The most distorted fuel, kerosene, was excluded from the increase. Only in 2001 could his administration make some progress by the application of an automatic adjustment mechanism, thanks to a smart move by Minister Yusgiantoro. This limited achievement compromised the target of reducing the overall subsidies as mandated by the PROPENAS.

To understand this achievement, I have argued that it is substantially because of the low executive strength in both constitutional and partisan terms. Wahid’s vulnerability to

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99 Under the new fiscal balance arrangement, oil windfall due to international oil price hike must be shared with the regions while the central government bears the whole responsibility for the fuel subsidy allocation even when it has increased significantly due to the same reason.
dismissal and the lack of legislative majority support forced him to give up – even back down – on his administration’s targets simply to please the parliament or to avoid further executive-legislative tension. His determined response when fuel subsidy reform was urgently required, that is, when the subsidy allocation exceeded budget allocation due to the oil price increase and the Rupiah depreciation, was a luxury given the lack of political capital. Such timely and effective response was a distant memory, given the DPR’s continuous threats to the executive’s survival and the lack of legislative support in parliament. The nature of policy making marked by the prominence of long deliberations to reach agreement and the absence of a clear veto and decree power had made the condition even worse. Had Wahid been in a politically secure position – having constitutionally protected security and tenure and a reliable partisan support in parliament as well as strong legislative powers – the story would have been different. A strong executive could have simply pushed the fuel subsidy reform by increasing fuel price as this refers to the amount of spending allocated in the approved budget. What happened under the Wahid administration is that the executive had to debate again the extent of price increase and, many times, it was far too low to match the allocation for fuel subsidy in the budget law. The DPR even betrayed its own decision creating further policy uncertainty. Only a strong president could cope with this inimical condition and, as I will discuss in the next chapters, SBY has the best opportunity compared to either Megawati or (especially) Wahid.

3.5 Conclusion

The discussion in this chapter indicates that only limited progress was achieved during the Wahid administration in terms of the adoption of economic policy reform. In the main areas under investigation – fiscal policy reform, investment policy reform, and fuel subsidy reform – his administration achieved only limited progress. When the DPR mounted its opposition and when a compromise could not be found, the executive had to give up its reform agenda. In general, his administration failed to turn the initial signs of recovery into a more sustainable recovery. Revenue-related policy reform such as tax reform progressed only slowly. The executive also failed to adopt reform initiatives in budget spending. This affected the performance of the budget deficit. As for privatization, no single state enterprise was privatized during his administration despite its frequently declared
commitment, either to meet the target of deficit financing or to free it from political capture. Additionally, economic policy reform in investment-related areas such as the oil and gas and electricity sectors faced the same fate. Wahid failed to meet his target due to his inability to cope with opposition. The case of fuel subsidy reform confirms this poor achievement in which delays and reversal were common despite the fact that its allocation had far exceeded the approved allocation in annual budget. All seem to justify the pessimism expressed over the capacity of Wahid since his administration's very first day.

To put this assessment into the context, this thesis applies an institutional approach, namely the degree of executive strength. Wahid had no constitutional security of tenure. Moreover, he came from a minor party. Therefore, though he established a grand coalition cabinet, he could not maintain consolidated and reliable legislative support. At worst, this very coalition prevented Wahid from governing effectively. His confrontation with parliament not only compromised his priority of bringing about economic recovery but also opened the chance for the DPR to be involved more deeply in almost all the executive's business. Since all the economic reform investigated was politically sensitive and the DPR mounted strong opposition employing populist and nationalist slogans, the achievement was extremely limited. The opposition from the DPR simply meant maintaining the status quo.

Considering these limitations, the experience of the Wahid administration serves as a very important lesson to contemporary Indonesia on the importance of political capital. Barton (2002a:379) summarizes it in a very illuminating way: 'from the outset, Abdurrahman's greatest problem was his lack of political capital. In itself this is to be expected, but he experienced surprising difficulty in finding a solution. Indeed, one of his greatest mistakes as president was his failure to recognize the need to build a coalition of support'. Should he realize his institutional shortcoming, the situation could have been different. This is a very strong message for subsequent presidents.

Among his supporters, Wahid's election as president raised grave concerns, of which two were important. The first one was that he would have to manage further transition and reform under a very unfavorable condition marked by economic crisis and surviving elements from previous regime that would block his reform initiatives. He also had to shoulder high yet unrealistic expectations from the people to immediately bring about economic recovery. The second concern centers on his eccentric, idiosyncratic, maverick, and personalized style of leadership as found during his leadership in NU (Mietzner 2001:30; Barton 2002a:285; Ghoshal 2004a:46).
On the basis of the qualitative evidence presented in this chapter, this thesis also argues that other factors such as the prevalence of oligarchic interests, the complexity of social and economic problems Wahid had to face, or even Wahid's personal weakness are not sufficient explanation for his lack of success. All these factors were important and were playing within the new institutional arrangements which were inimical to any effective policy making. The absence of constitutional protection over the executive's security of tenure and consolidated partisan support are a primary explanation for the lack of achievement in economic policy reform. Due to this lack of political capital, though Wahid had indeed committed to economic policy reform and even with the pressure from the IMF, his administration could only adopt very limited reform.

The next two chapters will look at what happened to economic policy reform during the Megawati and SBY administrations, both of which benefited from a higher degree of executive strength. With this important political capital, these two presidents could predictably adopt more economic policy reforms, especially those with political significance. The chapters that address their administrations contrast strongly with this one on Wahid and they serve as a good comparison to assess how the variation in executive strength affects economic policy reform.
4  
Economic policy reform  
under the Megawati administration, 2001-2004  

4.1 Introduction  

This chapter assesses the achievements in economic policy reform under the Megawati administration. Compared to Wahid, Megawati was able to adopt some significant reform initiatives in politically sensitive areas though some other policy reform initiatives were delayed. This is substantially explained by the improved executive strength under her administration, coming especially from the constitutional protection over the executive’s security of tenure. This protection gave the executive a sense of freedom to cope with the increasingly assertive DPR. As under the Wahid administration, Megawati’s main obstacle came from the lack of partisan support. To be able to govern in a fragmented parliament, she established a coalition with other parties. Though the support of her coalition allies was highly unreliable, the presence of security of tenure provided her with the bare minimum political capital to cope with the opposition to her reform initiatives. In the policy-making arena, there was more even balance of power between the president and the DPR and the latter could no longer dictate to the former.

Critics of Megawati might challenge this argument. They mainly point to poor leadership stemming from Megawati’s lack of personal drive or dedication as the main culprit for the slow progress in economic policy reform (Kingsbury 2002:252; Malley 2003:135; Sadli 2003:185; Soesastro 2003:3). Her poor leadership caused her administration to perform on an auto-pilot mode (Slater 2004:84; Kassim 2005:162). Some also point to her silent personality on one side and strong nationalist sentiment on the other, as idiosyncratic obstacle to her policy reform. For them, this risked the prospects for reform when a timely policy response was urgently required and good policy had to take priority over nationalist sentiment such as in the case of privatization. As will be discussed in the following section,
in the policy-making arena, this criticism finds very limited supporting evidence if any. She did not give in easily to populist and nationalist voices and committed herself to painful policy packages, especially those agreed with the IMF (Athukorala 2002:61; Abimanyu 2003:270). Controlling the budget deficit, cutting the fuel subsidy, pushing privatization, managing government debt and boosting investment are some outstanding examples of her achievements in the policy-making arena. She even questioned those who criticized her for not having an informed understanding of what the government had to do and had done under economic circumstance at that time, especially in relation to the IMF program (Sukardi 2004). Her critics also ignore the fact that the executive did not work alone in the policy-making process. With a more assertive yet less competent DPR, such criticism should also be directed to the parliament rather than solely to the executive.

Another alternative explanation refers to the role of the IMF but must not be exaggerated as well. Even with the pressure from this institution and a strong commitment from the Megawati administration to its prescribed reform, the achievements were mixed. Therefore this alternative explanation is inadequate, especially when the achievements in economic policy reform of the Wahid administration is considered as well.

Still another possible explanation for the improved achievements in economic policy reform under the Megawati administration is the restoration of political stability, especially among political elites. Prior to her election, there was an agreement among major parties to let her govern until 2004. The chair of GOLKAR even called for a political moratorium (Tanjung 2003). With restored stability, the executive could focus on its reform agenda. This explanation is inadequate as well. As will be discussed in the coming sections, this agreement did not provide a blanket guarantee for Megawati. Instead, those joining her coalition still posed a challenge not only to her reform initiatives but also to her office particularly when she pursued unpopular policies. A more measured explanation must then refer to her improved strength, especially the protection over security of tenure.

101 His reason was that to tackle dauntingly complex national problems, all national components must be put together in a spirit of inclusiveness. A political moratorium was important to keep the balance and the political system working (Tanjung 2003:42-3). The call for a political moratorium appeared first in the DPR’s plenary session when it was debating the fate of Wahid after the second memorandum. The KKI fraction invited all other political forces to prioritize reconciliation and political moratorium over conflict (Muhammad 2002:201).
To pursue this argument, in the first section I will discuss achievements made in economic policy reform during the Megawati administration. I then link these achievements to the degree of executive strength. After that, in the final section I will again present the case study of fuel subsidy reform under her administration to assess more deeply the effects of improved executive strength on economic policy reform.

4.2 Economic policy reform under Megawati

When Megawati came to power, she inherited social and economic conditions which were slowly improving though they were still far from sufficient to bring about economic recovery. In the economic arena, 'corporate debts remain largely unrestructured, bank lending is limited, the government owns or controls most of the banking system and substantial business assets, fiscal sustainability is questionable, inflationary pressures are strong and the investment climate is unattractive' (Deuster 2002:6).\(^{102}\) In essence, her administration faced two main challenges: maintaining macroeconomic stability and improving business-related micro economies. The first one dealt with increasing economic growth, fighting inflation, stabilizing the Rupiah exchange rate, increasing budget revenue, controlling spending, maintaining the deficit at a realistic level in order not to risk fiscal sustainability while at the same time boosting economic growth, and managing government debt. The second challenge was how to create a business-friendly investment climate, to include tax reform, banking restructuring, privatization, combating corruption, law enforcement, and enhancing security.

Considering the severity of the problems at hand, Megawati started her administration by restoring the relationship with the IMF. Her commitment to the IMF was expressed through the signing of the new Letter of Intent on 27 August 2002, a month after her election. After that, her administration still maintained a good relationship with the IMF by signing several

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\(^{102}\) For the banking system, Boediono (2005:374) maintains that due to the recapitulation program and liquidity support facility, government ownership over the banking sector was recorded at 95 per cent. The program had consequently led to "nationalization" of the banking sector under the spirit of "normalization". To correct this, government then launched a divestiture program by reselling its share ownership to the market.
Letters of Intent until the end of 2003.\textsuperscript{103} Through this document, her administration set several policy targets such as maintaining macroeconomic stability, enhancing fiscal sustainability, and continuing financial and corporate governance reform with privatization as one of the priorities. Though Megawati announced her cabinet program,\textsuperscript{104} many informed scholars and analysts argued that it was more realistic for her administration to commit to the policy measures agreed with the IMF. Some targets were tied to the IMF conditionality, the failure of which could cancel the financial support from the IMF and other donors (Feridhanusetyawan 2003:239). In contrast, the ability to commit to the approved agreement would not only secure the IMF’s financial support but also send positive signal to business actors which was very important to boost investment (Djiwandono 2003).

The following paragraphs will assess Megawati’s achievements in three main policy areas: fiscal policy, investment related policy, and fuel subsidy.

4.2.1 Fiscal policy reform

Fiscal policy reform was still the main agenda for the Megawati administration. Given the slow progress of reform in this area under the Wahid administration, her administration had to face even more daunting challenges. The four main issues were increasing budget revenue by broadening the revenue base, targeting budget spending, controlling the deficit and finding the resources to finance the deficit by focusing on domestic sources.

In trying to increase budget revenue, the executive employed several interrelated strategies: improving revenue administration, enhancing law enforcement, combating collusion and corruption in revenue-generating bodies, and pushing further policy reform. This was especially important for boosting tax receipts which were still the main source of budget revenue.

\textsuperscript{103} Up to the end of 2003, her administration sent eight Letters of Intent to the IMF.

\textsuperscript{104} The cabinet program of the Megawati administration consisted of six points: (1) to maintain national unity and integration; (2) to continue reform and democratization in all aspects; (3) to normalize the economy by strengthening the people’s economy; (4) to strengthen law enforcement, restore security and combat corruption, collusion and nepotism; (5) to restore Indonesia’s dignity and regain international credibility; and (6) to prepare for the 2004 general election (Kompas 10 September 2001; Koran Tempo 10 September 2001).
revenue. While the tax potential was promising, its contribution to the national budget was still limited as shown by the low tax ratio.\textsuperscript{105} Given that the DPR was still against any tax rate increase,\textsuperscript{106} the only possible way was by improving tax administration, enhancing law enforcement and combating corruption in the tax office. To maximize non-tax revenue, the main challenge was enhancing law enforcement given the severity of illegal mining, illegal logging and illegal fishing.

Taking this into account, Megawati launched a series of policy measures. For example, in 2002, her administration established the Large Taxpayers Office using modern systems to specifically serve large tax payers. This brought significant changes not only to increasing the tax revenue by 30 to 40 per cent annually but also in reducing corruption and collusion and restoring government credibility at the same time (\textit{Media Indonesia} 28 December 2006). It was clear that more efforts were needed for law enforcement and collusion and corruption eradication.

Another important achievement of Megawati in tax policy reform was the passage of Law 14/2002 on the Tax Court. This is to protect both tax payers and tax officers when tax-related disputes arise. The executive could push its agenda by setting up the tax court as the first and last resort to resolve any tax-related disputes despite the DPR’s demand to open up the opportunity for an appeal to the Supreme Court (\textit{Tempointeraktif} 13 March 2002). This was to avoid dealing with Indonesia’s corrupt legal system and tax administration.

The Megawati administration also signed several bilateral agreements on the avoidance of double taxation and prevention of fiscal evasion.\textsuperscript{107} The DPR fully endorsed these steps

\textsuperscript{105} The DPR always requested the executive to increase the tax ratio given that the Indonesian tax ratio was still much lower than those of its neighboring countries. The PROPENAS set a target to increase the tax ratio by 12 per cent of GDP in 2001, 13.6 per cent of GDP in 2002, 14.8 per cent of GDP in 2003 and 16 per cent of GDP in 2004. This is to at least approach the tax rate in other ASEAN countries. The actual achievement was far from those targets: 12.6 per cent of GDP in 2001, 13 per cent of GDP in 2002, 13.5 per cent of GDP in 2003, 12.2 per cent of GDP in 2004, 12.7 per cent of GDP in 2005 (Ministry of Finance 2006).

\textsuperscript{106} Three common and populist reasons for DPR’s opposition against a tax rate increase were (1) the severity of corruption in tax offices, (2) its concern over the investment climate, and (3) the burden placed on the people as a result of the economic crisis.

\textsuperscript{107} For example, she signed an agreement with the Democratic Republic of Korea (Presidential Decision No.57/2003), Thailand (Presidential Decision No.92/2003), Netherlands (Presidential Decision No.96/2003), Mexico (Presidential Decision No.7/2004), and Portugal (Presidential Decision No.67/2004) on this matter.
since it was also in its interest to pursue such measures. Realizing that further tax reform was needed, her administration also proposed to revise existing tax laws. Some of the main objectives were to provide tax incentives for investment by reducing the highest corporate tax rate and to reduce tax evasion and avoidance to be able to increase tax revenue (Kenward 2004:14; Marks 2004:167; Ministry of Finance 2004:79-80). Megawati submitted all the drafts to the DPR in late 2003 but no debate on this was held until she left office. Despite this mixed performance, her administration was able to increase tax receipts in nominal amount, though the target for increasing the tax ratio as set in the PROPENAS could not be met yet.  

The next reform agenda in the fiscal policy area was how to target government spending. Even if the executive could increase budget revenue, the challenge for accomplishing fiscal sustainability was not over yet since it was still below the spending level requested by the DPR. Therefore, the executive was forced to target budget expenses by focusing on certain priorities and reducing others. In this respect, balancing routine and development spending which also included subsidy and debt amortization allocation was of special concern. In this area, the Megawati administration made some significant progress. Regarding debt payment, amidst opposition from the DPR, the executive maintained a flexible approach. Considering the current fiscal condition, it preferred to pay its debt in line with the agreed schedule. However, the executive also expected to accelerate payments when the situation allowed though it might have to wait until the coming of a new government in 2004 (World Bank 2003b:7). Overall, the government-debt-to-GDP ratio had declined from 86 per cent in 2001 to 80 per cent in 2002, 70 per cent in 2003 and finally to 53 per cent in June 2004 (World Bank 2004a:5; World Bank 2004b:2). This was a far better outcome than the plan to maintain a safe level of maximum 60 per cent as stipulated in the Law 17/2003 on State Finance (discussed later).

108 The PROPENAS set a target to increase the tax ratio by 12 per cent of GDP in 2001, 13.6 per cent of GDP in 2002, 14.8 per cent of GDP in 2003 and 16 per cent of GDP in 2004. This is to at least approach the tax rate in other ASEAN countries. The actual achievement was far from those targets: 12.6 per cent of GDP in 2001, 13 per cent of GDP in 2002, 13.5 per cent of GDP in 2003, 12.2 per cent of GDP in 2004, 12.7 per cent of GDP in 2005 (Ministry of Finance 2006).
In the meantime, subsidies in general and the fuel subsidy in particular were reduced significantly. Her administration brought down the fuel subsidy from 4.9 per cent of GDP in 2001 to 1.9 per cent GDP in 2002. The application of an automatic adjustment mechanism explains this achievement in the face of strong opposition from the DPR (Ministry of Finance 2003:55). In 2003, fuel subsidy allocation again decreased to 1.7 per cent of GDP for the same reason. However, she partly backed down on fuel subsidy reform in 2003 in response to the DPR’s strong opposition. Her administration also could not push any further fuel subsidy reform in 2004 resulting in the increase in the fuel subsidy allocation to 3 per cent of GDP. This achievement affected the overall subsidy allocation. In 2002, her administration reduced the subsidy allocation to 2.5 per cent of GDP from 5.5 per cent of GDP in 2001. The subsidy was maintained at the same level in the 2003 budget. However, in 2004, with the delay of the fuel subsidy reform, the overall subsidy again increased to 3.5 per cent of GDP (Ministry of Finance 2001:49; Ministry of Finance 2003:73; Ministry of Finance 2004:61). Even with this achievement, the target as set in PROPENAS was clearly not met.

With the mixed achievements in revenue and spending sides, Megawati's next challenge in fiscal policy reform was controlling the deficit. In this respect, her administration made a quite impressive achievement. It always set certain targets for budget deficit according to which budget revenue and spending were adjusted. Even when the DPR requested the relaxation of the deficit target to boost economic growth, the executive insisted on this target arguing that boosting growth requires more than fiscal stimulus. The executive instead preferred to boost investment though it was not an easy job. Due to this persistence, budget deficit during her administration was reduced significantly. It was brought down from -2.8 per cent of GDP in 2001 to -1.5 per cent of GDP in 2002, -2.0 per cent of GDP in 2003, and -1.3 per cent of GDP in 2004 (Ministry of Finance 2003; Ministry of Finance 2004; Ministry of Finance 2005).109 Though it was still beyond the target set in the PROPENAS, it was maintained at a reasonable level which helped restore macroeconomic stability and accomplish fiscal sustainability.

109 The PROPENAS set the target to reduce the budget deficit to -2.7 per cent of GDP in 2001, -2.2 per cent of GDP in 2002, -0.7 per cent of GDP in 2003, and surplus of 1.5 per cent GDP in 2004.
At this level of deficit, the next challenge for the government was how to mobilize resources to cover the deficit. As in previous years and in line with the direction of PROPENAS, the executive planned to rely on domestic sources. Foreign debt was only supplementary and this was important to accomplish fiscal sustainability. To this end, privatization was again given top priority along with other measures such as asset recovery and creating bond market.

To guide privatization, the Ministry of State Owned Enterprises formulated a ‘Master Plan for State-Owned Enterprises, 2002-2006’. This document was to improve the financial performance of around 145 SOEs given that until 2001 only 94 enterprises had performed well. The rest were in such a critical condition that immediate action had to be taken. With this guideline in hand, privatization during her administration achieved significant progress at least to cover the budget deficit. Many of the delayed targets were finally privatized such as PT Telkom, PT Indosat, and many others as shown in Table 4.1. These were achieved under strong opposition from the DPR. While there were still many other state enterprises which the executive failed to privatize, this improved achievement could at least cover the budget deficit. In the 2001 fiscal year, with only few months left after the impeachment of Wahid, her administration could mobilize Rp 3.46 trillion out of the targeted Rp 6.5 trillion to cover the deficit (Law 17/2002; Law 14/2003; Kompas 10 December 2001). This consisted of Rp 3.1 trillion from the privatization of Telkom and another Rp 0.4 trillion from the privatization of Socfindo.

This achievement improved further in 2002. From the targeted Rp 6.5 trillion for deficit financing, the executive could mobilize Rp 7.6 trillion or around 17 per cent above the target. In that year, the executive could also divest some of the taken-over enterprises such as BCA, Bank Niaga and Bank Danamon Indonesia (BDI). These were all achieved under strong opposition from the DPR. After that, in 2003, the executive was also able to mobilize Rp 7.3 trillion to cover the budget deficit. This was again above the target of Rp

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110 There were 161 SOEs in total with total assets of around Rp 800 trillion. However, government was paid a dividend of only 1 per cent with another 2 per cent of tax revenue, or less than 10 per cent of total tax revenue in 2002 (Kompas 20 April 2003). This has improved lately. Until February 2004, tax income from the SOEs had increased to Rp 40 trillion with additional Rp 9.8 trillion from dividend (Kompas 27 February 2004). Dividend income had again increased to Rp 12.8 trillion in 2005 and Rp 21.4 trillion in 2006 (Kompas 29 May 2007).
6.5 trillion. These achievements are quite significant, especially when one compares them to what achieved by the Wahid administration.

Table 4.1 Progress in privatization during the Megawati administration

<table>
<thead>
<tr>
<th>Year</th>
<th>State enterprises</th>
<th>Sold (%)</th>
<th>Proceeds Rp billion</th>
<th>Proceeds US$ million</th>
<th>Remaining share (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2001</td>
<td>Kimia Farma</td>
<td>9.2</td>
<td>110</td>
<td>-</td>
<td>90.8</td>
</tr>
<tr>
<td></td>
<td>Indofarma</td>
<td>19.8</td>
<td>1,150</td>
<td>-</td>
<td>80.2</td>
</tr>
<tr>
<td></td>
<td>Socoindo</td>
<td>30</td>
<td>-</td>
<td>45</td>
<td>10</td>
</tr>
<tr>
<td></td>
<td>Telkom</td>
<td>11.9</td>
<td>3,100</td>
<td>-</td>
<td>54.1</td>
</tr>
<tr>
<td>2002</td>
<td>Telkom</td>
<td>3.1</td>
<td>1,100</td>
<td>-</td>
<td>51</td>
</tr>
<tr>
<td></td>
<td>Indosat</td>
<td>50</td>
<td>967</td>
<td>608</td>
<td>15</td>
</tr>
<tr>
<td></td>
<td>Tambang Batubara Bukit Asam</td>
<td>15</td>
<td>-</td>
<td>-</td>
<td>..</td>
</tr>
<tr>
<td></td>
<td>Tambang Batubara Bukit Asam</td>
<td>1.5</td>
<td>156</td>
<td>-</td>
<td>..</td>
</tr>
<tr>
<td></td>
<td>Wisma Nusantara International</td>
<td>41.99</td>
<td>255</td>
<td>-</td>
<td>0</td>
</tr>
<tr>
<td>2003</td>
<td>Indo cement TP</td>
<td>16.67</td>
<td>1,157</td>
<td>-</td>
<td>0</td>
</tr>
<tr>
<td></td>
<td>Bank Rakyat Indonesia (BRI)</td>
<td>30</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td>Bank Rakyat Indonesia (BRI)</td>
<td>15</td>
<td>2,512</td>
<td>-</td>
<td>59.5</td>
</tr>
<tr>
<td></td>
<td>Perusahaan Gas Negara (PGN)</td>
<td>20</td>
<td>.</td>
<td>.</td>
<td>.</td>
</tr>
<tr>
<td></td>
<td>Perusahaan Gas Negara (PGN)</td>
<td>19</td>
<td>1,235</td>
<td>-</td>
<td>61</td>
</tr>
<tr>
<td></td>
<td>Bank Mandiri</td>
<td>20</td>
<td>2,547</td>
<td>-</td>
<td>..</td>
</tr>
<tr>
<td></td>
<td>Bank Mandiri</td>
<td>10</td>
<td>2,844</td>
<td>-</td>
<td>70</td>
</tr>
<tr>
<td></td>
<td>Pembangunan Perumahan</td>
<td>49</td>
<td>63</td>
<td>-</td>
<td>51</td>
</tr>
<tr>
<td></td>
<td>Perusahaan Gas Negara (PGN)</td>
<td>.</td>
<td>282</td>
<td>-</td>
<td>61</td>
</tr>
<tr>
<td></td>
<td>Adhi Karya</td>
<td>49</td>
<td>66</td>
<td>-</td>
<td>51</td>
</tr>
<tr>
<td></td>
<td>Tambang Batubara Bukit Asam</td>
<td>12.45</td>
<td>186</td>
<td>-</td>
<td>65</td>
</tr>
</tbody>
</table>


This improved achievement in privatization not only helped the government finance the deficit but also reduced foreign financing and, therefore, improved fiscal sustainability. For the 2001 fiscal year, to finance the budget deficit of -2.8 per cent of GDP, her administration could reduce foreign financing to only 25 per cent (0.7 per cent of GDP) compared to domestic financing which accounted for 75 per cent (2.1 per cent of GDP) (Ministry of Finance 2002; Ministry of Finance 2003). For the same reason, foreign financing had overall decreased significantly during her administration. Together with other
reform initiatives, this had contributed to the improvement of almost all macroeconomic indicators as shown in Table 4.2.

Table 4.2 Budget performance, 2002-2004

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Growth (%)</td>
<td>4</td>
<td>4.3</td>
<td>4</td>
<td>4.5</td>
<td>4.8</td>
<td>5.1</td>
</tr>
<tr>
<td>Inflation rate (%)</td>
<td>9</td>
<td>10</td>
<td>9</td>
<td>5.1</td>
<td>6.5</td>
<td>6.4</td>
</tr>
<tr>
<td>Exchange rate (Rp to US$)</td>
<td>9,000</td>
<td>9,311</td>
<td>9,000</td>
<td>8,577</td>
<td>8,600</td>
<td>8,939</td>
</tr>
<tr>
<td>Oil price (US$/barrel)</td>
<td>22</td>
<td>23.5</td>
<td>22</td>
<td>28.75</td>
<td>22</td>
<td>37.17</td>
</tr>
<tr>
<td>Oil production (thousand barrel/day)</td>
<td>1,320</td>
<td>1,260</td>
<td>1,270</td>
<td>1,092</td>
<td>1.150</td>
<td>1,040</td>
</tr>
<tr>
<td>Interest rate (%)</td>
<td>14</td>
<td>15.2</td>
<td>13</td>
<td>10.2</td>
<td>8.5</td>
<td>7.4</td>
</tr>
<tr>
<td>Revenue (% of GDP)</td>
<td>17.9</td>
<td>18.5</td>
<td>17.3</td>
<td>19.1</td>
<td>17.5</td>
<td>17.7</td>
</tr>
<tr>
<td>Expenditure (% of GDP)</td>
<td>20.4</td>
<td>20.0</td>
<td>19.1</td>
<td>21.1</td>
<td>18.7</td>
<td>19</td>
</tr>
<tr>
<td>Deficit (% of GDP)</td>
<td>-2.5</td>
<td>-1.5</td>
<td>-1.8</td>
<td>-2.0</td>
<td>-1.2</td>
<td>-1.3</td>
</tr>
<tr>
<td>Domestic financing (% of GDP)</td>
<td>1.4</td>
<td>1.1</td>
<td>1.2</td>
<td>1.8</td>
<td>2.0</td>
<td>2.3</td>
</tr>
<tr>
<td>Foreign financing (% of GDP)</td>
<td>1.1</td>
<td>0.4</td>
<td>0.6</td>
<td>0.0*</td>
<td>-0.8</td>
<td>-1.0</td>
</tr>
</tbody>
</table>

* There was a gap of 0.2 per cent GDP and the government used unspent allocation from the 2002 fiscal year.


Another fiscal-related policy reform was the passage of Law 17/2003 on State Finance and Law 1/2004 on State Treasure. The first aims to enhance financial accountability and discipline at both national and local levels, including the controversial off-budget posts in each government body. The second aims to enhance financial discipline, transparency and accountability. The laws also lay down clearly the responsibilities of all government institutions including the role of the DPR. This is important to provide clear guidelines for
the policy-making process in the future. DPR opposed some of the contents but the executive was able push forward its target.

Still another important achievement was the passage of Law 19/2003 on State-Owned Enterprises. This was in response to the PROPENAS and MPR Decree No.VI/MPR/2002 requiring a stronger legal base for privatization. On many occasions when the executive proposed the privatization of SOEs to finance the budget deficit, the DPR always requested this (DPR RI 2002:307; PPP 2003). The executive adopted this important law amidst strong opposition from the DPR.

After that, the Megawati administration also passed amendments to the Central Bank Law. These included the proposals for a lender of last resort facility and a supervisory board aimed at enhancing institutional credibility while preserving policy independence. It took a long process of debate due to DPR opposition before it was finally passed on 15 January 2004.

The materials I have discussed indicate that the Megawati administration made significant achievements in fiscal policy reform. There was also a sign of the return of technocratic approach in the budget-making process. Her administration adopted important reforms in both the revenue and spending sides of the budget with tight control over deficit. Financing deficit also relied mostly on domestic sources with the adoption of several privatization agendas. As many scholars recognize, her main contribution was maintaining macroeconomic stability with the adoption of prudent fiscal policy (Malley 2003:142; Aswicahyono and Hill 2004:277). Moreover, it adopted many related reforms such as the Law 14/2002, Law 24/2002, Law 19/2003, and others.

4.2.2 Investment policy reform

Besides fiscal reform that would lead to fiscal sustainability, Megawati also bore the responsibility of promoting investment to increase economic growth. Since 1999, economic growth had been primarily consumption-driven given the continuous deterioration of

investment performance (Alisjahbana and Manning 2002:280; Ray 2003:250; Aswichayono and Hill 2004:282; McLeod 2005b:135; Kuncoro and Resosudarmo 2006:10). This is not an easy job. However, the following examples indicate that Megawati adopted several politically difficult reform agenda in this area.

Indonesia's obstacles to investment were notorious. Macroeconomic instability, policy uncertainty, tax policy, lack of security, weak law enforcement, regulatory burdens, hostile labor market, corruption, and uncertainty over property rights were among the concerns (Waslin 2003:10-11; World Bank 2003d:29). The government itself had realized these concerns but only limited action had been taken. Understandably, Indonesia was ranked as the worst among ASEAN countries for its murky investment climate (World Bank 2005c). Business confidence in Indonesia was also very low (Alisjahbana and Manning 2003:279). Through its World Investment Report, UNCTAD (2004:14) even ranked Indonesia's investment performance the second lowest among 140 countries. This sent a strong negative signal to the business community as to how uncertain the business prospects in Indonesia were. Beside net capital outflow, mainly to China (Ray 2003:251), some multinational corporations such as Nike and Reebok finally closed their operations in Indonesia especially due to its unfriendly labor policies (such as wages and severance), lack of security and political instability (Kompas 19 October 2002; Kompas 19 January 2003; Tempointeraktif 02 February 2004). Even in sectors as strategic and beneficial as oil and gas mining, investment level showed a decline resulting in the decline of the total output (MacIntyre and Resosudarmo 2003:147).

In response to these concerns, the Megawati administration planned to push through further policy reform. The main objective was to induce competition and endorse private sector participation, especially in strategic sectors with poor performance. As expressed in the Letter of Intent to the IMF, her administration also expected to push further reform in the energy sectors. One of the concerns was the oil and gas sector. Wahid had tried to push reform in this area but failed to cope with strong opposition from both the DPR and

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112 For example, the World Bank (2005c) reports that it takes 151 days to start a business in Indonesia (compared to only 30 days in Malaysia, 33 days in Thailand, 41 days in China, 50 days in the Philippines, and 56 days in Vietnam); 570 days to enforce the contract (compared to only 241 days in China, 300 days in Malaysia, 380 days in the Philippines, 390 days in Thailand, and 404 days in Vietnam); and 6 years to go through insolvency (compared to 2.3 years in Malaysia, 2.4 years in China, 2.6 years in Thailand, 5.5 years in Vietnam and 5.6 years in the Philippines).
PERTAMINA. To propel the process, her administration resubmitted the bill on oil and gas to the DPR for further debate in September 2001. Its main objective was to create reliable, transparent, efficient, competitive, and sustainable oil and gas management. The most important effect of this bill is the reduction of the PERTAMINA’s monopoly over the production and distribution of oil. The bill transfers Pertamina’s key functions to an Executive Board (Badan Pelaksana). Overall the bill tries to induce the spirit of competition into national oil and gas management with some degree of liberalization (Kurtubi 2004; Santosa 2004). It was expected that this reform would increase private investment in the oil and gas sector which had declined in the last years. After two months of debates, the bill was finally passed in November 2001 and named Law 22/2001 on Oil and Gas. Strong opposition from the DPR and other organized groups failed to block its passage.

Also in the energy sector, the Megawati administration passed Law 20/2002 on Electricity. As in the oil and gas law, this was a long delayed bill, left from the Wahid administration. Given its sensitive nature, opposition was widespread in both the DPR and outside. The law tries to induce competition into electricity provision while securing access for poor people. It also invites the private sector, cooperatives, and local governments to participate in electricity provision given the limitation of the PLN to meet power needs (Ministry of Finance and CEPS 2004). The PLN faced financial constraints during and after the economic crisis, so private investment was exceptionally required. Moreover, the lack of competition made this enterprise very inefficient in performing its functions. Together with the Oil and Gas Law, this was an integral policy package to improve Indonesia’s investment climate.

Also important to boost investment was Megawati’s initiative to push reform in the labor area to make the labor market more competitive for investors. Compared to other countries such as China and Vietnam, Indonesia’s labor market was less competitive. Alisjahbana and Manning (2002:298-9) quote complaints from the business community regarding the irrational labor policy, low labor productivity, poor law enforcement and strikes which threaten investors’ expectations of a return on investment in Indonesia. Consequently,

many investors in labor-intensive industries such as textiles and footwear had reallocated their business to other countries, mostly China and Vietnam (Kipp 2004:64).

To create a competitive labor market for investment while at the same time protecting workers, the Megawati administration initially proposed to revise Law 25/1997 which was notorious for its repressive nature. After a long debate, the DPR annulled Law 25/1997 in September 2002 and instead expected to establish the new one. It was finally passed on 25 February 2003 and named Law 13/2003 on Workforce, amidst strong opposition from labor unions.

Still in the area of the labor market, her administration also passed Law 2/2004 on the Settlement of Industrial Disputes, again under strong opposition from labor unions and workers. It details the rules and procedures as well as the institutions for addressing industrial disputes. It introduces the use of a bipartite mechanism, deliberation, mediation, conciliation, and arbitration to solve disputes as well as the establishment of an industrial relations court. Now actors know where to go when they get into an industrial dispute. While this offers disputing parties more choices, its emphasis on the deliberation mechanism (musyawarah untuk mufakat) will consume much time and energy in any dispute resolution. Moreover, there is a concern about the applicability of those mechanisms as they are to be executed at the district level, given the different levels of capacity and supporting systems. Kenward (2004:29) also argues that the law provides limited scope for the use of mediation and arbitration. Despite these limitations, however, the law provides a stronger base for industrial dispute resolution and this is another key prerequisite for business people to undertake their activities.

In March 2004, Megawati also passed Law 7/2004 on Water Resources. Considering the gap between water supply and demand, the executive – with the facilitation of the World Bank – expected to open up an opportunity for private sector involvement. In other words, water provision was partly privatized to close this gap. This triggered strong opposition but the executive insisted on adopting it.

These are all significant achievements especially when compared to the achievement in economic policy reform under the Wahid administration. Why could Megawati adopt many
politically difficult economic policies, at least compared to Wahid? While both faced strong opposition from the DPR, the achievements in economic policy reform are much higher under Megawati than Wahid. The following section will address this question.

4.3 The effect of executive strength

As in the previous chapter, to understand the achievements in economic policy reform under the Megawati administration, it is necessary to look at the context of policy-making in which she was working. This thesis argues that this improved achievement can be substantially explained by the improved executive strength under her administration and this came especially from the constitutional protection over the president’s security of tenure. This increased strength created a degree of independence for the executive from the DPR, thus making their relationships in policy-making arena more balanced. The DPR consequently found limited room to manipulate populist and nationalist sentiments, resulting in policy making becoming more technocratic, at least compared to that of under Wahid.

4.3.1 Executive strength under Megawati

When Megawati came to office, she inherited institutional arrangements similar to those in place in the Wahid era. Under the existing arrangements, she was still elected by the MPR and had to be responsible to it. However, the constitutional amendment right after her election in late 2001 made a significant change which distinguished her from Wahid. First, it introduced direct presidential election by the people and removed the power of the MPR accordingly. Once a very powerful institution, the MPR since then only has power to (1) amend the constitution, (2) swear in the president and vice president, and (3) dismiss the president and or vice president according to the law if the Constitutional Court decides so. The GBHN was consequently removed as constitutional function of the MPR. Second, the amendment tightened the process of presidential removal from office. From now on, the

114 Except for impeachment, the MPR and the president have no constitutionally direct contact with each other. The MPR can only deal indirectly with the president through the DPR and very limited through the DPD.
president (and vice-president) cannot be removed from office on policy grounds. Moreover, the decision on impeachment is to be determined by the Constitutional Court (NDI 2002:6).\textsuperscript{115}

These new arrangements have significantly restored the president’s security of tenure and Megawati was the first president to enjoy the benefits. Overall, the constitutional amendment in 2001 strengthened the working of executive-legislative checks and balances. This was the most significant progress of institutional reform which brings Indonesia’s government system to a purely presidential system. Though Megawati was elected by the MPR, these changes made her constitutionally stronger than Wahid as she was guaranteed uninterrupted security of tenure.

While the restoration of the president’s security of tenure is important, it is not sufficient to enable the president to govern effectively. Wahid’s experience presents a very important lesson on the importance of consolidated coalition to enable the president to survive and govern effectively (Barton 2002:xxv). For Megawati, this was also extremely important given the policy challenges she had to face. She needed adequate and consolidated support in the parliament to push her many reform initiatives (Malley 2002:125; Sadli 2002:16). Since the structure and composition of parliament were still the same as under Wahid, this was not an easy job. Establishing a coalition cabinet was one such strategy, even \textit{the} strategy, for Megawati despite her improved constitutional power. She finally established another coalition cabinet and named it the \textit{Gotong Royong} Cabinet (Appendix 3).\textsuperscript{116}

As under Wahid, Megawati consulted the leaders of major parties in establishing her cabinet. This prompted a concern about the practices of horse-trading as under Wahid. Fortunately, she established a strong economic team with figures with acknowledged economic credentials.\textsuperscript{117} Many analysts dubbed her economic team as a “dream team” and

\textsuperscript{115} See Article 7A and 7B of the Constitution for the details of impeachment proceedings.

\textsuperscript{116} \textit{Gotong Royong} simply means “working together voluntarily”. This is part of Indonesian culture where voluntary mechanisms are used to solve social problems especially at local community level.

\textsuperscript{117} She trusted the Coordinating Minister for the Economy post to Professor Dorodjatun Kuncoroadjakti, a well-respected economist who had previously served as the Indonesian Ambassador to the United States. Another prominent figure was Dr. Boediono who was trusted to lead the Ministry of Finance. He was well-experienced technocrat in dealing with economic issues as he ever served as the head of BAPPENAS under Habibie administration. The other key figure was Rini Soewandi, a highly regarded businesswoman and former head of a giant business group, ASTRA International. Megawati also placed
were optimistic especially about the improvement of economic policy coordination (Siregar 2001:280; Sadli 2002:151). Other cabinet posts were distributed among the major parties. PKB stayed out of the coalition and preferred to be in opposition due to the humiliation of Wahid’s impeachment. Similarly, the PK stayed out of coalition and preferred to remain neutral until 2004 general election. Overall, the cabinet consisted of 51.5 per cent of political delegates and 48.5 per cent of non-partisan professionals, creating a more balanced composition between them. Overall, her cabinet was supported by 83.2 per cent of the DPR seats. Table 4.3 presents the composition of the Gotong Royong Cabinet.

Table 4.3 Composition of the Gotong Royong Cabinet

<table>
<thead>
<tr>
<th>No</th>
<th>Affiliation</th>
<th>Total vote (%)</th>
<th>Total seat (%)</th>
<th>Cabinet portfolio (number)</th>
<th>Cabinet portfolio (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>PDIP</td>
<td>33.7</td>
<td>30.6</td>
<td>5</td>
<td>15.15</td>
</tr>
<tr>
<td>2</td>
<td>GOLKAR</td>
<td>22.4</td>
<td>24</td>
<td>3</td>
<td>9.10</td>
</tr>
<tr>
<td>3</td>
<td>PPP</td>
<td>10.7</td>
<td>11.6</td>
<td>2</td>
<td>6.06</td>
</tr>
<tr>
<td>4</td>
<td>PAN</td>
<td>7.3</td>
<td>6.8</td>
<td>2</td>
<td>6.06</td>
</tr>
<tr>
<td>5</td>
<td>PBB</td>
<td>1.8</td>
<td>2.6</td>
<td>1</td>
<td>3.03</td>
</tr>
<tr>
<td>6</td>
<td>ABRI</td>
<td>-</td>
<td>7.6</td>
<td>4</td>
<td>12.12</td>
</tr>
<tr>
<td>7</td>
<td>Non-partisan</td>
<td>-</td>
<td>-</td>
<td>16</td>
<td>48.5</td>
</tr>
<tr>
<td>8</td>
<td>Total</td>
<td>75.9</td>
<td>83.2</td>
<td>33</td>
<td>100</td>
</tr>
</tbody>
</table>

Source: Author’s calculation from www.dpr.go.id and various publications.

Looking further at the composition of fractions in the cabinet, Megawati’s coalition comprised seven fractions with overall 87 per cent of the DPR seats (see Table 4.4). The PKB fraction declared itself as opposition, joined by two tiny fractions – PDU and PDKB – with overall only 13 per cent of the DPR seats. Though the seat share was far from sufficient to be an effective opposition, it was politically important since fractions play an

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118 The involvement of Matori Abdul Jalil had no effect on PKB’s choice to be the opposition party.
119 An inter-fractions meeting on 27 July 2001 agreed that the total numbers of cabinet portfolios would be 36, out of which 22 posts went to political parties and 14 posts to non-partisan professionals. This consequently reduced the allocation of cabinet posts for parties (Kompas 27 July 2001; Media Indonesia 27 July 2001). Megawati also tried to please Islamic forces by recruiting two independent figures from NU and Muhammadiyah, the two largest Islamic organizations in Indonesia.
120 The share of PK can be added to this figure. However, though PK left the coalition, it still joined Reformasi fraction. The immediate likely effect was for the lack of cohesion in the Reformasi fraction.
important role in the policy-making process. Fractions outside coalition could put blame on fractions joining it in the case of poor government performance though its real play remained to be seen. Therefore, the cabinet was no longer a grand coalition but rather an oversized cabinet (Reilly 2006:159).121

Table 4.4 Fractions in Megawati's coalition cabinet

<table>
<thead>
<tr>
<th>No.</th>
<th>Fractions</th>
<th>Number of DPR seats</th>
<th>Percentage of DPR seats</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>PDIP</td>
<td>153</td>
<td>30.6</td>
</tr>
<tr>
<td>2</td>
<td>GOLKAR</td>
<td>120</td>
<td>24</td>
</tr>
<tr>
<td>3</td>
<td>PPP</td>
<td>58</td>
<td>11.6</td>
</tr>
<tr>
<td>4</td>
<td>Reformasi</td>
<td>41</td>
<td>8.2</td>
</tr>
<tr>
<td>5</td>
<td>PBB</td>
<td>13</td>
<td>2.6</td>
</tr>
<tr>
<td>6</td>
<td>KKI</td>
<td>12</td>
<td>2.4</td>
</tr>
<tr>
<td>7</td>
<td>TNI/POLRI</td>
<td>38</td>
<td>7.6</td>
</tr>
<tr>
<td></td>
<td>Total</td>
<td>435</td>
<td>87</td>
</tr>
</tbody>
</table>

Source: Author's calculation.

That this coalition would help Megawati achieve her legislative agenda was a big concern. The coalition was established before the constitutional amendment restored the executive’s security of tenure. As under Wahid, coalition allies were actually forced to Megawati though not to the extent as under Wahid.122 As so, there was no guarantee that this coalition would support her in the policy-making arena by providing consolidated support. However, the restoration of the president’s security of tenure after that implies that parties and the DPR had limited space to play her survival. In the policy-making arena, this gave her a sense of freedom from the DPR which enabled her to pursue her own policy reform agenda though they had to pass through the DPR. This is especially true for policy agenda within

121 Another important motive for establishing an oversized coalition was to create a balance between nationalism and Islamism and, through this, to restore political stability. While Islamic parties voted for Wahid’s impeachment, they remained reluctant about having a women as president. This partly explained the failure of Megawati to be elected as president in the 1999 election. Therefore, though she constitutionally replaced Wahid, she had to really consider the voice of Islamic parties. The election of Hamzah Haz as vice president with the support of PDIP was one strategy. The other one was by involving Islamic parties in the coalition. Moreover, these parties had played an important role in toppling Wahid. As a matter of payback, they got represented in the cabinet.

122 In establishing her cabinet, Megawati consulted with other party leaders. To better consolidate her coalition, she and other PDIP leaders held series of inter-party meetings. One of the outcomes of this process was the adoption of a scoring system in distributing cabinet posts and the consensus to let Megawati govern until 2004 (Gatra 04 August 2001:28; Gatra 11 August 2001; Kompas 02 August 2001)
the executive's domain such as the execution of privatization and the fuel subsidy removal which are tied to the annual budget bill. At the same time, the DPR also found limited room to employ its populist and or nationalist sentiments.

To link this argument to the achievements in economic policy reform discussed previously, the next section will assess fiscal policy reform followed by privatization, investment policy reform and fuel subsidy reform.

4.3.2 Fiscal policy reform

To push fiscal policy reform, the executive had to get the green light from the DPR for most of its proposed measures. Since the DPR had become more assertive, employing populist and nationalist slogans in policy-making arena, this was not an easy job. The executive needed to deal with many different voices expressing strong nationalist and populist sentiments and put them together into one single measure. However, in cases where there was a stark difference between the two branches and no compromise could be worked out, the opportunity was open for the executive to push forward its own agenda instead of being dictated to by the DPR. This is substantially attributable to the president's increased institutional strength.

To assess fiscal policy reform, it is important to look at the annual budget-making process. In this respect, compromise between the executive and the DPR again became a major feature except in the areas of taxation, privatization and subsidy where further negotiation was required. The results of such compromises are shown in Table 4.5.

The compromise in budget-making can be explained by the fact that it deals with resource allocation and distribution and all political actors in the executive and the DPR shared a common interest in making it the instrument to push economic recovery. The only constraint to achieving this was the executive's limitation in raising budget revenue partly due to DPR opposition which at the same time always requested more spending. However, compromise was indeed difficult to reach in areas of a redistributive nature such as subsidy, tax, and privatization. In these areas, when there was compelling need for policy reform
and a policy alternative was limited if not absent, the executive could push its agenda even when the DPR opposed it.

Table 4.5 Key indicators of the annual budget, 2002-2004

<table>
<thead>
<tr>
<th>Indicators</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Proposal</td>
<td>Budget</td>
<td>Proposal</td>
</tr>
<tr>
<td>Growth (%)</td>
<td>5</td>
<td>4</td>
<td>5</td>
</tr>
<tr>
<td>Inflation rate (%)</td>
<td>8</td>
<td>9</td>
<td>8</td>
</tr>
<tr>
<td>Exchange rate (Rupiah to US$)</td>
<td>8,500</td>
<td>9,000</td>
<td>8,700</td>
</tr>
<tr>
<td>Oil price (US$/barrel)</td>
<td>22</td>
<td>22</td>
<td>20.5</td>
</tr>
<tr>
<td>Oil production (thousand barrel/day)</td>
<td>1,232</td>
<td>1,320</td>
<td>1,200</td>
</tr>
<tr>
<td>Interest rate (%)</td>
<td>14</td>
<td>14</td>
<td>13</td>
</tr>
<tr>
<td>Revenue (% of GDP)</td>
<td>17.1</td>
<td>17.9</td>
<td>16.8</td>
</tr>
<tr>
<td>Expenditure (% of GDP)</td>
<td>19.7</td>
<td>20.4</td>
<td>18.1</td>
</tr>
<tr>
<td>Deficit (% of GDP)</td>
<td>-2.5</td>
<td>-2.5</td>
<td>-1.3</td>
</tr>
<tr>
<td>Domestic financing (% of GDP)</td>
<td>1.5</td>
<td>1.4</td>
<td>0.8</td>
</tr>
<tr>
<td>Foreign financing (% of GDP)</td>
<td>1.0</td>
<td>1.1</td>
<td>0.5</td>
</tr>
</tbody>
</table>


In some of these difficult policy areas, compromise was difficult to reach and the executive had to find other alternatives. On the revenue side of the budget, the DPR always requested the executive to increase revenue especially from tax receipts. However, as in previous years, the DPR was against the proposal to increase the tax rate. According to the DPR,
what the executive needed to do was to improve tax administration and law enforcement in the tax office which was (and is still) notorious for corruption and collusion. For example, in debating the 2003 budget, the DPR maintained that efforts to increase tax revenue had to be achieved in line with fairness and transparency principles and not at the cost of private investment (GOLKAR 2002; KKI 2002; PBB 2002; PDKB 2002; PDU 2002; PKB 2002; Reformasi 2002; TNI/POLRI 2002). Moreover, it criticized the tax base which was still dominated by income and value-added taxes (VAT) and, as such, was concentrated on the low-income group. Therefore, it had to be broadened to cover those with higher income by improving self-assessment regulation and law enforcement (PDIP 2002). The same criticism was also expressed in the making of the 2004 budget (GOLKAR 2003; KKI 2003; PBB 2003; PDIP 2003; PDKB 2003; PDU 2003; PKB 2003; PPP 2003; Reformasi 2003; TNI/POLRI 2003). Besides, the DPR also requested the executive to increase the revenue from non-tax sources, especially receipts from natural resources, by improving law enforcement given the severity of illegal logging, illegal mining and illegal fishing. However, this had to be accomplished in line with the environmental sustainability (KKI 2003). The executive was also requested to increase the revenue from the state enterprise dividends given the notorious practices of corruption in these enterprises (PDIP 2002; PKB 2002; PPP 2002; Reformasi 2002).

In response to these criticisms, the executive agreed to increase budget revenue from all sources. To meet this target, more than simply pushing administrative reform such as the improvement of tax administration, the executive also proposed policy reform especially in areas of taxation. This is not an easy job. However, Megawati had the minimum political capital to do so.

The passage of Law 14/2002 on the Tax Court is a clear example. This was a politically difficult issue with strong opposition from the DPR. While the DPR demanded an opportunity for an appeal to the Supreme Court be opened up, the executive insisted on making the tax court the first and last resort to resolve any tax-related disputes. This is important for a simple process in an area which was notorious for corruption and collusion. However, those involved in tax-related disputes might appeal to the same tax court. In disputes over the tax obligation to the tax office, an appeal could only be accepted if the tax
payer paid 50 per cent of the tax amount under dispute. With this requirement, not all disputes could be brought to appeal. The DPR again criticized this for giving the chance for appealing only to those able to meet such requirement and this is against democratic principle. However, the executive again maintained that such stipulation was necessary to simplify the process and to limit the opportunity for further abuse which potentially compromise tax receipts (Tempo Interaktif 13 March 2002). This is a clear example of how the executive could push its own policy preference rather than being dictated to by the DPR. Megawati’s improved executive strength substantially explains this achievement.

However, the executive failed to amend the tax laws; they had to comply with the DPR’s Rules of Procedure. With unreliable partisan support, it could not force the DPR to pass them in a timely manner.

The next challenge for the executive in pushing fiscal policy reform was how to target spending. As in the previous years, the DPR always requested more spending against the obvious fact that budget revenue was limited. This required the executive to really target spending more efficiently and effectively by focusing on certain priorities and reducing others. The area of criticism was mainly development spending which was far below the routine spending for public servants and other administrative expenses (Golkar 2002; KKI 2002; PDU 2002; PPP 2002; TNI/POLRI 2002; PBB 2003; PKB 2003; Reformasi 2003; TNI/POLRI 2003). In the 2003 budget, this resulted in an increase of development expenditure from 2.8 per cent of GDP in the executive’s initial plan to 3.4 per cent of GDP. However, as if to contradict itself, the DPR also requested more spending for certain sectors such as public servant’s salaries (Golkar 2002; KKI 2002; TNI/POLRI 2002), education (Golkar 2002; PBB 2002; PDU 2002; PKB 2002), health, defense and security (KKI 2002; PBB 2002; PDU 2002; PKB 2002).

123 The business community opposed this article on the basis of the presumption of innocence. However, the executive argued that such a requirement is not a final verdict and the government would return all the tax already taken plus 2 per cent of interest if the tax court decided in favor of the tax payer who appealed. Dissatisfaction with this stipulation led some private companies to undertake a judicial review to the Constitutional Court. However, the Constitutional Court rejected the review twice (Hukum Online 21 July 2006; Tempo Interaktif 13 December 2004).

125 Education spending was (and is still) a delicate issue. The amended constitution requires the government to allocate at least 20 per cent of the budget expenditure for education sector. In the draft budget 2003, the executive only proposed to allocate around 4 per cent of the budget for the education sector. This stood in contrast to the allocation for debt payment which consumed more than 40 per cent of expenditure. The government was actually in a real dilemma, between the need to improve people’s welfare and the reality that it had inherited a huge amount of debt which was soon to be paid.
2002; TNI/POLRI 2002). This implied that the government had unlimited resources and could increase spending for development and routine posts simultaneously. The real condition was that the executive sometimes needed to make a trade-off between the two, given the very limited resources and its commitment to reducing government debt. Even in the face of strong opposition, the executive had made it clear that it could only accommodate what the DPR requested insofar as it did not compromise the budget deficit, and therefore, fiscal sustainability. Again, Megawati’s improved executive strength substantially explains this determination.

Another delicate issue that triggered strong opposition from the DPR was the proposal to deal with debt amortization. This was another key measure to achieve fiscal sustainability. For example, in debating the 2003 budget, some fractions in the DPR requested the executive to reduce allocation for debt payment which consumed a large proportion of the total revenue (PBB 2002; PKB 2002; PPP 2002) especially when compared to the spending for other key sectors such as health, education, job creation, and poverty eradication (KKI 2003; PBB 2003; PDU 2003; PKB 2003; Reformasi 2003; TNI/POLRI 2003). Worse than that, in debating the 2004 budget, as the election approached and in anticipation of the graduation from the IMF program, the parties took different positions on dealing with government debt payment. TNI/POLRI (2003), for example, demanded the executive not pay 100 per cent of its debt as it would put foreign reserves in danger. Reformasi (2003) even mobilized support from other fractions to approve debt amortization only at a rate similar to new debt. On the other hand, PKB (2003) demanded the executive pay back the whole of its debt to the IMF so that the government could have full control over its policies.126

In response to these criticisms, as I have discussed previously, the executive insisted on taking a flexible approach. It realized that amortizing all government debt requires a huge amount of spending and the government simply did not have it. Adopting DPR’s request

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126 Ray (2003:253-5) maintains that with the cessation of the IMF program at the end of 2003, the Government of Indonesia would have to allocate Rp 44.9 trillion for debt amortization in 2004 (2.2 per cent of GDP) compared to Rp 17.3 trillion (0.9 per cent of GDP) in 2003 under the Paris Club rescheduling facility. Total debt amortization for 2004 was Rp 69.5 trillion (3.5 per cent of GDP) or an increase of 107 per cent annually since 2002. From this, Rp 24 trillion (1.2 per cent of GDP) was for mature domestic debt or an increase of almost 150 per cent annually since 2002 (Ministry of Finance 2004:69).
would certainly create turbulence in its fiscal condition. A more realistic strategy was to follow the agreed schedule with donor institutions and accelerate it when fiscal condition allowed (World Bank 2003b:7).

The way the executive dealt with DPR opposition in spending side was another example of how the Megawati administration was able to cope with populist opposition from the DPR. This helped improve fiscal sustainability significantly. The achievement was made possible by her improved strength, especially from the constitutional protection over security of tenure which enabled her to take policy distance from the DPR.

Controlling budget deficit is the next achievement in fiscal policy reform and another example of how the executive could push its agenda amidst strong opposition from the DPR. Given that the DPR always requested more spending than what budget revenue could afford, fiscal sustainability could be placed at risk. The DPR always criticized the executive for not providing adequate stimulus for economic growth simply to maintain a low deficit (GOLKAR 2002; PDIP 2002; PKB 2002). The executive had a different opinion. Fiscal stimulus for economic growth could only be allowed at a level that would not compromise fiscal sustainability. Scholars also questioned the validity of DPR's argument. For example, Alisjahbana and Manning (2002:288) argue:

This view assumes that the continued existence of unused production capacity results simply from a lack of aggregate demand – ignoring such crucial matters as the enormous problem of widespread corporate defaults, the continued ill health of the banking system, the lack of strong leadership and consistent policy making on the part of the government, and the ever more obvious inadequacies of the legal system.

For the executive, boosting economic growth required more than just a fiscal stimulus from the government's pocket by allocating more expenses, which could lead to an even higher deficit. Other measures were also needed especially from investment. Moreover, given the financial constraints at that time, the only way to expand expenditure was from foreign debt. This was certainly against the government's long-term fiscal strategy toward self-reliance and fiscal sustainability by keeping government debt at maximum 60 per cent of GDP. Therefore for the 2004 budget, for example, Minister Boediono said that the best and
safest way was through investment (*Kompas* 22 July 2003; Ray 2003:255). This was not easy to accomplish given the poor investment performance since the economic crisis in 1997. Therefore, the most likely strategy was still a combination of debt and investment. This persistence helped the Megawati administration control deficit at a safe level while at the same time providing a necessary stimulus for economic growth.

This is another example of Megawati’s ability to take a different policy path from that of the DPR. Her economic team adopted fiscal reform measures in a relatively technocratic manner, as under Suharto. This enabled her administration to move forward with the target of achieving fiscal sustainability.

Some further points must also be made regarding Megawati’s achievement in pushing fiscal policy reform. The first is the passage of Law 24/2002 on the Treasury Bond. During the debates, the DPR mounted its opposition. GOLKAR, for example, questioned the importance of this bill which it assumed to be no more than a survival kit to cover recapitulation costs. The executive maintained that it was more than a survival kit; it was a promotional kit to boost economic growth (*Kompas* 7 February 2002). The other reason for opposition was related to the status of the treasure bonds already issued by the government. As expressed by the Reformasi fraction, it would only approve the law if the executive undertook a thorough audit of the already issued treasure bonds (*Sinar Harapan* 27 September 2002). Amidst this opposition, the law was passed. All fractions but Reformasi endorsed the law.

To improve budget management even further, the Megawati administration passed two more bills, one on state finances and the other on state treasury management. The first bill was passed on 6 March 2003 and called Law 17/2003 on State Finance. The law was approved by all fractions in the DPR. It aims to enhance financial accountability and discipline at both national and local levels, including the controversial off-budget posts in each government body. However, the law potentially creates tension between the executive and the DPR as both have a strong role in the budget-making process. As the people’s representative, the DPR wanted to play more roles in the budget making. From this point on, the DPR would play a pivotal role as it has the right to approve the budget until its...
details which was in the past left to the president.\textsuperscript{127} DPR approval is also mandatory in cases of privatization and foreign loan and grant. Besides, the law requires the involvement of the DPR in the budget preparation stage to propel the process. Furthermore, the DPR set much stronger legal sanctions and fines for financial misconduct in all state bodies (\textit{Sinar Harapan} 06 March 2003). However, the executive also succeeded in securing its agenda. The law sets out the timetable for each stage in the budget-making process with which the DPR must comply. The law even requires the DPR to approve the annual budget at least two months prior to its implementation, that is, by the end of October, for the coming fiscal year. Moreover, while the DPR’s role is important even to revise executive’s budget draft, the law limits this so as not to cause a budget deficit of more than 3 per cent of GDP. The government-debt-to-GDP ratio is also set at a maximum 60 per cent. Overall, the law provides better guidance for budget management with a more balanced relationship between the executive and the DPR (see also Ginting 2003; MacIntyre and Resosudarmo 2003:142-3).

To further enhance financial discipline, transparency and accountability, the government also passed Law 1/2004 on the State Treasury on 18 December 2003 (\textit{Kompas} 19 December 2003; \textit{Tempointeraktif} 18 December 2003). All fractions in the DPR approved it. It aims to improve the management of state funds and assets to prevent leakages and combat corruption (Kenward 2004:29). Again, the DPR wanted to play a stronger role in this area. The law stipulates that when the executive plans to sell state assets, it must proceed through open tender in which DPR approval is mandatory. Both the off-budget revenue and expenses which were commonly found in each department must now be included in the state annual budget (APBN). This was to limit the room for corruption. Moreover, a performance-based budget was to be introduced for every state institution at both national and local levels. The negative side of this law is that it now takes a long process for the disbursement of government budget, especially in the early months of any fiscal year, leaving a huge amount to be spent in the end months of the same year. Moreover, being a program or project treasurer has become a nightmare for government officers. Some experts express their concern that this and other measures in corruption

\textsuperscript{127}Article 15 stipulates that DPR approval is required for budget details concerning organizational unit, function, program, activity and type of expense. This invites negative response from the executive as it will require long and time-consuming process and the legislators have no such special competence in this area (Interview with some officers in BAPPENAS and Ministry of Finance, Jakarta 22 June 2006).
eradication have led to bureaucratic inertia and delays in undertaking urgent decisions in a timely manner (Kuncoro and Resosudarmo 2006:19).

Another related achievement in fiscal policy area was the passage of Law 3/2004 on the amendments of the Central Bank Law. During the debates, the DPR opposed some of the executive’s proposals. A clear example is the proposal for the establishment of a financial service authority (Otoritas Jasa Keuangan). The DPR argued that such an amendment was beyond the scope of the law. It had only requested the establishment of a banking supervisory body (Kompas 18 September 2003). Even against such opposition, the executive could finally push its proposal. The executive could also push its proposal on the establishment of a Supervisory Board to monitor the Central Bank against strong opposition from the Central Bank. While such a proposal is important to enhance public accountability and transparency, the Central Bank argued that it could compromise its independence (Tempo interaktif 17 December 2003). The executive also managed to push its proposal on a financial safety net. This was meant to extend the function of the Central Bank as the lender of last resort, through which the Central Bank would also provide a credit facility for an emergency situation or crisis with systemic effects for the whole economy. An agreement was also reached to establish a separate law on this matter (Sinar Harapan 19 December 2003).

Once more, this and other policy reforms adopted indicate how the executive maintained its independence in the policy-making process. It could pursue its own agendas against strong opposition from the DPR and others. These achievements would not have been possible had Megawati been in a position as vulnerable as Wahid. Having constitutional protection over security of tenure enabled her administration achieve many contentious legislative agendas though there were still some agendas which were delayed due to the lack of partisan support in the parliament.

This improved achievement in the fiscal policy area contributed significantly to efforts to bring about economic recovery. Overall, macroeconomic stability was restored and fiscal sustainability improved. Many welcomed this achievement as the main contribution of the Megawati administration. This cannot be separated from her improved executive strength which enabled her to pursue policy reform relatively independently from the parliament.
4.3.3 Privatization

The other contentious issue in the fiscal policy area is privatization. In this area, scholars placed great skepticism on her ability since this was a politically sensitive issue where nationalist, regional, and populist sentiments mixed together to block it (Alisjahbana and Manning 2002:302; Sadli 2003:187-8). Such skepticism also related to her strong nationalist personality. As I have discussed in the previous section, this was not the case. She was even, many times, accused of selling the nation to foreigners by pushing forward privatization, even for strategic enterprises such as Indosat.128

As under Wahid, the most serious challenge to privatization came from the DPR. It requested the executive to establish a special committee to discuss and oversee every single step in the privatization process for every single enterprise. It even set certain targets for pricing, beyond which it would reject the plan (World Bank 2002b:6). This frustrated the executive as privatization and divestiture used more political rule than good corporate principle. Criticism was raised, even among the members of the DPR, that privatization had been more dictated by political rule of the DPR than following corporate management principles (PKS 2006). The opposition became even stronger as the 2004 election approached. The timing of higher prices and demonstrations of nationalist sentiment were often manipulated to block reform in this area (Deuster 2002:34). All these obstacles justified pessimism over the progress of privatization.

Despite this pessimism and the opposition from the DPR, her administration achieved some significant progress in this area though slowly. As in the other areas I have discussed, the main explanation for this was her relative independence from the DPR. Her security of tenure was constitutionally protected and could not be compromised simply by policy wrongdoings. This enabled her to pursue different policy preferences from what the DPR wanted even when the latter often opposed her decisions and used interpellation and/or investigation rights to threaten her. Insofar as the executive got the approval from the DPR’s respective committees – Committee VIII and Committee IX – and followed the

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128 Among Megawati’s prominent critics are Amin Rais and Refrisond Baswir. The criticism also came from Kwik Kian Gie who was also the Minister of National Development Planning.
required procedure, it could execute the plan even with strong opposition from the DPR.\textsuperscript{129} Several of the significant cases are discussed below.

When Megawati started her administration, one of the crucial issues in privatization was PT Semen Gresik. Wahid had tried this but had failed to proceed up until the time he left office. Considering the opposition from local governments, the DPR and the executive then agreed to postpone the selling of government shares in this company to Cemex. This was because the DPR rejected the use of the put-option strategy by selling 51 per cent of government shares in this company (DPR RI 2002:320). It rather preferred the spin-off by separating its two subsidiaries – PT Semen Padang and PT Semen Tonasa – before privatizing it (Kompas 09 October 2001; Kompas 11 December 2001). The executive agreed to postpone the plan until the spin-off was accomplished.

The postponement of the Semen Gresik privatization meant that the new administration had to find other promising enterprises to cover the budget deficit. With only four months left in the 2001 fiscal year, the executive then proposed to privatize PT Telkom. To increase its trading value, the executive also planned to increase the phone tariff before privatizing this enterprise. This was important since Telkom had long been subsidized in order to be able to provide communication services at relatively low tariffs. No investors would be interested in buying the shares if the phone tariffs were maintained at that level. This proposal made the privatization of Telkom even more difficult. The DPR opposed the plan unless the executive could develop a clear plan regarding tariff increase. Despite this opposition, the executive held to its initial plan (Tempointeraktif 12 November 2001). Moreover, given that the 2001 fiscal year was about to end and the target for deficit financing was still unmet, the executive moved forward with the plan. It finally privatized 11.5 per cent of the shares in Telkom and mobilized Rp 3.1 trillion for deficit financing (Tempointeraktif 10 December 2001).

\textsuperscript{129} Here lies the main problem in undertaking privatization in Indonesia. Even when the executive received approval from the DPR's respective committees, the other legislators could still oppose the plan, making it very unclear as to who decided what. The reason for this was simply that privatization risked the interests of certain short-sighted legislators and their cronies who used SOEs as their cash cows. This was worsened by negative supervisory politics which aimed to take credit from any executive's decision rather than helping it get things right.
In addition to this, the new administration also mobilized extra receipts from the privatization of PT Socfindo. The Wahid administration had planned to sell 40 per cent of government shares in this company by September 2001. The new administration followed up on the plan and sold 30 per cent of government shares. This process was relatively smooth since the government only held minority ownership in this enterprise.

This achievement was an important test for the new administration, to show it could cope with DPR opposition in this contentious area. This is quite a significant achievement given limited time the new administration had and the political opposition it had to face. Megawati’s improved strength by the restoration of protection over security of tenure in the late 2001 substantially explains this. Such protection enabled the executive to cope with opposition especially for policy initiatives under president’s sphere. From this very moment on, Megawati had more sense of security when pushing painful reform initiatives such as privatization.

In 2002, the Megawati administration could also execute some privatization plans though slowly. As I have discussed previously, it could mobilize privatization receipts above the set target. This came from the privatization of PT Telkom, PT Tambang Batubara Bukit Asam, PT Wisma Nusantara International, and most importantly, PT Indosat. The executive postponed the privatization of other 14 enterprises, and six carry-over enterprises from the 2001 target. Given strong opposition from the DPR, the executive only prioritized on enterprises with promising value to cover budget deficit and those delayed were not the priority.

The privatization of Indosat deserves special attention as it is the most controversial one. In December 2002, after a long process, the Ministry of State Owned Enterprises sold 41.94 per cent of the share to a Singaporean company, Singapore Technologies Telemedia (STT).

130 Wisma Nusantara International and Indocement were previously private companies which were acquired by the government due to financial problem (McLeod 2005b:143).

131 They are PT Intirub, PT Atmindo, PT Cambrics Primissima, PT Kertas Padalarang, PT Kertas Blabak, PT Kertas Basuki Rahmat, PT Igles, PT Jakarta International Hotel, PT Indah Karya, PT Indra Karya, PT Virama Karya, PT Yodya Karya, PT Rekayasa Industri, PT Indocement. Government only had minority share in some of these companies such as PT Intirub, PT Atmindo, PT Jakarta International Hotel, PT Kertas Blabak, and PT Kertas Basuki Rahmat so that there was no compelling need for privatization.

132 They are PT Indorama, PT Kimia Farma, PT Bank Mandiri, PT Indocement, PT Angkasa Pura II, and PT Semen Gresik (Ministry of State Owned Enterprises 2002:22).
Before that, in April 2002, another 8.06 per cent of government shares was sold through the placement in the stock market. This left the government with a minority share of only 15 per cent in Indosat. This angered the DPR though it had approved the plan through series of consultation with the Committee VIII and the Committee IX. The Reformasi fraction even mobilized support from other fractions to use interpellation and or investigation rights (Tempointeraktif 31 December 2002; Tempointeraktif 10 January 2003). The reasons were, firstly, what the DPR agreed was simply a principal approval, through a preliminary discussion that the executive may proceed with privatization plan. There was no specific approval on what enterprises were to be privatized, to whom and at what price. The DPR requested a case-by-case consultation and approval, including for PT Indosat. Secondly, unlike the case of BCA and Bank Niaga divestment, the executive did not establish a special team for Indostat privatization. For this fraction, this was a serious infringement of the principle of due process. Thirdly, there was a strong indication that the process was not transparent, indicated by the relatively low price offered compared to the promising value of PT Indosat. Even the MPR speaker, Amin Rais, demanded the executive to cancel the agreement because Indosat is a national strategic asset. Privatizing it to foreign investors would potentially put political stability and national security at risk (Tempointeraktif 27 December 2002).

The other major fraction, GOLKAR argued contrarily that what the executive did was already in line with the law and that it had consulted with the DPR. Therefore, there was no such need to use interpellation or investigation by the DPR (Kompas 31 December 2002). Those who opposed the Indosat privatization were recommended to bring this case to the administrative court.

The executive's response to DPR opposition was no less critical. Through the Vice President and the Minister of State Owned Enterprises, it argued that what it did was in line with the MPR Decree No.IV/MPR/1999, MPR Decree No.VIII/MPR/2000, MPR Decree No.X/MPR/2001, MPR Decree No.VI/MPR/2002, Law 25/2000 on PROPENAS, and the budget bill itself, and undertaken through a very transparent and accountable procedure (Kompas 29 December 2002; Kompas 31 December 2002; Kompas 02 January 2003; Suara Merdeka 10 February 2003). The share price was even higher than expected (Tempointeraktif 03 January 2003). Moreover, the privatization of Indosat was one of the
four carry-over targets from the 2001 fiscal year which was critical to cover the deficit, whose target the DPR itself had approved (Kompas 29 December 2002; Tempointeraktif 03 January 2003). It was therefore against the law, so the executive argued, for the plan to be postponed. The vice president even welcomed the DPR’s plan to use interpellation and investigation so that the executive could explain publicly what had actually happened (Kompas 23 December 2002). The Ministry of State-Owned Enterprises also published a White Book on the chronology of Indosat privatization.133

This conflict went on until the early 2003 when 117 legislators from various fractions sent a letter to the House Speaker to use investigation right (Tempointeraktif 17 January 2003). This also failed to force the president to back down on her decision. Since all fractions finally gave up their opposition and given the strong party discipline, this move was simply ineffective. The conflict then turned on another intricate issue, namely, the executive’s decision to increase fuel prices along with electricity prices and phone tariffs. The tension finally reduced and the DPR decided not to continue its opposition to the Indosat privatization. However, even if the DPR had continued its opposition, it would have found itself with limited room to maneuver against the president.

The case shows the president’s enhanced determination in adopting difficult economic policy reform under its jurisdiction amidst DPR opposition. It is made possible by Megawati’s relative independence from the DPR due to constitutional protection over security of tenure despite the lack of a reliable legislative support. In contrast to what had happened under Wahid, the executive could now deal with DPR opposition effectively. The fact that the executive had followed all the procedures made it even more confident.

Beside the privatization of state enterprises, in 2002 the Megawati administration also received fresh cash from the divestment of BCA. This continued the process already started by the Wahid administration which had been delayed due to executive-legislative confrontation. Initially IBRA proposed a 40 per cent divestment: 30 per cent through a strategic partner and 10 per cent through a public offering. Before its execution, IBRA further requested the DPR to increase the sale to the strategic partner to 51 per cent since no

133 For detailed chronology of Indosat privatization, see Ministry of State-Owned Enterprises (2003).
potential investors would be interested in having a minority share ownership. After a long
debate, the DPR’s Committee VIII and Committee XI finally approved it (DPR RI
2002:295; Tempo 17-23 September 2001). The process was finally completed in March
2002 amidst strong opposition from the DPR and other prominent figures such as Kwik
Kian Gie and Amin Rais as well as the BCA employees (Koran Tempo 13 March 2002;
Tempo 18-28 March 2002; Tempointeraktif 01 March 2002). The main reason for this
opposition was the fact that government had allocated a large amount of money under the
recapitulation program: around Rp 29 trillion of liquidity support and another Rp 60 trillion
of treasure bonds. The government would also have to pay the bond interest of around Rp
15 trillion in 2000 and 2001. The fact that the new major shareholder would be exempted
from these costs made the DPR even more reluctant to divest it. Its opposition was even
stronger as it would potentially go to foreign investor (Tempo 17-23 September 2001). For
this reason, the DPR requested the executive to prioritize divestment for local partners
despite the fact that the domestic banking players were also part of the problem. The
executive, on the other hand, insisted on applying a fair and transparent procedure,
regardless of investors’ nationality. A US-based company, Farallon, finally won the bid and
it paid only 10 per cent of government recapitulation costs.\footnote{See also Sjahrr (2002) for a counter argument on the value of BCA and government costs should this company not be divested immediately.} The executive’s
determination had secured additional receipts of Rp 5.2 trillion from this company though it
was far below the cost the government had paid to recapitalize and restructure it.

The success in divesting BCA was followed by success in other enterprises. One immediate
target was the divestment of Bank Niaga which was expected to be undertaken in June
2002. The DPR had approved the divestment of 51 per cent of government shares in this
company to strategic partners. However, IBRA failed to find a prospective investor with the
appropriate price. Therefore, the DPR requested the executive to cancel the plan (Kompas
21 June 2002; Sinar Harapan 21 June 2002). When IBRA found a potential investor, the
DPR again opposed the plan arguing that the price offered was lower than expected. It
requested the executive to sell the government’s shares at a minimum of Rp 30/share,
otherwise, the tender process had to be cancelled and repeated. Amidst this opposition, the
executive moved forward with the plan and finally divested 51 per cent of government
shares in BCA to Commerce Holding Asset Berhard from Malaysia at a price of Rp 26.5/share.\textsuperscript{135}

The divestment of Bank Danamon Indonesia (BDI) presents a similar story. The DPR initially requested the executive to give priority to the people through a public offering. If the executive wanted a strategic sale, the investor had to have a good reputation proven by a fit and proper test by the Central Bank and it must consider the best timing and pricing (DPR RI 2003:485). Through a series of debates, the IBRA and the DPR then agreed to divest 71 per cent of government shares – 51 per cent to a strategic partner and 20 per cent through a public offering. Later, the DPR backed down on its approval due to the low market price. It opposed the plan due to its disappointment with the executive’s decision to privatize Indosat. It also requested the executive to cancel all plans until the establishment of a clear legal framework for privatization (\textit{Kompas} 05 November 2002; \textit{Kompas} 04 February 2003; \textit{Pikiran Rakyat} 04 February 2003). Despite this opposition, IBRA maintained in early 2003 that it would go ahead with the plan regardless of the DPR’s disapproval since it had accepted a promising proposal from potential investors. It finally completed the privatization of 51 per cent of its share in the BDI in May 2003 (\textit{Kompas} 06 May 2003). In response to this, the DPR requested the Minister of State-Owned Enterprises to explain the process before the DPR’s plenary session. This request was simply ignored by the executive and the plan went ahead (\textit{Tempointeraktif} 22 May 2003).

So far, the discussion has indicated the executive’s heightened determination in pushing privatization amidst strong opposition from the DPR. Though Megawati had inadequate partisan support, she had minimal political capital to push ahead with difficult policy reform, drawn from the constitutional protection over the president’s security of tenure. This capital helped the executive privatize some state enterprises against strong opposition from the DPR. This stands in contrast to what happened under Wahid when DPR opposition had blocked all targets.

\textsuperscript{135} Please visit \url{http://www.perbendaharaan.go.id/modul/terkini/index.php?id=446} for detailed information on this. Rumors spread during this process that the legislators in the Finance Committee had received bribe from the IBRA, varying from US$ 1,000 to US$ 15,000 to secure their support for Bank Niaga divestment. IBRA rejected the rumors but some legislators blatantly admitted to have accepting it (\textit{Koran Tempo} 21 August 2002).
Due to its increased confidence, the executive again proposed the privatization of other 30 SOEs in the 2003 fiscal year. Ten of them were new targets such as PT Bank Rakyat Indonesia (BRI), PT Angkasa Pura I (Bali International Airport), PT Adhi Karya, PT PGN, PT Asuransi Kredit Indonesia (AKI), PT Kawasan Berikat Nusantara, PT Jakarta Industrial Estate Pulo Gadung, PT Surabaya Industrial Estate Rungkut, PT Danareksa, and PT Pembangunan Perumahan. Also included was Bank Mandiri which was planned to be privatized through an initial public offering (IPO). It also planned to privatize other 16 carry-over enterprises from the 2002 fiscal year and four carry-over enterprises from the 2001 fiscal year (TempoInteraktif 02 February 2003). This was expected to mobilize Rp 8 trillion for the 2003 budget (Ministry of Finance 2003:79). Priority was given to three promising enterprises: BRI, PGN and Bank Mandiri. Achieving this target would predictably be quite difficult since all parties tried to appeal to the public prior to the 2004 election. Megawati herself was electorally too vulnerable to push a politically unpopular agenda since she was preparing herself for reelection. Therefore, the executive adopted a more reasonable strategy by focusing on certain enterprises only which had the potential to cover the budget deficit.

Up to the end of 2003, the executive had only privatized four enterprises. PT Indocement followed Wisma Nusantara International to become purely private enterprises by the selling of 16.67 per cent of government shares. As expressed by Minister Boediono, this was completed relatively smoothly since the government only held minority share ownership and no approval from the DPR was required (Sinar Harapan 11 September 2003). On the contrary, such approval was required for the privatization of Bank Mandiri, BRI and PGN.

To privatize the Bank Mandiri, the executive planned to complete the IPO by June 2003 but this was subject to market price. More importantly, to proceed with the plan, the executive had to get DPR approval. After a long debate, the DPR finally approved the sale of a maximum 30 per cent of government shares. In June 2003, the executive finally sold 20 per cent of government share through the IPO in the Jakarta and Surabaya stock markets due to weak market response (TempoInteraktif 04 June 2003).

Meanwhile for the BRI, the executive proposed to privatize a minimum of 30 per cent of government shares through IPO (TempoInteraktif 14 April 2003). This required the
approval of the DPR. The DPR requested that the IPO proceed in two stages: 20 per cent in the first stage and another 10 per cent in the second stage. It also requested the executive to set an above-book-value price (Kompas 03 September 2003). Taking this feedback into account, the executive moved forward with its initial plan and issued another 15 per cent of new shares (Tempointeraktif 05 September 2003).

After that, the executive again proposed the privatization of PT PGN. Initially, the executive and the DPR agreed to sell a maximum of 40 per cent of the shares through IPO. However, since the PGN could only list its company in domestic market, the DPR only approved a maximum 30 per cent (Kompas 05 September 2003; Sinar Harapan 04 November 2003). Finally, the executive decided to sell only 20 per cent of government shares along with the issuance of 19 per cent of new shares which was executed in December 2003 (Koran Tempo 05 November 2003; Tempointeraktif 15 December 2003).

Beyond this performance, there were many other enterprises which were unable to be privatized in 2003. These include PT. PUSRI (fertilizer), PT Angkasa Pura I, PT Angkasa Pura II, PT Adhi Karya, and PT Pembangunan Perumahan, all deal directly with public interest. For these enterprises, the DPR preferred restructuring to privatization (DPR RI 2004:287-8; Kompas 07 February 2003). This was also applied to other enterprises with a public service obligation nature such as PT PLN, PT PERTAMINA and other state-owned commercial ports. The DPR also preferred the restructuring of PT Merpati Nusantara Airlines – an Indonesian airline company beside Garuda (Kompas 31 June 2004).136

Another carry-over enterprise, PT Indofarma, also met opposition from the DPR.137 This last enterprise was the most critical to meet the budget target but the executive had to give up well before the end of the fiscal year (Tempointeraktif 27 May 2003). Considering all these obstacles, the executive then proposed a budget revision, through which privatization receipts were reduced from Rp 8 trillion to Rp 6.5 trillion. By the end of 2003, it could

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136 Merpati is a clear example of an SOE with a public service obligation (PSO) nature as it reaches most remote regions throughout the country. This very nature – beside management failure – had caused it to suffer financial problems year after year. In 1997, it showed negative equity of Rp 770 billion. In 2003, it still faced lost and required extra Rp 200 billion to stay in business (Tempointeraktif 26 June 2003).

137 Some investors from Australia, German, Belgium and Korea had expressed their interest in Indofarma but the government suddenly cancelled the decision to divest 51 per cent of its shares. Learning from the case of Indosat, potential investors thus preferred to avoid this uncertain business or face the risk of reversion.
mobilize Rp 7.3 trillion which came from the privatization of Bank Mandiri, BRI and PT PGN (Tempointeraktif 03 December 2003; see also Law 2/2006).

What emerges from the progress of privatization in 2003 is a mixed picture. In the case of the BRI, the executive could push its own agenda which was a bit different from what the DPR had approved. In other cases such as Bank Mandiri and the PGN, the market response was so poor that the executive could privatize only a certain percentage of the approved shares. Opposition from the DPR to the privatization of these enterprises was moderate since they employed the IPO option rather than a strategic sale. Others simply failed to progress since they had to be sold in consultations with the DPR on a case-by-case basis, a requirement which was unrealistic given the workload of both the DPR and the executive. For this reason, while involving many enterprises in its privatization list, the executive only focused on certain enterprises with a promising value that could cover the deficit. What was important, at least in the short run, was the fact that the executive could secure budget target from privatization receipts. This achievement was made possible by Megawati's security of tenure which enabled her to pursue her policy agenda even when the DPR opposed it.

Still in the area of privatization, the Megawati administration also made one significant achievement in 2003, probably the most significant one in the privatization area, by the passage of Law 19/2003 on the State-Owned Enterprises. The draft was presented to the DPR in late 2001. Given its importance, instead of revising the existing law, Law 9/1969, the executive and the DPR agreed to establish a totally new one. However, there were many differences between the executive and the DPR which required long debates. Among the issues were the extent of state ownership, the objective,\(^{138}\) scope of privatization\(^{139}\), and the guarantee over basic public services as mandated by the Constitution (Kompas 19 February 2003; Kompas 14 May 2003; Tempointeraktif 11 October 2003). Moreover, as discussed previously, parties had no clear platform on this issue.

\(^{138}\) Article 74 of Law 19/2003 states that privatization aims to (1) broaden public ownership, (2) increase efficiency and productivity, (3) create strong financial and management structure, (4) create healthy and competitive industrial structure, (5) create a global-scale and competitive enterprise, and (6) improve business climate, macroeconomic condition and market capacity.

\(^{139}\) Article 76 of Law 19/2003 states that enterprises with competitive nature and fast-changing technology can be privatized. On the other hand, Article 77 maintains that enterprises dealing with security and defense matters, having social mission to serve people, managing strategic natural resources, and having legal mandate for state ownership cannot be privatized.
During the debates, opposition came mainly from the FKB fraction which required the executive to maintain majority ownership (at least 51 per cent of shares) in certain enterprises and ensure that the Privatization Committee could perform its task effectively. Other fractions, despite their criticism during the debates, finally supported the executive's draft with PDIP and GOLKAR providing unconditional support. GOLKAR as the second major fraction sometimes mounted opposition but finally supported the executive in all important matters. The executive could also win its proposal for the establishment of the Privatization Committee which was to be chaired by the Coordinating Minister for the Economy and consisted of the Minister of State Owned Enterprises, Minister of Finance, and respective line ministers who directly supervise the enterprises as its members.

If there was any DPR victory, it was the stipulation that any plan to privatize SOEs should be consulted with the DPR (article 82). However, this must not be exaggerated. The law also stipulates very clearly that only enterprises in which the government has more than a 50 per cent of shares can be categorized as state-owned enterprises. This means that for enterprises with less than 50 per cent of government shares, the executive can simply move forward once it decides to privatize them without consulting the DPR. Thus, in general, the law represents another victory of the executive.

What I have discussed so far generally indicates a significant improvement in the determination of the executive to deal with privatization compared to what happened under Wahid. Even when the DPR opposed the plan and/or backed away from its approval, the executive still moved forward with the agenda. The case of Indosat, BCA, BDI, Bank Niaga, BRI, and the passage of Law 19/2003 on State-Owned Enterprises are indicative evidence of how the executive could adopt difficult reform measures amidst DPR opposition. While many state enterprises were not privatized, the executive could still privatize some of them to at least meet budget targets. This improved achievement was made possible substantially because of the improved executive strength under the Megawati administration. Even with unreliable partisan support in the DPR, Megawati and her team could still move forward since she had constitutionally protected security of

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140 One speculation about this was because PDIP backed Akbar Tanjung during the trial process for his allegedly involvement in BULOG scandal. He was finally cleared of any allegations and speculation was widespread that this was because of Megawati's intervention. He paid it back by consolidating GOLKAR's support for the Megawati administration.
tenure. This provided her with the important political capital she needed to push a difficult reform agenda such as privatization.

For the 2004 fiscal year, the executive again planned to mobilize Rp 5 trillion from privatization to cover the budget deficit. This was to be achieved from the privatization of 28 enterprises including some carry-over targets from previous years. Among the targets were PT Bank Mandiri, PT BNI, PT Danareksa, PT Timah, PT Aneka Tambang, PT Tambang Batubara Bukit Asam, PT Merpati Nusantara Airlines, PT Perkebunan Nusantara III, PT Kimia Farma, PT Indofarma, PT Cambrics Primissima, and others (Kompas 27 February 2004).

This time, the task would be much more difficult given the changing political and institutional circumstances. The conduct of the 2004 election caused political actors in both the executive and the DPR to avoid unpopular measures such as this. Megawati suffered the most as all criticisms centered on her, no matter what she did or did not do. Furthermore, since the passage of Law 19/2003, the Ministry of State-Owned Enterprises could not conduct the privatization alone. Privatization required approval from the Privatization Committee. The committee had to submit the plan to the DPR for its approval. Even if the Privatization Committee approved the plan, the possibility was still wide open for the DPR to oppose it. The executive, however, would encounter no such constraints if the government only had minority shares (less than 50 per cent) in an enterprise.

As shown in Table 4.1, only 5 SOEs were privatized in 2004. Except PT Pembangunan Perumahan with a 49 per cent of shares sold, the others were privatized at a minor rate. PT Bank Mandiri and PT Tambang Batubara Bukit Asam were carry-over targets from the 2003 fiscal year. At that time, the executive had cancelled part of the approved shares. It only sold 20 per cent out of 30 per cent shares approved by the DPR in Bank Mandiri. Therefore, in March 2004 it sold the remaining 10 per cent of shares (Kompas 12 March 2004; Kompas 24 March 2004). This also applied to PT Tambang Batubara Bukit Asam. In 2003, the DPR had approved the privatization of 35 per cent of government shares but the executive only sold 15 per cent of them (Kompas 28 August 2003; Kompas 24 March 2004). For PT Pembangunan Perumahan, the executive applied the employee-and-management-buy-out (EMBO) approach, which triggered no opposition from the DPR.
Meanwhile, for PT Adhi Karya, the executive used a combination of the IPO and the EMBO (Kompas 24 March 2004). As for PT PGN, the receipts were a carry-over from the 2003 fiscal year.

With this slow progress, the total proceeds for the 2004 fiscal year only amounted to Rp 3.4 trillion or around 69 per cent of the target amount. A combination of DPR’s strong opposition and the executive’s reluctance to push this agenda due to electoral pressure mainly explains this shortfall. No political actors in either the executive or the DPR would risk their electoral fate by pursuing such an unpopular measure as privatization. Megawati would suffer the most if she pushed politically difficult and unpopular reform. Moreover, her administration was only responsible for the budget implementation until October and would leave the rest of the 2004 fiscal year to the new administration. The Minister of State Owned Enterprises blatantly said that the privatization process had been much slower that year and the executive could only move with the approval of the DPR (Kompas 14 August 2004). More attention was directed to winning the election. The DPR opposed the plan and requested the executive to postpone it until the establishment of the new administration. For example, the DPR opposed the plan to sell 30 per cent of government shares in PT BNI by October 2004 (Kompas 30 January 2004; BPKP 18 February 2004). This caused it to postpone and leave it to the new government (Kompas 04 September 2004; Kompas 28 September 2004; Tempointeraktif 27 September 2004).141

The executive also proposed to push further privatization of Bank Mandiri after selling off 10 per cent of the shares in March 2004. However, the DPR only approved another 10 per cent which was planned to be completed by the end of 2004. Amidst difficulties to get DPR approval for its detailed execution, the executive decided to postpone the plan. Moreover, no investor would be interested in having only a minority share ownership. The same applied to PT Aneka Tambang, PT Timah, PT Perkebunan Nusantara III, and others (Kompas 28 May 2004). In April 2004, the DPR even demanded the executive postpone all privatization plans until the establishment of the new administration (Kompas 29 April 2004).

141 One of the prominent parliamentary figures opposing this plan was Drajad Wibowo who was also one of the BNI’s commissioners. This case recalls the fact that some of the leading figures in the DPR also hold many key positions in both state-owned and private enterprises. They understandably play a crucial role in either supporting or blocking economic reform in these sectors.
The DPR also opposed the proposal to privatize PT Merpati Nusantara Airlines of 51 per cent of shares unless it could guarantee to continue providing flight services to remote regions (Kompas 09 September 2004). The final decision was that the government would maintain its majority ownership in this enterprise and privatization to a foreign investor could only proceed for a maximum 49 per cent of the shares. The DPR finally requested the executive to postpone this plan as well until the establishment of the new administration (Kompas 28 September 2004; Tempointeraktif 27 September 2004).

Regarding further divestment of private enterprises under government control, the DPR again only approved minor sales: 1.48 per cent of government shares in BCA, 5.65 per cent in Bank Niaga, 7.85 per cent in Bank Danamon, and 1.99 per cent in BII. As for Bank Permata, the DPR approved a plan to divest a maximum of 71 per cent in two stages. In the first stage it could divest 20 per cent through market placement while the remaining 51 per cent had to wait for an unspecified time, in consultation with the DPR (DPR RI 2004:401).

The case of privatization I have presented here shows a stark difference from what happened under the Wahid administration. Except for 2004, strong opposition from the DPR could not prevent the executive from pursuing its agenda, especially when it was critical to cover the budget deficit. The Megawati administration even privatized state enterprises with strategic value such as Indosat, Telkom, PGN and many state banks where DPR opposition had in the past blocked the process. This also applies to some taken-over enterprises such as BCA, Bank Niaga and Bank Danamon Indonesia. This stronger performance had also helped enhance fiscal sustainability. This achievement is substantially explained by Megawati’s improved executive strength. Although she lacked consolidated partisan support in the DPR, the constitutional protection over the president’s

While fiscal sustainability had improved, DPR opposition to privatization had risked investor confidence in doing business in Indonesia since it was not clear who decided what. In response to the executive-legislative tension in Indosat privatization, for example, investors from Kuwait and other Middle Eastern countries had expressed concern. While they were interested in privatization in Indonesia, the lack of legal certainty had worried them (Tempointeraktif 30 December 2002). The most worrying condition for them was the lack of credible commitment when the approved agreement could be revised and then reversed. The other indicative case was PT Indoarma. Prospective investor demand from Australia, German, Belgium and Korea on the privatization plan of this pharmaceutical industry soon faded given strong political opposition and in anticipation to Indosat-like case (Koran Tempo 13 February 2003; Tempointeraktif 11 February 2003). So were the cases of Semen Gresik and BCA. Therefore the executive for many times requested the DPR not to compromise early sign of investor confidence by posing unreasonable opposition to the already agreed decision (Kompas 29 December 2002; Tempointeraktif 21 May 2003).
security of tenure enabled her to pursue her own agenda rather than being dictated to by the DPR.

Following on from this conclusion, those who criticized the Megawati administration for the lack of progress in pushing privatization agenda must reconsider their argument. While this is true that many SOEs were still under government control, such criticism must be put in perspective. If the achievement under her administration is compared to what the Wahid administration achieved, a different conclusion will be drawn. Her administration had succeeded in pushing significant privatization though not as much as expected. Given strong opposition from the DPR and the lack of partisan support, her administration only focused on certain enterprises with a potential value that would cover deficit financing. When her administration decided so, it could push the agenda in a relatively resolute way. Her institutional underpinning, namely, constitutional protection over executive's security of tenure, substantially explains this improved achievement.

4.3.4 Investment policy reform

Improved achievements of the Megawati administration are also found in the investment area. In this area, the passage of the Law 22/2001 on Oil and Gas and the Law 20/2002 on Electricity was a clear example of the effect of the enhanced executive strength. The passage of the Law 22/2001 was extremely difficult due to strong opposition from both the DPR and Pertamina. Wahid had proposed this bill in 2000 and tried to pass it during his period. However, he could not cope with this opposition. Megawati tried to accelerate the process. A new draft was sent to the parliament in September 2001. At this time, her administration was in a much more secure position to push this difficult agenda. This also enabled the executive to maintain its initial purpose by liberalizing the oil and gas sector. Prior to its passage, some legislators sent a letter to the House Speaker to postpone the approval. The main reason was that the law was seen as being against Article 33 of the Constitution, which requires compelling state ownership over strategic resources such as oil and gas. Furthermore, the law closes the opportunity for the regions to involve in oil and gas management which potentially worsens social, economic and environmental conditions.

in respective regions. More importantly, the law contains liberal spirit by adopting market mechanism to determine domestic fuel price (Kompas 20 October 2001). In the plenary session when the law was approved, these same legislators also proposed a note of objection (minderheidsnota). Given the strong party discipline, the president only considered the voice of fractions and simply ignored opposition such as this. The PDKB fraction even refused to approve the law but it was far from an effective opposition (Kompas 20 December 2004). The executive could now go ahead with this important agenda.

Also in the energy sector, the Megawati administration passed the Law 20/2002 on Electricity. Given its sensitive nature, the draft took a long process of debate between the executive and the DPR. The Wahid administration had tried the same in 2000 but failed until he left the office. Megawati then resubmitted the draft to the DPR in late 2001 as part of her administration’s commitment to the IMF and the ADB. DPR opposition centered on the spirit of liberalization in that bill which stands in contrast to Article 33 of the Constitution. Also worrisome for the DPR was the effect of competition on public access, especially by people in remote regions and the poor. Therefore, the DPR requested access for all consumers throughout the country to be ensured (Kompas 23 November 2001). The law accommodates this by establishing a supervisory body (Badan Pengawas Pasar Tenaga Listrik) with the mandate of regulating certain segments excepted from competition and to supervise the competition in competitive segments sanctioned by the law. Moreover, the PLN could still maintain its monopoly in regions where no other provider could provide the service. During the debate, the GOLKAR fraction requested the executive not to pass the bill hastily but instead improve the management of the PLN. The executive insisted on its initial objective of inducing competition as the key to the improvement of electricity provision and efficiency (Kompas 26 April 2002). Almost all fractions finally supported the bill. Only the PKB fraction which requested the executive to socialize the law for at least two weeks before its implementation and, if it later proved to be against the Constitution, the government had to revise it (Kompas 28 August 2002). Opposition from many organized NGOs as well as from PLN’s employees failed to stop the executive from

144 Later in January 2003, a coalition of some NGOs (Asosiasi Penasihat Hukum dan Hak Asasi Manusia Indonesia (APHI), Perhimpunan Bantuan Hukum dan Hak Asasi Manusia (PBHI), and Indonesian Center For Environmental Law (ICEL) submitted judicial review to the Constitutional Court. The Constitutional Court annulled some of the articles in this law and requested the government to revise it.
adopting this reform agenda. This would not have been the case had Megawati not been in a safe position to push difficult policy reform as under the Wahid administration.

The passage of Law 13/2003 on Workforce is another achievement of the Megawati administration. Because of its sensitive nature, it took two years and nine months for the whole process. The most difficult challenge was how to accommodate the interests of the employers, employees and also the government itself. The government then involved the representatives from labor unions and employer associations during the process (Tempointeraktif 22 November 2002). This failed to stop opposition from labor associations even during the plenary session in the DPR when the law was about to be passed. As many as 22 labor unions opposed the law on the basis that it would benefit the employers more than the employees (Kompas 08 February 2003). In their assessment, the law potentially compromised their rights in areas of strike and severance pay. Moreover, the fact that the law opened up the chance for short term contracts to foreign workers scared the workers even more. However, the president insisted that the new law had accommodated the interest of all parties through a very participatory and inclusive process (Tempointeraktif 25 March 2003; Tempointeraktif 26 March 2003). All fractions in the DPR shared a similar view with the president due to a very participatory process during the debate. The law introduced some important changes though many argue that it was still far from the expectation of creating a competitive labor market.145 Given its sensitive nature, the law was the best the government could produce at the time. Revising it would be a much more difficult task in the near future.

With the passage of Law 13/2003, the Megawati administration moved to the next reform agenda, to revise the law on industrial dispute settlement. The executive expected to pass it by April 2003 (Kompas 15 March 2003). It was then extended to September 2003. This was an unrealistic target given the strong opposition from the workers and labor unions. No fewer than 60 labor unions under the banner of the Labor Protection Committee mounted strong opposition to the bill and requested government protection for the workers. This was due to their relative vulnerability in front of the employers on one side and the corrupt

145 What scared the employers was the stipulation on severance pay which can reach as high as 16 times the salary. However, the law provides stronger guidance for strikes. The workers would still be paid during a strike only if they report and get approval from the employers.
Indonesian legal system on the other side (*Tempointeraktif* 19 September 2003; *Tempointeraktif* 27 October 2003). Considering the strong opposition from the labor unions, the executive and the DPR then established a tripartite group to discuss the law in detail. The deadline was again extended from September to the end of 2003 to accommodate the interests of the workers. The law was finally passed on 16 December 2003 and called Law 2/2004 on the Settlement of Industrial Disputes in the face of strong opposition from labor unions and workers.

The last two bills discussed show that while the executive could convince the DPR on its reform agenda, it had to cope with strong opposition from the public, especially organized labor unions. With constitutional protection over security of tenure, the executive could move forward. Moreover, the DPR had put forward joint approval of the law. The opposition from the labor unions only delayed the process but did not compromise it. The DPR also found more and more limited opportunities to manipulate its populist and nationalist sentiments which in the past had compromised the executive's reform agenda.

Finally, as discussed previously, Megawati also adopted Law 7/2004 on Water Resources. Given that the law contains the spirit of privatization, it triggered strong opposition from both the DPR and the people. As expressed by the Coalition against Water Privatization, the main concern for this law was that it would require people to pay extra money for water. This even included poor farmers who rely on water supply for their activities. It criticized the government for being dictated to by the World Bank.¹⁴⁶ When the law was passed by the DPR in the plenary session, the opposition was sustained. The Reformasi fraction refused to approve the law while the PKB fraction neither approved nor rejected it. The other seven fractions only requested the executive to conduct more socialization among the people considering widespread opposition (*Walhi* 24 February 2004). This paved the way for the executive to adopt its agenda.

All these initiatives show the president's strong sense of mission to improve economic conditions in the country. While these were far from adequate, they were actually an important achievement considering the strong opposition to every single reform agenda the

¹⁴⁶ The adoption of this policy reform was a condition of the government obtaining financial support of US$ 500 million from the World Bank for Water Resources Sector Adjustment Loan (WATSAL).
executive tried to adopt. These were made possible by Megawati’s improved degree of executive strength relative to the opposition forces, especially the DPR and other interest-groups such as the labor unions.

Despite some criticisms of the deficiency of reform measures in investment-related areas, all these measures indicate Megawati’s seriousness in improving investment performance. The market seemed to respond positively by improved investment trend at the end of her administration (Soesastro and Atje 2005:14). However, the problems raised through boosting investment were much more complex than what she had done. The other bottleneck was implementation in which the government bureaucracy failed to perform as expected.

What I can conclude from the discussion so far is that achievements in economic policy reform, especially in politically difficult areas such as fiscal policy, privatization, taxation and investment had improved under Megawati. Under Wahid, the DPR opposition effectively blocked almost all initiatives to progress. This is not the case under her administration. Megawati’s improved executive strength coming from the constitutional protection over security of tenure substantially explains this. Such protection enabled Megawati to maintain policy distance from parties and parliament and pursue her own reform agenda. While strong opposition from the DPR sustained, the DPR found limited room to play with her in the policy-making arena.

4.4 Fuel subsidy reform

Fuel subsidy reform under the Wahid administration progressed very slowly despite the real challenges it had to face, especially the extent of the budget deficit. I argued in the previous chapter that this was substantially because of the president’s low executive strength. Executive strength had improved under the Megawati administration; I will show in this section that the achievement in fuel subsidy reform improved as well. The presence of constitutional security of tenure enabled her to pursue fuel subsidy reform though this almost always triggered strong opposition. As far as the executive referred to the allocation
for fuel subsidy in the annual budget and got approval from the DPR’s Committee VIII and Committee IX, it could push further reform in this area even when the DPR opposed it.

Since fuel subsidy reform was included in the annual budget bill, Megawati’s chance to push fuel subsidy reform could only start in 2002. In her speech when proposing the 2002 budget draft, she maintained that the fuel subsidy had seriously constrained the national budget, given its increased allocation. Moreover, the subsidized fuel price had triggered smuggling to neighboring countries. Therefore, the fuel price had to be increased to maintain fiscal sustainability and to prioritize spending on more vital sectors (Kompas 08 September 2001; Media Indonesia 08 September 2001). To this end, Megawati proposed a fuel subsidy allocation of Rp 32.3 trillion (1.9 per cent GDP) or a reduction by roughly 40 per cent from the 2001 budget allocation (Siregar 2001:290). This would be accompanied by another fuel price increase of 30 per cent on average (Ministry of Finance 2001).

In response to the executive’s proposal, the DPR first requested the executive to review this plan (Sinar Harapan 08 September 2001). It would only support the plan if the executive had a clear strategy on how to cope with the effect of such measure on the poor people including the readiness to deliver the compensation fund (Kompas 11 September 2001). Moreover, through the Budget Committee (2001), it expressed its criticism on three grounds. Firstly, a fuel subsidy reduction should not lead to a fuel price increase if the executive could improve efficiency in PERTAMINA. Secondly, the fuel price increase had also proved ineffective in combating smuggling so that other related measures especially law enforcement were required. Thirdly, the executive had to establish an appropriate strategy to cope with public opposition. Through a series of debate, the DPR decided to increase the fuel subsidy allocation slightly to Rp 32.9 trillion (Kompas 20 October 2001). However, it requested the executive to recalculate the extent of the fuel price increase very carefully. Whether or not the DPR fully supported the measure would be seen when the president announced the fuel price increase. Moreover, since this decision was made only by the Budget Committee, Committee VIII, and Committee XI, legislators from other committees could still oppose it.
Convinced by this initial agreement, Megawati expressed her commitment to push fuel subsidy reform in the Letter of Intent sent to the IMF on 13 December 2001.\footnote{In Paragraph I.12, the letter says: "the GOI views the phased elimination of poorly-targeted energy subsidies as a major part of its strategy to refocus spending on priority areas and achieve medium-term fiscal consolidation. Following a reduction of 0.8 percentage points of GDP in 2001, the GOI aims to reduce fuel subsidies by a further 2.8 percentage points to 1.8 per cent of GDP in 2002. To achieve this objective, domestic fuel prices will be increased by an average of 30 per cent by January 2002. For industrial and some non-industrial users, fuel prices will continue to be adjusted on a monthly basis in line with movements in international prices and the exchange rate. The GOI is exploring the possibility of applying a system of automatic adjustments for other non-industrial users not currently covered by such a system. The GOI will ensure that adequate mechanisms are in place ahead of the fuel price increase to compensate the poor."} This commitment was finally put into action on 16 January 2002 after a short delay (Jakarta Post 17 January 2002). In response to public protest, Megawati and her team insisted that the plan had to proceed, given the inefficient subsidy which had burdened the national budget and rampant smuggling to the neighboring countries (Jakarta Post 23 January 2002). The executive also maintained that it had to implement the already approved budget bill and commit to the agreement with the IMF, all requiring the reduction of the fuel subsidy. With reduced fuel subsidy allocation, fuel price had to be increased accordingly (Tempointeraktif 07 January 2002). Therefore, continuing what Wahid had initiated, Megawati issued Presidential Decision No. 9/2002 which applied an automatic fuel price adjustment to international market price referring to the Mid Oil Platts Singapore (MOPS). It increased the long-protected kerosene price for households and small-scale enterprises by 50 per cent (from Rp 400 to Rp 600 per liter) and applied 75 per cent of the market price for kerosene used by industries (with additional stipulation that it ranged from Rp 900 to Rp 1,650 per liter). The decision also applied 100 per cent market price for premium fuel, ranging from Rp 1,450 to Rp 1,750 per liter. The largest nominal increase was for diesel fuel by 67.8 per cent and it applied 75 per cent of market price, ranging from Rp 900 to Rp 1,520 per liter. Excepted from this stipulation was the price for mining-related activities to which a 100 per cent of the market price was applied while foreign vessels and ships with international destination used the international market price (Jakarta Post 17 January 2002). The decision also stated that from March 2002, fuel price would be adjusted monthly to the market price based on the price level in the previous month plus 5 per cent tax.
In response to this decision and in line with public protests, the DPR again showed its strong opposition arguing that the scheme was off the track. The DPR argued that it only approved the plan to increase the fuel price by 30 per cent on average. There was no such approval that tied the domestic fuel price to the international fuel price. The DPR also suspected that this was a trick by the executive to avoid the DPR’s approval whenever it decided to increase the fuel price. Therefore, the DPR planned to summon the Minister for Energy and Mineral Resources (Jakarta Post 18 January 2002). Despite this opposition, the executive went ahead. It argued that what it did was in line with the amount of the fuel subsidy allocated in the annual budget. This was another victory for the executive considering the implications of its decision not only to increase fuel price but also tie it partly to the international market price.

By using this mechanism, the decision presented at least two advantages. First of all, it depoliticized the policy-making process by automatically adjusting the fuel price to the market price in line with international fuel price fluctuations. The executive would not need DPR approval to increase the fuel price every time it needed to do so. Secondly, it helped reduce the fuel subsidy and make the budget less vulnerable to dramatic changes in international oil prices (World Bank 2002a:5). Using this framework, the executive could adjust the fuel price almost every month in 2002 without substantial opposition (see Table 4.6).\textsuperscript{148} The DPR gave up its opposition to this measure except requesting the executive to control commodity prices that they would not exceed the level of fuel price increase (Tempointeraktif 17 January 2002). With this measure, the Megawati administration could significantly reduce the fuel subsidy allocation from 4.9 per cent of GDP in 2001 to 1.9 per cent in 2002. Her government could also save some Rp 1.8 trillion due to lower actual spending on subsidy (Rp 31.1 trillion) compared to budget allocation (Rp 32.9 trillion) even when the international oil price was higher than assumed (US$ 24 compared to US$ 22 in the budget).

\textsuperscript{148} Note that after January 2002, the rate of price increase (and decrease) was relatively small. However, even this small change always brought about an inflationary effect on the economy. This was triggered by the speculation which almost always led to fuel scarcity in petrol stations right before government announcement. This caused the fuel price to increase more than the rate which the government determined. Moreover, once the price was increased, it would stay at that level even when the government decided to decrease it. It is this distorting effect which made the decision to increase the fuel price politically and socially sensitive, regardless of the level of increase. For this reason, even a small price increase triggers opposition not only from the DPR but also from the people.
**Table 4.6 Fuel price change during the Megawati administration (per cent)**

<table>
<thead>
<tr>
<th>Period</th>
<th>Premium</th>
<th>Kerosene</th>
<th>Diesel fuel</th>
</tr>
</thead>
<tbody>
<tr>
<td>January 2002</td>
<td>6.9</td>
<td>50</td>
<td>67.8</td>
</tr>
<tr>
<td>March 2002</td>
<td>n.a</td>
<td>n.a</td>
<td>4.6</td>
</tr>
<tr>
<td>April 2002</td>
<td>3.2</td>
<td>n.a</td>
<td>7.6</td>
</tr>
<tr>
<td>May 2002</td>
<td>9.4</td>
<td>n.a</td>
<td>11.8</td>
</tr>
<tr>
<td>July 2002</td>
<td>0</td>
<td>n.a</td>
<td>-5.8</td>
</tr>
<tr>
<td>August 2002</td>
<td>-0.9</td>
<td>n.a</td>
<td>-1.7</td>
</tr>
<tr>
<td>September 2002</td>
<td>-2.6</td>
<td>n.a</td>
<td>2.8</td>
</tr>
<tr>
<td>October 2002</td>
<td>3.6</td>
<td>n.a</td>
<td>6.1</td>
</tr>
<tr>
<td>November 2002</td>
<td>n.a</td>
<td>n.a</td>
<td>10.4</td>
</tr>
<tr>
<td>December 2002</td>
<td>n.a</td>
<td>n.a</td>
<td>-2.8</td>
</tr>
<tr>
<td>January 2003</td>
<td>3.4</td>
<td>16.7</td>
<td>-19.9</td>
</tr>
<tr>
<td>2004</td>
<td>n.a</td>
<td>n.a</td>
<td>n.a</td>
</tr>
</tbody>
</table>


The materials presented so far indicate the increased determination of the executive in pushing fuel subsidy reform. Given its sensitive nature, this would not have been possible if Megawati had had no political capital, at least, the constitutional protection over security of tenure. Such protection gave the executive a sense of freedom to pursue this politically sensitive agenda. When the DPR posed its strong opposition, the executive went ahead with the agenda referring to the annual budget.

Whether this smart move could be maintained until 2004 was a big question. Since fuel subsidy is a politically sensitive issue, political actors could manipulate it for their benefit in anticipation of the 2004 election. Moreover, the DPR seemed to have realized that the executive's smart move had deprived it of power in this contentious area. This was expressed when the executive and the DPR debated the fuel subsidy allocation for the 2003 budget.

Through its draft budget, the executive again planned to reduce the overall subsidy from Rp 41.58 trillion in 2002 to only Rp 25.34 trillion or 39 per cent cut. From this amount, Rp 13.2 trillion or 52.1 per cent would go to the fuel subsidy while the remaining 47.9 per cent was for other subsidies. This is a significant reduction from 1.9 per cent of GDP in 2002 to
0.7 per cent of GDP in 2003. Whether the executive could maintain this target was a big question given the coming election.

The responses to this proposal were various and I categorize them into two main groups. The first one was those who could understand the executive’s proposal to reduce subsidy but required the executive to do it gradually considering the real economic condition of the people. Included in this group were the PDIP (2002), Reformasi (2002) and PBB (2002) fractions. The latter emphasized further that the subsidy had to be eliminated immediately by as late as 2004 as stipulated in the PROPENAS since it had really burdened the state budget. Such a fund could be reallocated to raise development expenditure.

The second group included those who conditionally agreed with the executive’s plan to eliminate the subsidy. The condition included the request for the executive not to eliminate subsidy for kerosene consumed by poor households. Additionally, the executive had to stop subsidizing PERTAMINA and distribute it directly to the people through health and education programs. With this scheme, a price increase would not compromise the people’s access to these basic services. This was expressed, among other, by the KKI (2002) and TNI/POLRI (2002) fractions.

The most difficult condition for the executive was raised by the PDU fraction. It supported the plan to reduce the fuel subsidy and implement 100 per cent of the market price for fuel products by 2003, except for kerosene. However, the PDU requested the executive to improve compensation mechanisms, formulate a strategy for a quick response to the effects of the price increase especially addressing public protests and the fuel scarcity, distributing the compensation fund selectively with a well-targeted strategy and using a cash transfer program rather than price subsidy mechanism, enforcing transparency and accountability in delivering the compensation fund, improving the efficiency of oil production and distribution in PERTAMINA so that subsidy reduction did not lead to price increase, and preparing a sound concept and a more concrete policy measure to empower the people as part of the compensation programs (PDU 2002).

149 The only concern for the PDIP was the validity and accuracy of data on the eligible beneficiaries. Government had at least four different sources of data: the National Bureau of Statistics, the Ministry of Trade and Industry, the Ministry of Cooperatives and Small and Medium Scale Enterprises, and the Central Bank. Rather than using these data, it required village-level data.
In response to these criticisms, the executive then increased the fuel subsidy allocation only slightly, to Rp 13.6 trillion (0.7 per cent of GDP). This was still a huge reduction from the previous year by around 137 per cent. The sense of confidence due to the success with automatic adjustment in 2002 led the government to take this decision. However, in late 2002, the DPR demanded the executive annul the automatic adjustment mechanism used throughout 2002. This was certainly a drawback since it brought fuel subsidy reform back into the political process. With this decision, the DPR would again play a key role in the process, posing more difficulty for the executive. This was a politically understandable move given the coming of election and politicians desired to appeal to the people. It appeared as if they were committed to protect the people from the effects of the automatic adjustment especially when the international oil price increased. This change brought an immediate effect when the president decided to increase the fuel price together with electricity and telecommunication tariffs on 1 January 2003 through Presidential Decision No.90/2002.

In response to this decision, the DPR expressed strong opposition. The Head of the Budget Committee and the Head of Committee VIII were quoted as confirming that their committees had never discussed or approved the plan. For them, the president had acted against procedure (Kompas 14 January 2003; Republika 13 January 2003). Therefore, the DPR then invited the executive to a consultation meeting (Kompas 17 January 2003). In that meeting, the Reformasi, KKI, and PKB fractions requested the president to cancel the price increase while GOLKAR, PBB, PDU, PPP and TNI/POLRI fractions requested the president to postpone the plan. It was only Megawati’s PDIP which supported the plan but at the same time requested the Minister of Transportation to postpone the plan to increase phone, toll road, and naval and air transportation tariffs (Kompas 19 January 2003).

After the consultation with the DPR, Megawati first announced she was reviewing her decision, but then backed down on part of the decision on 20 January 2003. She slightly reduced the price for gasoline and diesel fuel, maintained the kerosene price as announced on 1 January 2003, and postponed the telecommunication and electricity price increase (Tempointeraktif 20 January 2003; Waslin 2003:6; World Bank 2003a:4). She also maintained that this decision would not compromise other priorities in the annual budget such as health, education, and poverty reduction programs.
In response to her decision, some legislators tried to mobilize support to block it. The Reformasi fraction showed blatantly its opposition and requested the president not only to revise her decision but to cancel it (Kompas 26 January 2003). However, Megawati maintained her decision. Given the strong party discipline, the opposition from the individual legislators was simply a small ripple and she only needed to consider the voice of fractions. Moreover, her decision was finally accepted by all fractions but the Reformasi and this was more than sufficient to give her a way to move forward.

The consequence of this decision was quite significant for the 2003 budget. Fuel subsidy allocation in this fiscal year increased from Rp 13.6 trillion (0.7 per cent of GDP) to Rp 30 trillion (1.7 per cent of GDP) since the international oil price had increased to US$ 27 (compared to US$ 22 in the budget assumption). It also contributed to the increase of the deficit in the 2003 fiscal year from the planned -1.8 per cent of GDP to -2 per cent of GDP (Ministry of Finance 2005). Another year of delay meant that the fuel subsidy would still burden the state budget, especially throughout 2004 when the coming of the election made the government even more reluctant to cut the subsidy. Moreover, this policy-making pattern exacerbated the already bad investment climate in Indonesia as investors were not guaranteed policy certainty.

There is another point to make regarding this decision. In expressing their criticism of the president’s decision, the members of the DPR had made it clear that their intention was not to remove her. Beyond a political commitment to let Megawati rule until 2004, they also realized that the chance for an impeachment-like measure was constitutionally limited as there was no criminal act or constitutional infringement in the president’s decision (Kompas 19 January 2003; Tempointeraktif 06 January 2003). This should have given Megawati a stronger sense of security to pursue her agenda. The fact that she backed down on part of her decision reflects more of her calculation for the next election than the lack of tenure.

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150 They united under the banner of the Caucus to Save the Nation, a loose caucus established on 6 January 2003 comprising members of several fractions including PDIP who felt dissatisfied with DPR’s decision-making mechanism (Kompas 26 January 2003). The restoration of the recall mechanism limited their policy-making power significantly and they had to submit to party or fraction leaders.

151 Kompas published three articles on 19 January 2003 with expert judgment and some legislators’ statement that Megawati could not be brought down on this ground. Among the titles are “Tiada lagi jalan untuk turunkan presiden” (There is no way to remove the president), “Megawati toh tidak bakal jatuh” (Megawati cannot be brought down), and “Megawati nyaris tergelincir BBM” (Megawati almost falls down by BBM), all in Kompas 19 January 2003.
security. The coming of the election had reduced her degree of freedom to adopt painful measures and the DPR was playing with these changing circumstances. Realizing that the DPR was playing negative politics despite all its commitments, the Vice President Hamzah Haz even asked those who had rejected the fuel price increase to direct their criticisms and protests to the DPR as well (Kompas 08 January 2003; Tempointeraktif 08 January 2003). The Minister of Energy and Mineral Resources, Yusgiantoro, also requested the DPR – together with the executive – to revise Law 25/2000 on PROPENAS since many of the targets including fuel subsidy could not be met (Tempointeraktif 06 March 2003).

Considering the achievement in fuel subsidy reform in 2003, the prospects of reform in the 2004 fiscal year were much more uncertain given the conduct of election planned this year. Through its draft budget, the executive proposed a decrease in the overall subsidy from Rp 25.5 trillion in 2003 to Rp 23.3 trillion in 2004.\(^{152}\) From this amount, Rp 14.5 trillion was allocated to the fuel subsidy. The PKB (2003) questioned this reduction given the overall increase in routine spending. It questioned where the executive had reallocated the saving from the subsidy reduction. Similarly, the Reformasi (2003) expressed its concern about the decrease of subsidy allocation since it was really important to boost the performance of the people-based economy. It also reminded the executive not to become involved in the distribution of the subsidy; it had to be directly allocated to the targeted beneficiaries. Moreover, the subsidy through a price mechanism had to be replaced by a direct cash transfer to poor households. The executive was also requested to stop subsidizing PERTAMINA. Finally, the Reformasi requested the executive to generate real economic sectors, especially those of small-scale enterprises, to create jobs and reduce unemployment.

Sharing similar concerns, the PDU fraction requested the executive to pay special attention to the reduction of the subsidy since it contradicted the very nature and challenge of poverty reduction. Moreover, the executive had to consider not only the quantity of money for the subsidy but also how to allocate it in a well-targeted and effective manner (PDU 2003).

\(^{152}\) This figure was based on temporary budget realization at the time the draft budget was prepared (August 2003). The actual realization was much higher than this. In 2003, the realization for fuel subsidy alone reached Rp 30 Trillion or 1.7 per cent of GDP, much higher than Rp 13.6 trillion or 0.7 per cent of GDP in the budget law.
A more critical assessment of the draft budget for the fuel subsidy allocation was raised by the PBB fraction. It appreciated the president’s plan to significantly reduce the fuel subsidy as it is in line with PROPENAS. It could also understand why the government still provided a subsidy for certain groups. However, it required the executive to thoroughly design the plan so as to comply with the PROPENAS direction. It also argued that while the fuel price increase could cause some negative effects, sustaining the fuel subsidy would only worsen the national economy. Therefore, it required that the subsidy be directly allocated to improve access to education and health services (PBB 2003). The PDIP fraction also questioned the executive’s plan to deal with the fuel subsidy reallocation since it was unclear as to how much the allocation for free health care and mandatory nine-year education programs was (PDIP 2003). Likewise, the TNI/POLRI fraction requested the executive to implement a tight supervision for the implementation of fuel subsidy compensation fund. However, it endorsed the plan to gradually reduce subsidy and replace the current price mechanism with a direct transfer approach (TNI/POLRI 2003).

Overall, the deliberation over the fuel subsidy allocation in this fiscal year was an exception. There were four fractions, namely the PPP, PDKB, KKI and GOLKAR, which raised no challenge to the executive’s proposal on this issue. However, this does not imply that they agreed with the plan. A more measured interpretation is their lack of interest in touching sensitive issue such as this. Besides, they seemed to believe that the executive was not careless enough to take such a risky measure prior to the election.

As if to continue on the previous track, the executive finally agreed to allocate fuel subsidy despite with a slight reduction from Rp 14.5 trillion to Rp 12.7 trillion (0.6 per cent of GDP). It was also decided to maintain the existing price level without further increase. It was sufficiently clear that the executive was anticipating the 2004 election. Maintaining the current status-quo was not only important for creating social and political stability important for the conduct of election but also to boost electoral support for the incumbent. This was achieved at the cost of fiscal sustainability. Due to the international oil price increase from US$ 22 to US$ 36 and the government’s unwillingness to increase the fuel price, the subsidy allocation in 2004 increased to as high as Rp 69 trillion (3 per cent of GDP), a significant increase of more than four times the initial amount. The budget deficit had also increased from the planned -1.2 per cent of GDP to -1.3 per cent of GDP.
What I have presented in this section support with my argument: at one time, Megawati was able to adopt the fuel subsidy reform while at other times she backed down on part of her decision. She had made a good start in 2002 by applying an automatic price adjustment against strong opposition from the DPR. This had significantly reduced the fuel subsidy allocation and the budget deficit. In 2003, a similar breakthrough faced much stronger opposition. Given the lack of partisan support and she was not electorally independent enough to push though unpopular agenda, Megawati backed down on part of her decision. The progress was even more distant in 2004. This was the time when her administration could not adopt a politically sensitive policy reform given the more unfavorable electoral politics. Except for the 2003 and 2004 fiscal years, her administration made significant progress in fuel subsidy reform. This achievement is best explained by her improved executive strength coming from the constitutional protection over security of tenure.

4.5 Conclusion

The discussion so far shows that during her administration, Megawati succeeded in adopting important economic policy reforms. In the fiscal policy area, her administration adopted significant reforms in revenue, spending, deficit and deficit financing. It maintained a prudent fiscal policy even when the DPR tried to compromise it such as in the cases of reducing the budget deficit and dealing with government debt (Aswicahyono and Hill 2004:277).

The achievement in other reform areas, however, fluctuated somewhat. Regarding fuel subsidy policy reform, her administration adopted one significant reform in 2002 with the application of an automatic adjustment mechanism. However, a similar reform was quite uncertain in 2003 when she backed down on part of an already-declared decision. The reform was delayed for the 2004 fiscal year. In terms of privatization, her administration also made significant progress by privatizing some state enterprises amidst very strong opposition from the DPR. While it could only privatize several enterprises, this had at least helped the government cover its budget deficit. Her administration also adopted further reform in the tax area though it failed to push through the amendment to the tax laws.
Also important is Megawati’s achievements in the investment policy area against strong opposition from the DPR and the people in general. Among these achievements are the passage of the oil and gas law, the electricity law, the treasury bond law, the labor law, the industrial dispute settlement law, and the water resources law. The opposition to these reforms, as I have discussed previously, was very strong but failed to stop Megawati from adopting these reforms.

This improved achievement enabled her administration to restore macroeconomic stability (Malley 2003:142; World Bank 2003a:1; World Bank 2004b:2). Fiscal sustainability also improved significantly, marked by a significant reduction in the ratio of government debt to GDP. Meanwhile, the performance of investment improved in 2004 after years of decline since 1997 though it was still far from the expected target. Considering these achievements, it might be too hasty for Megawati’s critics to raise criticisms that her administration failed bring about economic recovery. A more measured judgment would lead to a different conclusion. Moreover, such negative assessment is sometimes triggered by her unpopular reform initiatives which should be seen as her achievements such as privatization and fuel subsidy reform.

This improved performance is substantially explained by the fact that, compared to Wahid, Megawati had a better institutional underpinning as her political capital in pushing through difficult reform initiatives. This came mainly from the constitutional protection over the executive’s security of tenure. It enabled the executive to maintain a degree of freedom from the DPR which frequently tried to block unpopular reform initiatives. In general, her administration could deal with the DPR opposition more effectively than the Wahid administration, especially in reform areas with political significance such as privatization, investment, taxation and fuel subsidy. While the Wahid administration contributed in the technical preparation of some of these reform initiatives, it was the debates between the executive and the DPR which mattered. Her administration was even able to take a starkly different policy position from the DPR such as in the cases of the Indosat

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153 This is not to say that technical preparation is unimportant. However, as the narratives I have presented, the core problem lies on the negotiation between the executive and the DPR such as in the cases of the privatization of PT Semen Gresik and BCA. Megawati also ordered her team to revise some of the reform proposals.
privatization and BCA divestment. Again, this is substantially due to her improved executive strength.

With this argument, the effect of the IMF must not be exaggerated. Indeed, it played an important role in pushing much of the difficult reform agenda. However, even with its pressure, the executive was only able to adopt some reform initiatives but failed in others. Wahid even had failed to push forward the IMF-sponsored reform. The effect of political stability must also be viewed with caution. Though the political elites had agreed to let Megawati rule until 2004, the challenges to her office and policies were sustained. Opposition to her reform initiatives was almost always present resulting in the variation of reform achievement during her administration. A more measured explanation must therefore link this achievement to the policy-making context the executive was working with.

The next chapter will further assess this argument in an assessment of the SBY administration. Compared to all post-Suharto presidents, SBY has the highest degree of executive strength. As I will argue and show, this enabled him to adopt more economic reform initiatives especially in politically difficult areas.
5

Economic policy reform
under the SBY administration, 2004-2007

5.1 Introduction

This chapter assesses the achievement in economic policy reform under the SBY administration. I will argue that given his higher executive strength, his administration adopted more economic policy reform initiatives especially in politically difficult areas, compared to both the Megawati and (especially) Wahid administrations. This stems from the fact that he was directly elected by the people and was not dependent on the legislature for his continuation in office. Having a direct mandate from the people with uninterrupted security of tenure has enabled him to focus on governing especially in taking politically difficult measures. Moreover, he has more consolidated partisan support with 74 per cent of seats and seven out of ten fractions in the DPR. These are an institutionally strong combination to help him achieve most of his legislative agenda. True opposition, if any, comes only from the PDIP but it is far from sufficient to be an effective force. Thus, as far as difficult policy reform is concerned, the SBY administration has the best opportunity to pursue its own policy preferences in the face of DPR opposition.

One possible alternative explanation for this argument is SBY’s personality. He is the most technocratic and has the strongest personal commitment to economic policy reform of all presidents since 1999. I find this interpretation inadequate considering the achievement in economic policy reform in the early months of his administration. Until December 2004, given his weak partisan power, he delayed many policy reforms despite the requirement to do so. Only after the inclusion of GOLKAR in his coalition could he adopt many reform agenda. Therefore, SBY’s personality is best seen a useful but not sufficient capital for the adoption of difficult policy reform.
To pursue this argument, the first section of this chapter discusses the achievements in economic policy reform during his administration, looking especially at fiscal policy and investment-related measures. The second section connects these achievements to the effects of executive strength. The case study of fuel subsidy reform will be presented in the final section. The overall conclusion for this chapter is that the achievement in economic policy reform during the SBY period is significantly high – the highest among post-Suharto administrations – and this is mainly due to higher executive strength compared to his predecessors.

5.2 Economic policy reform under SBY

When SBY started his administration, Indonesia’s economic condition had significantly improved. However, the challenge to bring about economic recovery was far from over. While key elements of the economy were already on the right track, especially macroeconomic indicators, sustained effort to maintain them was still needed. Moreover, the micro, business-related environment was still of great concern and further policy reform was required. Among the concerns were improving the investment climate, continuing privatization, cutting wasteful subsidies, enforcing the law, combating corruption, fighting terrorism, establishing security, and still many others (see Aswicahyono and Hill 2004:278; McLeod 2005b:133). These issues are all interconnected in the context of pushing economic recovery and, given the high expectations for the new administration to bring about significant change, decisive and concerted actions in these areas were desperately required. A series of natural disasters during his administration combined with the international oil price hike and the Rupiah depreciation required him to take even more determined measures to maintain the momentum of recovery. In other words, policy environment under the SBY administration was no better than the other administrations as far as the micro economic environment is concerned.

Many informed scholars and observers argue that SBY’s election as the new president confirmed people’s dissatisfaction with Megawati’s poor performance in bringing about expected change, especially in the economic area. The rising costs of basic commodities and unemployment were the two biggest problems frustrating the Indonesian people (Asia
Foundation 2003:43; Vatikiotis and McBeth 2004:14; IFES 2005:16). In other words, his election was ‘a consequence of “deficiency fatigue”: tired of weak government, people clamoured for change and rejuvenation and swung behind the candidate who to them came like a breath of fresh air’ (Kassim 2005:174). The people, once more, expected immediate changes and they expected SBY to fulfill their expectations. On many occasions, SBY articulated his vision for change (Yudhoyono 2004). Through this strategy, he succeeded in projecting himself as the champion of change as many people expected. His personality gave him another credit. By electing SBY, people showed their high expectation for a change toward a better Indonesia (Ananta et al. 2005:118; Wessel 2005:16). Whether he can fulfill such expectations is another matter but he has sufficient political resources to achieve them.

To cope with these new expectations and policy challenges, SBY had more leeways than his predecessors. The involvement of the IMF was more limited under the Post-Program Monitoring which would be applicable until Indonesia paid all its debt, presumably 2010. Moreover, as the president is now directly elected, he has been given more policy discretion to formulate his own program. Since 2004, the GBHN was replaced by a much longer term planning document called the Long-Term Development Plan (Rencana Pembangunan Jangka Panjang, hereafter RPJP) which will last for 30 years. This is then translated into the Medium-Term Development Plan (Rencana Pembangunan Jangka Menengah, hereafter RPJM) with a duration of five years. Based on the RPJM, the president then formulates his own agenda for every year, called the Government Work Plan (Rencana Kerja Pemerintah, hereafter RKP). Based on these documents, the SBY administration set targets for 2005, 2006 and 2007 as shown in Table 5.1.

154 A series of survey conducted by IFES in 2004 show the importance of personality of the presidential candidate in the eyes of voters. It is even more important than policy and capacity (IFES 2004a; IFES 2004b; IFES 2004c). For Many people, SBY was assumed to be ‘a person of integrity, sufficient competency and “authoritative bearing”...he was very tegas, meaning “firm” and able to take decisive action’ (Ananta et al. 2005:91).

155 As in his presidential campaign, the priorities of RPJM 2004-2009 include maintaining macroeconomic and fiscal sustainability, financial sector reform, improving investment and exports, developing infrastructure by involving the private sector, and improving human resource quality.

156 There are few differences between the RPJM and PROPENAS and between RKP and REPETA in their content. The only difference is their legal base. While PROPENAS and REPETA were formulated by the executive and the DPR through a special bill, the RPJM and RKP are now formulated by the executive through presidential decision (Keputusan Presiden or Keppres) which has a much lower legal status than the law.
Table 5.1 **Targets for key economic indicators, 2005-2007**

<table>
<thead>
<tr>
<th>Indicators</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>Growth (%)</td>
<td>5.4</td>
<td>6.2</td>
<td>6.4</td>
</tr>
<tr>
<td>Exchange rate (Rp to US$)</td>
<td>8,600</td>
<td>8,700</td>
<td>9,200</td>
</tr>
<tr>
<td>Inflation (%)</td>
<td>5.5</td>
<td>7.0</td>
<td>6.0</td>
</tr>
<tr>
<td>Deficit (% of GDP)</td>
<td>-0.7 - (-0.9)</td>
<td>-0.5 - (-0.7)</td>
<td>-0.5 - (-0.7)</td>
</tr>
<tr>
<td>Tax ratio (% of GDP)</td>
<td>13.5 - 13.6</td>
<td>13.6 - 13.7</td>
<td>13.7 - 14.1</td>
</tr>
<tr>
<td>Government debt (% of GDP)</td>
<td>54.9</td>
<td>41.3 - 43.3</td>
<td>36.6 - 37.1</td>
</tr>
<tr>
<td>Unemployment (%)</td>
<td>9.8</td>
<td>8.9</td>
<td>10.4</td>
</tr>
<tr>
<td>Poverty (%)</td>
<td>..</td>
<td>13.3</td>
<td>14.4</td>
</tr>
<tr>
<td>Investment (%)</td>
<td>8.1</td>
<td>15.2</td>
<td>11.5</td>
</tr>
</tbody>
</table>

*Source: Author's summary from RKP 2005; RKP 2006; RKP 2007 (also available at www.bappenas.go.id)*

Having set these targets is only half the journey. Some of the targets require the approval of the DPR before any policy action can be taken. As in the previous chapters, the following section will discuss the achievement in fiscal policy and investment policy reform of the SBY administration.

### 5.2.1 Fiscal policy reform

The first test for pushing fiscal policy reform toward fiscal sustainability is the budget-making process. In this area, the executive’s determination was required even more. After the termination of the cooperation with the IMF in 2003, the SBY administration had to work extra hard to deal with debt payment since there was no longer a rescheduling facility offered by the Paris Club. The only exception was in 2005 due to the natural disaster in Aceh and Nias in December 2004. Its immediate consequence was that the government had to mobilize extra revenue and target spending effectively and efficiently to control the budget deficit. As in the two previous administrations, financing the deficit would rely more on domestic sources.

Looking at these aspects of fiscal policy, it can be concluded that the SBY administration achieved more significant policy reforms than the Megawati and (especially) Wahid administrations. On the revenue side, given that the government still relied on tax receipts
for the majority of its revenue, the executive adopted two main reform measures. The first one was by improving tax administration. As if to continue what Megawati had initiated, his administration adopted and implemented the large taxpayers office policy with the application of modern technology. As mentioned earlier, this has helped increase the tax revenue by 30 to 40 per cent annually (Media Indonesia 28 December 2006). The other measure was by pushing further tax policy reform. This is very important in order to be able to offer additional incentive to investors. For this purpose, the SBY administration continued Megawati's attempts to revise the existing taxation laws: Law 16/2000 on General Taxation Arrangements and Procedures, Law 17/2000 on Income Tax, and Law 18/2000 on Value Added and Luxury Taxes. One of the concerns in this plan is the provision for increased power of the tax office, making its relationship with the tax payers more asymmetrical (Sen and Steer 2005:297). The revision was expected to improve the tax payers' position by giving them legal protection against arbitrary actions by the tax office which is notorious for corruption. It was also expected that the new laws could reduce tax obstacles and legal uncertainty which had been complained about by investors (World Bank 2005c:24). In this respect, SBY's challenge came mainly from vested interests affected directly by the proposed revision, especially those in the tax office (Kuncoro and Resosudarmo 2006:20). His other job was to push the DPR to prioritize the debates on these drafts. Until the time of writing, the SBY administration had only passed Law 28/2007 to revise Law 16/2000 on the General Taxation Arrangements and Procedures. The other tax laws are still under debate and both the executive and the DPR wanted to discuss them more carefully to make them more sustainable, even though this means a delay.

The next reform agenda in the fiscal policy area was to target resource allocation. This required the capacity to prioritize limited revenue. While the DPR had a similar view to the executive on the importance of targeting limited resources, it had a different interpretation of how to accomplish the task. However, the executive could push its reform agenda such as in the case of the education allocation. Even when the Constitutional Court declared that the annual budget was partly unconstitutional due to its failure to meet the minimum required allocation as sanctioned by the constitution, the executive maintained it. More importantly, the SBY administration adopted a significant fuel subsidy reform in 2005 by significantly increasing the fuel price. In March 2005, it increased the fuel price by an average of 29 per cent while in October the same year, the fuel price was increased by more
than 114 per cent on average with the highest increase going to the long-protected kerosene for households. This was adopted even with strong opposition from the DPR and the people. The scale of opposition to this measure was the strongest one in the post-Suharto era.

Another achievement in fiscal policy reform under the SBY administration was controlling the deficit. In this area, his administration set a tight deficit target though this always triggered opposition from the DPR since it reduced stimulus for growth. Due to an increased sense of confidence, the executive slightly loosened the budget deficit target in 2006 and again in 2007 to provide fiscal stimulus for economic growth (Ministry of Finance 2007:VI-1). This was adopted without compromising the target of reducing the government debt-to-GDP ratio. It had been reduced from 56.1 per cent of GDP in 2004 to 47.9 per cent of GDP in 2005 and 41.3 per cent of GDP in 2006 (Ministry of Finance 2006:53; World Bank 2007:14). This is a significant achievement, far better than the ceiling set in Law 17/2003, that is, 60 per cent of GDP.

To finance the deficit, the executive maintained that it would rely mostly on domestic sources. Again, privatization of state enterprises became one of the priorities though the receipt target was set much lower than in previous years. For the 2005 fiscal year, the executive proposed Rp 7.5 trillion but the DPR only approved Rp 3.5 trillion (Kompas 31 May 2004; Tempointeraktif 04 May 2005). Since this had been decided by the Megawati administration prior to the election of SBY, it was uncertain whether this could be met. Among the targets to be privatized were PT Bank Mandiri, PT Tambang Batubara Bukit Asam, PT Tambang Timah, and PT Aneka Tambang. Others, such as PT Bank BNI, PT Perkebunan Nusantara III and PT Merpati Nusantara Airlines were rejected by the DPR. Minister Sugiharto maintained that while this target was important to cover the deficit, his team would prioritize on increasing the dividend revenue from Rp 8.9 trillion to Rp 12 trillion which consequently almost covered the target for budget revenue from state enterprises of Rp 12.4 trillion. Until late 2005, none of these targets were privatized (Kompas 29 October 2005).

In the 2006 fiscal year, the executive targeted a privatization receipt of Rp 3.5 trillion to cover the deficit. After long debates, the target was reduced to Rp 1 trillion only (Ministry
of Finance 2005; *Tempo*interaktif 22 June 2006). This was fully covered by the receipts from the privatization of PT PGN.

For the 2007 budget, the executive initially proposed Rp 2 trillion from privatization receipts. Through the budget debates, the target was then increased to Rp 3.3 trillion. Before its execution, the executive decided to increase it to Rp 4.3 trillion which also covered carry-over targets from the 2006 fiscal year (*Sinar Harapan* 21 February 2007; *Tempo*interaktif 20 February 2007). PT BTN (housing bank), PT Wijaya Karya (road construction), and PT Krakatau Steel (steel production) were among the main targets. However, the Privatization Committee and the DPR opposed the privatization of PT BTN considering its strategic function in providing credit for public housing (*Tempo*interaktif 01 March 2007). The executive then proposed PT BNI and PT Jasa Marga beside PT Wijaya Karya (*Tempo*interaktif 17 May 2007). In addition to that, PT Iglas, PT Cambirics Primissima, PT Jakarta International Hotel Development Tbk (JIHD), PT Atmindo, PT Intirub, PT Prasadha Pamunah Limbah Industri (PPLI), PT Kertas Blabak and PT Kertas Basuki Rahmat would also be privatized since the government had only minority shares in these enterprises. The main target was PT BNI (*BUMN* Online 27 June 2007; Detikcom 26 June 2007) and the DPR had approved the sale of 30 per cent of government shares in this bank (*Tempo*interaktif 07 March 2007). When an initial public offering was finally launched on the Jakarta Stock Exchange, the government could only get Rp 3.9 trillion, far below its target of at least Rp 7.2 trillion (Detikcom 13 August 2007). Until the time of writing, no other enterprises have been privatized. However, it will not be difficult for the executive to cover the remaining 10 per cent of the budget target.

Overall, the achievement in privatization during the SBY administration has been very limited. However, this limited achievement has not compromised fiscal sustainability. The executive has focused instead on restructuring state enterprises, a strategy which was expected to increase their dividend. Even since 2005, the executive has relied more on the issuance of state bonds than on pushing privatization to cover the budget deficit though it is still important.

What I can conclude from the discussion on fiscal policy reform is the ability of the SBY administration to adopt more policy reforms than his two predecessors. This was achieved
under a strong opposition from the DPR and other organized groups. Amidst this opposition, his administration has adopted several economic policy reforms on the revenue, spending, deficit and deficit financing sides of the budget. Meanwhile, privatization has progressed very slowly. However, the executive could push it forward when it needed to cover budget deficit such as in the case of PT PGN. It has also adopted important fiscal policy-related reforms such as the passage of Law 28/2007 and a significant fuel price increase. These contributed to increased fiscal sustainability and macroeconomic stability as a whole. Considering this achievement, Hill (2007:163) points to the return of prudent macroeconomic management as under the Suharto regime. With increased confidence, on 12 October 2006, the SBY administration amortized the remaining US$ 7.6 million of government debt to the IMF, resulting in the termination of the Post Program Monitoring and, more importantly, more independence in formulating economic policies (Bank Indonesia 2007:3, 145). This is an important achievement given that this debt was initially to be due in 2010.

5.2.2 Investment policy reform

Beside fiscal policy reform, the SBY administration has also had to struggle to push policy reform to improve investment climate. This is an important agenda for boosting economic growth which was still mainly consumption-driven. While investment performance has improved slightly since 2004, it is still far from sufficient to boost economic growth to be able to tackle unemployment and poverty.\(^{157}\) It seems clear that many investors are buying time given the many uncertainties in Indonesia, and despite SBY’s international campaign to attract investors. The reasons for this are as the Word Bank (2005c:24) and the Bank Indonesia (2007:5) have identified. At the top of these concerns are macroeconomic instability, regulatory uncertainty, and corruption.\(^{158}\) While the first concern has improved significantly, two other concerns remain so worrisome that immediate measures are urgently required.

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\(^{157}\) Investment performance has improved slightly during 2004 but then decreased again since 2005. For discussion on investment performance see Sen and Steer (2005:281); Soesastro and Atje (2005:14); Basri and Patunru (2006:298); Kuncoro and Resosudarmo (2006:10); Manning and Roesad (2006:147); and Lindblad and Wie (2007:13).

\(^{158}\) The other ones are tax rates, cost of finance, burdensome labor regulations, legal system or conflict resolution, tax administration, electric power unreliability, and crime, theft and disorder.
One clear example of regulatory uncertainty was the decision of the Constitutional Court to annul Law 20/2002 on Electricity and to revise some articles in Law 22/2001 on Oil and Gas. The annulment of the electricity law not only created legal uncertainty but also caused a legal vacuum. The state electricity provider, PLN, once again became both the regulator and the provider. This is a serious drawback since its monopoly over power provision prevents the electricity sector from improving, despite widespread complaints about the shortage of power supply (World Bank 2005c:38).

Meanwhile, the uncertainty of the regulation in the mining sector such as in oil and gas resulted in poor performance in this area. The decision of the Constitutional Court to annul some of the articles in Law 22/2001 created further uncertainty. Overall, mining contribution to investment, and therefore to economic growth, is still gloomy despite its huge potential. Cumbersome regulations primarily explain this. The Fraser Institute Report (2004, quoted in Aswicahyono and Hill 2004:298) shows that out of 53 countries, Indonesia ranks sixth in the Mineral Potential Index. However, in the Policy Potential Index, it ranks fourth lowest. This is in line with the report from PriceWaterhouseCoopers (2006) which puts regulatory conflict at the top of the concerns.\textsuperscript{159} When security issues in mining areas are considered as well, the prospect is even more uncertain.

How did SBY deal with these concerns? On many occasions, he maintained the importance of investment for boosting economic growth and his commitment to improving the investment climate. Through the RPJM and the RKP, SBY maintained the importance of investment as the prime mover of growth. His administration also set a target to increase investment by 8.1 per cent in 2005 and 15.2 per cent in 2006 or 18.9 per cent of GDP and 20.4 per cent of GDP respectively. While investment contribution to GDP growth has improved, it has not reached the expected level of at least the same as prior to the 1997 economic crisis. Even in mid 2005, it again showed a decreasing trend. Beside the above concerns, some analysts attribute this to the cabinet's poor direction in pushing economic reform, not to mention its poor performance in the field (Kuncoro and Resosudarmo

\textsuperscript{159} Other concerns are the tax system, overlapping jurisdiction between regions, illegal mining and the lacking of coordination among government departments (PriceWaterhouseCoopers 2006:5).
Taking these concerns into account, SBY made several breakthroughs. Maintaining macroeconomic stability was put at the top of the agenda, in line with investors' concern. This included a realistic exchange rate, low inflation, sufficient foreign reserves, realistic budget balance, and reduced debt. As I have discussed previously, he was ready to take bitter policy measures to accomplish fiscal reform. His reform initiatives brought about significant improvement in the macroeconomic stability, especially budget deficit and fiscal sustainability. Boosting investment will then rely on his administration's capacity to push regulatory reform, simplify license procedures, improve legal certainty, reform labor policy, and improve infrastructure (RKP 2005; RKP 2006). Some of these reform initiatives had to go through the DPR.

Realizing that solving these problems would normally require a long legislative process during which the DPR still had the potential to frustrate the executive, SBY succeeded in making many breakthroughs through employing different strategies. He issued numbers of high profile policy packages using government regulation, presidential decisions, presidential instructions, or presidential regulations. Such initiatives often have a more immediate effect than laws since the president does not need DPR approval. This is critical to fill the gap in the existing rules of the game especially in areas related to economic recovery. As I will discuss in the following paragraphs, this short-cut strategy often provoked strong opposition from the DPR and the people – despite the fact that they are constitutionally under the domain of the president – but SBY moved forward with his reform agenda.

For example, on 16 January 2005, the president issued Government Regulation No.3/2005 (or PP 3/2005) on the Provision and Use of Electricity Power. This was an important step in response to the annulment of Law 20/2002 on Electricity by the Constitutional Court. With such annulment, the previous law, Law 15/1985, was reinstalled. Since this was against the

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160 George Soros, the founder of the Open Society Foundation who also pays attention to Indonesian development, once expressed the same concern that macroeconomic instability and corruption in Indonesia have led to low investment in this country compared to, for example, Singapore (Tempointeraktif 14 December 2006).
expectation to boost investment, the executive maintained that it prefers revising the annulled law to reinstalling the old one (Tempointeraktif 16 December 2004). This worried some investors since there was no legal protection for their ongoing businesses. Through the Indonesian Electricity Community, they requested the government to provide a legal guarantee over the existing contracts (Tempointeraktif 17 December 2004). Realizing that revising the annulled law could take a long process and that the re-establishment of Law 15/1985 would be a real drawback, the president then took a short cut by issuing PP 3/2005. The PP maintains the spirit of Law 20/2002 by endorsing private sector and local government participation in the provision of energy in partnership with the PLN. Though it still lacks the competition incentive as a key trigger to improve electricity performance, its introduction could at least fill the gap in the PLN’s power supply capacity.

In the Indonesian legal hierarchy, the PP must refer to and is an implementation of law (UU). Realizing that some articles in PP 3/2005 are against Law 15/1985 and instead very similar to the Law 20/2002 which was already annulled, the DPR and some elements in the society posed their opposition (Suara Pembaruan 05 February 2005). They requested the president to review the PP and accelerate the process of drafting the new bill and submit it to the DPR for further debate. However, until the time of writing, the president still maintains the PP 3/2005. Efforts to establish a new law are still underway.

After that, following the Infrastructure Summit in January 2005, SBY issued Presidential Rule No.36/2005 on the Land Provision for Public Interest (PERPRES 36/2005) in May 2005. Before that, Indonesia has no such legal provision as the ‘eminent domain’ (McLeod 2005b:146). With this rule in place, the government now has a legal basis for appropriating private land for as many as 21 categories of public interest. This was also expected to provide a stronger legal assurance for investors in dealing with land acquittal and compensation and at the same time protect the people from misappropriation by the government. This was very important to encourage private sector participation especially in infrastructure development, an area where the government only had limited resources.

According to the MPR Decision No III/MPR/2000, the hierarchy of legal product is in the following order: (1) Constitution (UUD 1945), (2) MPR Decision (TAP MPR), (3) Law (UU), (4) Government Regulation in Lieu of Law (PERPU), (5) Government Regulation (PP), (6) Presidential Decision (KEPPRES), and (7) Local Regulation (PERDA). Despite this stipulation, the president sometimes uses presidential instruction or presidential rule to push policy agenda.
Given that land acquittal and compensation are a very sensitive issue, opposition from the people spread throughout the country. Public opposition centered on the fact that the PERPRES would justify appropriation of land with only poor compensation which could compromise their right and access over the land (Gatra 12 June 2005; Kompas 09 June 2005; Kompas 09 July 2005; Pikiran Rakyat 12 June 2005; Suara Merdeka 06 July 2005; Tempo Interaktif 05 June 2005). Moreover, the PERPRES would only benefit the government and investors at the cost of the people. Through Committee II, the DPR also expressed its strong opposition. However, as in other cases previously discussed, SBY maintained this PERPRES.

Still related to investment promotion, the SBY administration also adopted the amendment to the customs law through Law 17/2006. This revised Law 10/1995 to make it up to date. It is expected to enhance law enforcement, transparency, and accountability in public service delivery, to support economic development in the global village, to endorse exports and imports, and to combat smuggling. The executive adopted this amidst opposition from the DPR.

One other important achievement of the SBY administration in the investment area is the passage of the new investment law, Law 25/2007. This is the most significant achievement in the investment area. The Megawati administration had initiated this in 2003. SBY then ordered his team to rewrite the draft, putting emphasis on registration rather than approval (Tempo Interaktif 12 January 2005), and submitted it to the DPR on 21 March 2006. During the debates, the DPR expressed strong opposition on many issues especially regarding equal treatment for domestic and foreign investors, incentives and facilities for (foreign) investors, and the role of the local government (Investor Daily 22 February 2007). PKS demanded the executive to base the content of the draft on Article 33 of the Constitution (PKS 2007). Meanwhile, PDIP demanded the executive to clarify the scope of incentives and facilities offered to investors and the role of the local government (Kompas 16 January 2007). The same kind of opposition also came from PAN (DPR-RI 12 October 2006). Amidst this opposition, the law was finally passed on 29 March 2007.

The Law 25/2007 was broadly welcomed by the international business community though other concerns remained (Wyatt 2007). Among the important features of the law are: (1)
equal legal status and treatment for both domestic and foreign investors; (2) stronger protection for investors (including protection against nationalization and expropriation and for fair compensation at market price in the case of nationalization); (3) the use of an international arbiter for dispute resolution involving government and foreign investors; (4) stronger property right provision with extended land use rights for up to 95 years (up from the current maximum of 35 years) and building rights for up to 80 years (up from 30 years); (5) supportive immigration regulations for foreign workers through giving two year residence status with multiple travel visa and offering permanent residence status for those living continuously for at least two years; and (6) numerous tax incentives (such as tax holidays for pioneer industries, reduction of income tax, reduction or exemption of import duties and value added taxes for capital goods and raw materials, and reduced property tax). This terminated the discriminatory and distorting investment laws, Law 1/1967 on Foreign Investment (revised through Law 11/1970) and Law 6/1968 on Domestic Investment (revised through Law 12/1970).

Following the passage of the new investment law, SBY planned to invite more investors by creating special economic zones. Hill (2007:151) argues that this initiative is another shortcut to avoid difficulty in achieving first-best or economy-wide liberalization. SBY had had this on his agenda since March 2006. The delay was mainly because of the requirement for a particular law for the creation of special economic zones. Considering that it would be a long process to obtain DPR approval, he initially planned to take a short-cut by issuing a government regulation (PP). However, his plan changed since this is legally weak and no investors would respond to this initiative. Therefore, he finally issued a government regulation in lieu of a law, PERPU 1/2007.162 This was the first time in Indonesia’s history that a president declared a decree of an economic policy nature. The underlying argument was the compelling nature of the initiative, especially to guarantee legal certainty for investors, which could have been at risk if he had followed the normal procedure through

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162 The issuance of PERPU is based on Article 22 of the Constitution: (1) should exigencies compel, the President shall have the right to establish government regulations in lieu of laws; (2) such government regulations must obtain the approval of the DPR during its next session; (3) should there be no such approval, these government regulations shall be revoked.
the DPR (Antara 24 May 2007; Hukum Online 21 May 2007). The DPR again voiced its opposition but SBY went ahead with his agenda.

If there is one policy reform that SBY has failed to push, it is the amendment to the labor law. This is very important given that Indonesia’s labor policy is still in general less attractive for investors than other neighboring countries. To push reform in this area, at the end of her administration, Megawati had proposed a further revision to Law 13/2003 on the Workforce (Kompas 17 September 2004). SBY took the same position with the objective of creating a new balance between the interests of employers and employees. Among the crucial issues here are severance pay, minimum wage and restriction of short-term contracts and outsourcing which all gave the impression of an over-protected labor market in Indonesia at the cost of employers. As this had long burdened employers, SBY’s main intention was not only to lift the constraints up but also to create a more competitive job market in order to be able to combat unemployment and poverty. For workers, the revision was considered to risk their already vulnerable position. Therefore, many labor unions with their thousands of members mounted strong opposition to the plan. On 1 May 2006, for example, the commemoration of International Labor Day in Jakarta and other big cities was marked by large scale protests involving more than a hundred thousand workers. The protests were especially directed toward the DPR realizing that this was the place where legislation is made. Faced with the scale and intensity of labor opposition, the executive withdrew its draft in April 2006 (Kompas 09 April 2006). The delay of reform in this area along with tax reform has deteriorated business perception on Indonesian labor and tax policies (World Bank 2007b:22).

163 The executive used the performance of exports in certain areas as its justification to immediately create special economic zones. For example, the value of exports from Bintan and Batam has declined since the annulment of the bonded zone status in these areas in 2001 (Batom Pos 22 September 2006; Batam Pos 16 March 2007). Only immediate action could stop this from worsening, justifying the issuance of PERPU on practical ground.

164 The World Bank and International Finance Corporation (2005, 2006) report that, using the Employment Rigidity Index, Indonesia is among Asian countries with more restrictive labor markets (or higher Employment Rigidity Index) together with India, Cambodia and Vietnam. This stands in contrast to other countries such as Korea, China, the Philippines, Thailand, Malaysia and Singapore which have less restrictive labor markets. In terms of ease of doing business, Indonesia ranked 131 in 2006 and 135 in 2007 out of 175 countries surveyed. Its severance rate is also among the costliest (Aswicahyono and Hill 2004:291).

165 That labor reform of this type will find strong opposition and take longer time to accomplish is not surprising. Comparative experiences show the same trend. For example, The World Bank and International Finance Corporation (2005:22) report that it took 11 years in Germany and 9 years in Netherlands for this type of reform to succeed.
Considering the ongoing progress and all that has been achieved, the SBY administration has brought the country back on track toward recovery after the worrying uncertainty prior to his election. Though several challenges remain, his administration shows more promise of recovery from the impacts of the crisis and of bringing Indonesia to a better future (Green 2007). In the area of investment, for example, Indonesia’s investment rating has moved upward from the non-investment grade (below BB+ in S&P Rating) closer to a reasonable investment grade (BBB- and above), that is, back to the pre-crisis level (Bank Indonesia 2007:146). This cannot be separated from SBY’s effort to push policy reform in many areas, some of which have been discussed previously. This achievement is creditable given the scale of opposition he has had to face from both the DPR and other organized groups.

Looking back and comparing these achievements to those of the Megawati and especially Wahid administrations, the general conclusion must be that the SBY administration has achieved more economic policy reforms than the two preceding administrations, especially given the scale of opposition. The ways in which reforms were adopted are also different. Wahid and Megawati could only legislate through the DPR while SBY combined this route with high profile policy instruments which triggered even stronger opposition. The next section will discuss this variation.

5.3 The effect of executive strength

To understand the achievements in economic policy reform under the SBY administration, the policy-making context is once again important. Compared to both Wahid and Megawati, SBY has higher executive strength, the highest among all post-Suharto presidents. This comes from the combination of constitutional protection over the president’s security of tenure and the consolidated partisan support in the DPR. It is this institutional underpinning which substantially explains why the SBY administration was able to adopt so many significant economic policy reforms despite strong political opposition, especially from the DPR but also from organized groups.
5.3.1 Executive strength under SBY

Similar to Megawati and Wahid, SBY only has moderate legislative (veto and decree) powers. His only advantage compared to his two predecessors is the fact that he is the first directly elected president in Indonesia. With the tightening of the impeachment process, this gives him more security of tenure and a degree of freedom from political pressure.

The introduction of direct presidential election is especially interesting and SBY is the first president who enjoys this advantage. It has brought many significant effects, three of which are the most important (Singh 2003:437-8). Firstly, the MPR has lost its power as an arbitrary institution to elect the president and vice president. With the removal of its power to lay down the GBHN, the MPR has very limited space to play with the president even in the impeachment process which is now constitutionally more difficult and legally bound. Of immediate effect for the 2004 presidential election was the fact that there was no longer room for horse-trading practices. All have made the president at least more independent of the MPR as well as the DPR.

Secondly, the introduction of the direct presidential election strengthens the workings of checks and balances as under a pure presidential system. As the president is now no longer responsible to the MPR, he or she has more political leverage to bargain with the DPR. Even in certain situations, the potential for a directly elected president to stand up against the DPR has been increased and the president who has the willingness to do so can turn this potential into a powerful force. This is the situation which distinguishes SBY from Megawati and especially Wahid. He even has the chance to be an imperial president as he inherits a direct mandate from the people in addition to constitutional powers. Such arrangements also open the chance for the problem of dual legitimacy since both the president and the DPR constitutionally represent the people.

Thirdly, direct presidential election also significantly reduces the role of self-interested actors in the process of cabinet formation. This applies mainly to political parties. While parties having significant seats in the DPR can still bargain with the elected president, especially in the process of cabinet formation as in the case of Wahid and Megawati, the
chances are now more limited for them to dictate to the president. Constitutionally, a directly elected president such as SBY can free himself from other forces and act as an independent person. The party’s political leverage is still important but it is not necessarily converted into the power to compromise presidential power. The president will still need legislative support from the DPR to win the policy agenda and, given his strong constitutional mandate, he can engineer a more limited but reliable partisan support in the parliament. The chance for the establishment of a more professional cabinet is also now wide open.

Though having strong constitutional powers, SBY also needed to establish a legislative majority to achieve any legislative agenda. In this respect, the restoration of the president’s security of tenure enabled him to establish a more consolidated coalition. This is not an easy job given two things. First, like Megawati and Wahid, he comes from and is supported by a minor party. PD only has 56 out of 550 seats in the DPR or 10.18 per cent. Second, the 2004 general election resulted in a more fragmented parliament with at least seven major parties having more than 8 per cent of DPR seats (Sherlock 2004:6-7; see also Appendix 5). As shown in Table 5.2, there are ten partisan blocks which will affect the dynamics and performance of the policy-making process. Therefore, SBY had to be extra careful in choosing his coalition allies to be able to deal with this new partisan configuration.
Table 5.2 Composition of fraction in DPR, 2004-2009

<table>
<thead>
<tr>
<th>No.</th>
<th>Fractions</th>
<th>Number of seats</th>
<th>Percentage of seats</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>GOLKAR (127 GOLKAR + 2 PKPB)</td>
<td>129</td>
<td>23.45</td>
</tr>
<tr>
<td>2</td>
<td>PDIP</td>
<td>109</td>
<td>19.81</td>
</tr>
<tr>
<td>3</td>
<td>PPP</td>
<td>58</td>
<td>10.54</td>
</tr>
<tr>
<td>4</td>
<td>PD (56 PD + 1 PKPI)</td>
<td>57</td>
<td>10.36</td>
</tr>
<tr>
<td>5</td>
<td>PAN</td>
<td>53</td>
<td>9.63</td>
</tr>
<tr>
<td>6</td>
<td>PKB</td>
<td>52</td>
<td>9.45</td>
</tr>
<tr>
<td>7</td>
<td>PKS</td>
<td>45</td>
<td>8.18</td>
</tr>
<tr>
<td>8</td>
<td>BPD (11 PBB + 4 PPK + 3 PP + 1 PPD + 1 PNIM)</td>
<td>20</td>
<td>3.63</td>
</tr>
<tr>
<td>9</td>
<td>PBR</td>
<td>14</td>
<td>2.54</td>
</tr>
<tr>
<td>10</td>
<td>PDS</td>
<td>13</td>
<td>2.36</td>
</tr>
<tr>
<td></td>
<td>Total</td>
<td>550</td>
<td>100</td>
</tr>
</tbody>
</table>

Note: In early 2007, PP joined the PD fraction, increasing the seats of this fraction to 60.


Besides this new configuration, SBY also had to face a new polarization in the DPR between the National Coalition and the People’s Coalition in the early months of his administration.\(^{166}\) He then established an oversized cabinet on 21 October 2004 and named it the United Indonesia Cabinet or Kabinet Indonesia Bersatu (see Appendix 6). It consisted of thirty-six members incorporating figures from various backgrounds of parties, profession and ethnic with a relatively balanced proportion between portfolios given to parties (53 per cent) and to non-partisan professionals (47 per cent). For some, this was a big disappointment, especially referring to the composition of economic team where Aburizal Bakrie and Jusuf Anwar were the main target of criticism (Tempointeraktif 21 October 2004; Tempointeraktif 22 October 2004; Qodary 2005; Soesastro and Atje 2005:6).\(^{167}\)

\(^{166}\) Included in the National Coalition were parties supporting the Megawati-Muzadi package in the presidential race such as GOLKAR, PDIP, PPP, PBR, PDS, PKPB and PNIM with 321 seats in total or 58.4 per cent of DPR seats. While the People’s Coalition consisted of PD, PKS, PBB, PPK, PKPI, and PPDI which supported SBY-Kalla package with only 121 seats in DPR or 22 per cent (Soefihara 2005:149). Standing in the middle as neutral force were PAN and PKB.

\(^{167}\) Criticism of Bakrie was especially centered on the fact that he runs such extensive businesses that putting him at the position of economic portfolio would risk the whole country's economy. Some of his business operations were actually in trouble, the clearest and latest case is LAPINDO's hot mud eruption in East Java. His transfer to the social welfare post through first cabinet reshuffle did not change these concerns much as he is still in the inner circle of the (vice) president but at least it gave SBY more control over economic running through the appointment of Boediono.
However, such criticism must be put into perspective and cabinet composition is best understood in the context of SBY’s vulnerability in the legislative arena. His coalition is indeed the best reflection of the political configuration at that time. As shown in Table 5.3, his coalition has 74.26 per cent of the DPR seats, involving all major parties except PDIP.\(^{168}\)

### Table 5.3 Composition of the United Indonesia Cabinet

<table>
<thead>
<tr>
<th>No</th>
<th>Affiliation</th>
<th>Total vote (%)</th>
<th>Total DPR seat (%)</th>
<th>Cabinet portfolio (number)</th>
<th>Cabinet portfolio (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>GOLKAR</td>
<td>21.58</td>
<td>23.27</td>
<td>3</td>
<td>8.3</td>
</tr>
<tr>
<td>2</td>
<td>PD</td>
<td>7.45</td>
<td>10.36</td>
<td>3</td>
<td>8.3</td>
</tr>
<tr>
<td>3</td>
<td>PAN</td>
<td>6.44</td>
<td>9.45</td>
<td>2</td>
<td>5.5</td>
</tr>
<tr>
<td>4</td>
<td>PKB</td>
<td>10.57</td>
<td>9.45</td>
<td>2</td>
<td>5.5</td>
</tr>
<tr>
<td>5</td>
<td>PKS</td>
<td>7.34</td>
<td>8.18</td>
<td>3</td>
<td>8.3</td>
</tr>
<tr>
<td>6</td>
<td>PBB</td>
<td>2.62</td>
<td>2.0</td>
<td>2</td>
<td>5.5</td>
</tr>
<tr>
<td>7</td>
<td>PPP</td>
<td>8.15</td>
<td>10.55</td>
<td>3</td>
<td>8.3</td>
</tr>
<tr>
<td>8</td>
<td>PKPI</td>
<td>1.26</td>
<td>1.0</td>
<td>1</td>
<td>2.8</td>
</tr>
<tr>
<td>9</td>
<td>Non-partisan</td>
<td>..</td>
<td>..</td>
<td>17</td>
<td>47</td>
</tr>
<tr>
<td>Total</td>
<td></td>
<td>65.41</td>
<td>74.26</td>
<td>36</td>
<td>100</td>
</tr>
</tbody>
</table>

*Source: Author’s calculation from www.dpr.go.id and www.kpu.go.id.*

If we look at the partisan configuration in legislative arena, namely the fractions, SBY has sufficient partisan support. As shown in Table 5.4, seven out of ten fractions in the DPR joined the coalition with overall 75.27 per cent of the DPR seats, giving SBY a sufficient capital to govern effectively. The election of Jusuf Kalla as the chair of GOLKAR in December 2004 made his partisan support even more consolidated.\(^{169}\) Meanwhile, three fractions stayed outside the coalition with PDIP declaring itself the opposition party. Should the other two fractions join PDIP, their share will be large enough to be a significant opposition with overall 24.7 per cent of the DPR seats.

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\(^{168}\) This party composition stands until the time of writing. SBY has undertaken two cabinet reshuffles without much opposition from his allies. Of special concern was to consolidate PKB’s support by recruiting its true figure-heads such as Erman Suparno and Muhamad Lukman Edy (see Appendix 4).

\(^{169}\) Jusuf Kalla was not formally supported by GOLKAR in the presidential race. GOLKAR instead supported the package of Wiranto-Sollahuddin Wahid who only got 22.15 per cent of vote in the first-round election. Therefore, as far as GOLKAR is concerned, the composition as shown in table 4 and 5 was valid only after the election of Jusuf Kalla as the chair of GOLKAR on 19 December 2004 which also automatically dismissed the National Coalition.
Table 5.4 Fractions in SBY’s coalition cabinet, 2004-2007

<table>
<thead>
<tr>
<th>No.</th>
<th>Fractions</th>
<th>Number of DPR seats</th>
<th>Percentage of DPR seats</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>GOLKAR</td>
<td>129</td>
<td>23.45</td>
</tr>
<tr>
<td>2</td>
<td>PPP</td>
<td>58</td>
<td>10.54</td>
</tr>
<tr>
<td>3</td>
<td>PD</td>
<td>57</td>
<td>10.36</td>
</tr>
<tr>
<td>4</td>
<td>PAN</td>
<td>53</td>
<td>9.63</td>
</tr>
<tr>
<td>5</td>
<td>PKB</td>
<td>52</td>
<td>9.45</td>
</tr>
<tr>
<td>6</td>
<td>PKS</td>
<td>45</td>
<td>8.18</td>
</tr>
<tr>
<td>7</td>
<td>BPD</td>
<td>20</td>
<td>3.63</td>
</tr>
<tr>
<td></td>
<td>Total</td>
<td>414</td>
<td>75.27</td>
</tr>
</tbody>
</table>

Source: Author’s calculation.

Until the end 2007, SBY had undertaken two cabinet reshuffles. While the process involved ripples of opposition from the parties whose representatives were expelled from the posts, SBY could manage the process decisively. His aim was twofold: maintaining a more consolidated and reliable coalition support in the legislative arena and putting more professional figures in his cabinet. Contrary to what happened under Wahid when the cabinet reshuffle triggered opposition from political parties resulting in a shaky coalition, SBY could still maintain coalition stability with his allies. Even the replacement of figures from major parties such as Sugiharto of PPP and Yusril Ihza Mahendra of PBB only triggered limited opposition.\(^\text{170}\) Above any other reasons, it is because of the institutional advantage SBY enjoyed as he had constitutional protection over security of tenure and direct mandate from the people as the first directly elected president. This limits the parties’ room to maneuver against president’s survival.

Looking at the combination of constitutional power and partisan support, it can be concluded that SBY is indeed a strong president. Though he also has only moderate legislative powers like his predecessors, the constitutional protection over security of tenure and consolidated partisan support in the DPR give him sufficient political capital to adopt difficult economic policy reform. The following section connects this argument to the

\(^{170}\) In the case of the replacement of Yusril Ihza Mahendra, PBB initially threatened to withdraw from the coalition but then decided to stay. It acknowledged that the cabinet reshuffle is SBY’s prerogative which it can only accept (Antara News 07 May 2007)
achievements in fiscal policy reform and investment policy reform of the SBY administration so far, followed by fuel subsidy reform as the case study.

5.3.2 Fiscal policy reform

As discussed previously, the SBY administration has adopted many significant reforms in the fiscal policy area. In the budget-making process, the executive has pursued reform initiatives amidst strong opposition from the DPR. A clear example is the revision of the 2005 budget. The annual budget was passed by the outgoing administration in late 2004. In response to the catastrophic tsunami in Aceh and Nias which required huge costs for rescue, reconstruction and rehabilitation, the DPR urged the executive to revise the budget but the latter rejected this request (Soesastro and Atje 2005:118). A quick response from the international community had helped ease the government's burden so that the annual budget could go through without major revision. However, at the same time, the international oil price had increased to a level beyond the target set in the budget law. This was also accompanied by the Rupiah depreciation. SBY was urged to immediately revise the budget by taking firm action especially to cut the fuel subsidy.

After a long debate, the executive and the DPR accomplished the first budget revision in June 2005. All key budget assumptions were adjusted, the most significant of which was the international oil price and the Rupiah exchange rate (see Table 5.5). The adjustment was made so as not to compromise the budget deficit target of -0.8 per cent of GDP despite a slight increase in the nominal amount (from Rp 17.4 trillion to Rp 20.3 trillion). Given the uncertain conditions at that time, many expressed concerns about the revised budget as neither reflecting the real condition nor anticipating it (Tempo*aktif 27 May 2005; Tempo*aktif 11 August 2005).

These concerns soon materialized and the revision was only valid for one month. As early as August 2005, almost all the underpinning assumptions needed further revision. The international oil price reached US$ 50/barrel while the Rupiah exchange rate reached Rp 9,500/US dollar. The interest rate also increased to 8.25 per cent and inflation rose to 8 per
cent (Ministry of Finance 2005). This forced the government to undertake another revision, this time even more significant, especially of the oil price and Rupiah exchange rate which then affected all the budget posts. After heated debates with the DPR’s Budget Committee, an agreement was reached to revise all budget assumptions except the target for GDP growth, as shown in Table 5.5.

Though the executive and the DPR could work out a compromise over the budget target, opposition was sustained on the effects of such changes on budget allocation. Budget revenue increased to 19.6 per cent of GDP while spending rose to 20.6 per cent of GDP. The fuel subsidy increased significantly to 3.8 per cent of GDP. This time, the volume of budget deficit could no longer be maintained at the initial level of -0.8 per cent of GDP. It increased to -1.0 per cent of GDP. Based on a rough calculation, the international oil price increase alone had contributed Rp 5.6 trillion or 0.17 per cent of GDP to this scale of deficit. The figure was even higher than this given the Rupiah depreciation at the same time.

<table>
<thead>
<tr>
<th>Assumptions</th>
<th>Budget</th>
<th>First revision</th>
<th>Second revision</th>
</tr>
</thead>
<tbody>
<tr>
<td>Growth (%)</td>
<td>5.4</td>
<td>6.0</td>
<td>6.0</td>
</tr>
<tr>
<td>Inflation (%)</td>
<td>5.5</td>
<td>7.5</td>
<td>8.0</td>
</tr>
<tr>
<td>Exchange rate (Rupiah to US$)</td>
<td>8,600</td>
<td>9,300</td>
<td>9,500</td>
</tr>
<tr>
<td>Oil price (US$/barrel)</td>
<td>24</td>
<td>45</td>
<td>50.6</td>
</tr>
<tr>
<td>Oil production (thousand barrel/day)</td>
<td>1,125</td>
<td>1,125</td>
<td>1,075</td>
</tr>
<tr>
<td>Interest rate (%)</td>
<td>6.5</td>
<td>8.0</td>
<td>8.3</td>
</tr>
<tr>
<td>Revenue (% of GDP)</td>
<td>17.4</td>
<td>18.7</td>
<td>19.6</td>
</tr>
<tr>
<td>Expenditure (% of GDP)</td>
<td>18.2</td>
<td>19.5</td>
<td>20.6</td>
</tr>
<tr>
<td>Deficit (% of GDP)</td>
<td>-0.8</td>
<td>-0.8</td>
<td>-1.0</td>
</tr>
<tr>
<td>Domestic financing (% of GDP)</td>
<td>1.7</td>
<td>1.1</td>
<td>1.2</td>
</tr>
<tr>
<td>Foreign financing (% of GDP)</td>
<td>-0.9</td>
<td>-0.3</td>
<td>-0.2</td>
</tr>
</tbody>
</table>


To anticipate the worsening effect of these changes to the 2005 budget, the president proposed to cut the fuel subsidy (discussed later). This triggered strong opposition from the DPR, especially from PDIP. Since no compromise could be reached on this issue, the final decision on the second budget revision had to be made through voting. In the floor voting, the executive’s proposal was supported by GOLKAR, PD, PPP, PAN, PKS, BPD and PBR fractions. Only PDIP opposed the revised budget while PKB abstained (Hukum Online 28 September 2005; Kompas 28 September 2005). This was an early sign of the president’s determination in the policy-making process though some criticized that this response was too late. The protection over the president’s security of tenure supported by a consolidated partisan support enabled SBY to achieve this.

For the establishment of the 2006 and 2007 budgets, the executive again had to face DPR opposition even in areas as technical as setting macroeconomic assumptions such as economic growth rate, inflation, interest rate, the Rupiah exchange rate, and the oil price. In this area, despite the lack of competence, the DPR played an assertive role in criticizing the set targets leading to significant changes in almost all budget items (Detikcom 28 October 2005; Kompas 28 October 2005; Tempointeraktif 23 August 2005). It simply wanted to project itself as an independent body, no longer the executive’s rubber stamp despite the lack of economic literacy. In debating the 2006 budget, for example, it criticized the set targets as either too optimistic or expansionary, so the executive had to revise it (Suara Merdeka 19 August 2006). Special attention was given to the assumption of the oil price which was set far below the actual price in the international market (Detikcom 23 August 2005). So too was the case for the 2007 budget (Bisnis Indonesia 29 August 2006; Suara Karya 29 August 2006; Suara Pembaruan 29 August 2006).

In response to DPR criticism, the executive again showed its determination. It insisted that it could only revise the assumptions in consultation with the DPR and the Central Bank as it is supposed to; it could not unilaterally do this. Therefore, it invited the DPR to undertake further deliberation to work out more realistic targets (Suara Merdeka 31 August 2005). For the 2007 budget, the executive even insisted on maintaining the proposed targets

\[172\] The executive had to be extra careful in setting the oil price assumption as it would affect the volume of fuel subsidy as well as the transfer to the regions under the profit-sharing scheme. Many analysts criticized the executive for setting a lower-than-international oil price as part of its strategies to reduce transfers to the regions (Pikiran Rakyat 19 August 2005).
amidst criticism from the DPR that the targets were either too optimistic in one sense or too conservative in another (Tempointeraktif 05 September 2006). This included the target for the oil price which was set far below the actual oil price in the international market. This is another example of how the DPR could no longer dictate to the executive on technical issues like setting budget assumptions, for which the executive is considered to be more competent. Due to the executive’s persistence, the overall targets set for the 2006 and 2007 budgets became a more reliable instrument in bringing about recovery. Table 5.6 summarizes the budget targets.

Table 5.6 Summary of the annual budgets, 2005-2007

<table>
<thead>
<tr>
<th>Indicators</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Proposal</td>
<td>Budget</td>
<td>Proposal</td>
</tr>
<tr>
<td>Growth (%)</td>
<td>5-5.5</td>
<td>5.4</td>
<td>6.2</td>
</tr>
<tr>
<td>Inflation (%)</td>
<td>5-6</td>
<td>5.5</td>
<td>7</td>
</tr>
<tr>
<td>Exchange rate (RP to US$)</td>
<td>8,400-8,600</td>
<td>9,400</td>
<td>9,900</td>
</tr>
<tr>
<td>Oil price (US$/barrel)</td>
<td>22-24</td>
<td>24</td>
<td>40</td>
</tr>
<tr>
<td>Oil Production (thousand barrel/day)</td>
<td>1,100</td>
<td>1,125</td>
<td>1,075</td>
</tr>
<tr>
<td>Interest rate (%)</td>
<td>6.5-7.5</td>
<td>6.5</td>
<td>8</td>
</tr>
<tr>
<td>Revenue (% of GDP)</td>
<td>17.2</td>
<td>17.4</td>
<td>18.0</td>
</tr>
<tr>
<td>Expenditure (% of GDP)</td>
<td>18</td>
<td>18.2</td>
<td>18.7</td>
</tr>
<tr>
<td>Deficit (% of GDP)</td>
<td>0.8</td>
<td>0.8</td>
<td>0.7</td>
</tr>
<tr>
<td>Domestic financing (% of GDP)</td>
<td>1.6</td>
<td>1.7</td>
<td>1.7</td>
</tr>
<tr>
<td>Foreign financing (% of GDP)</td>
<td>-0.8</td>
<td>-0.9</td>
<td>-1.0</td>
</tr>
</tbody>
</table>


Another difficult challenge that SBY had to cope with was when the executive and the DPR debated budget revenue and other reform measures in this area. For example, in debating the 2006 budget, the PDIP Fraction rejected the executive’s plan to increase budget revenue.
from tax receipts since that could compromise business prospects (Suara Merdeka 18 August 2005). Instead, it demanded the tax office improve tax administration by broadening tax coverage. Other fractions also criticized the tax revenue target as too conservative given the still low tax ratio, that is, 13.4 per cent GDP in the draft budget (Detikcom 23 August 2005).

In response to the DPR’s criticism, the executive then made some adjustments. After a long debate, an agreement was finally reached to increase tax revenue to 13.7 per cent of GDP. Non-tax revenue including dividends from the state-owned enterprises was also increased significantly from 4.4 per cent of GDP in the draft budget to 6.8 per cent of GDP. This led to an overall increase in budget revenue from 18 per cent of GDP to 20.6 per cent of GDP. The case is also true for the 2007 budget.

A more daunting challenge than setting revenue targets was how to meet these targets. Improving tax administration was one such strategy and this has helped the executive increase tax receipts. The remaining challenge was how to push tax policy reform. In this respect, the SBY administration adopted further reform in tax arrangement and procedure by the passage of Law 28/2007. This is one of the three tax laws proposed by SBY for further amendment.173

The passage of Law 28/2007 itself was far from easy. It took around two years before it was finally passed. The most crucial issue which took up the longest process in the debate was how to maintain the balance of power between tax officers and tax payers.174 The executive rejected the DPR’s proposal to separate the Directorate General of Tax from the Ministry of Finance; it preferred to empower the existing system. In addition, the proposal from the PKS and PAN fractions to establish an independent Tax Revenue Committee to replace the Directorate General of Tax was also rejected by the executive (Antara 19 June 2007; Hukum Online 06 June 2007; Hukum Online 20 June 2007; Sinar Harapan 19 June

173 The other two are Law 17/2000 on Income Tax and Law 18/2000 on Value Added and Luxury Taxes which are still in the process of debate.

174 Concerns over this issue were accommodated, for example in Article 25 of the law. Tax payers are required to pay an additional 50 per cent of the amount which they have to pay if their note of objection is refused by the tax office. The penalty is waived if their objection is accepted by the tax office. For more detailed information see Article 25 of Law 28/2007 (Bisnis Indonesia 24 March 2007; Bisnis Indonesia 27 March 2007).
GOLKAR and PD stood behind the executive. It was finally agreed only to establish the Tax Supervisory Committee to help the Minister of Finance improve tax administration. In response to the executive’s opposition to establish a separate Tax Revenue Committee, the PAN fraction sent a note of objection to the plenary session but it could not stop the approval of the law.

The passage of this law is another example of the effect of executive strength. During the debate, the executive maintained its agenda against opposition from the DPR. With protected tenure and strong partisan support, the executive could distance itself from the pressure of self-interest groups such as the Indonesian Chamber of Commerce (KADIN) which actively involved in this process through its proxy in the DPR. Even when the DPR as a whole posed opposition to some articles as in the early stage of the debate, the executive through the Minister of Finance maintained that it had no compelling need to approach the DPR and moved forward with the initial plan (Kompas 27 March 2007; Kompas 10 July 2007; Kompas 05 September 2007). Besides the presence of constitutional protection over the president’s security of tenure which gives the executive a sense of freedom from the opposition, SBY also had a consolidated partisan support. GOLKAR and PD as well as other fractions joining the coalition always supported president’s agenda though they sometimes mounted opposition during debates.

On the spending side, the SBY administration also adopted reform in the face of strong opposition from the DPR and organized groups. One case was the allocation for education expenses. Article 31 of the Constitution and Law 20/2003 on the National Education System require that ‘the state shall prioritize the budget for education to a minimum of 20 per cent of the National Budget (APBN) and of the Regional Budget (APBD) to fulfill the needs of implementation of national education’. This is a difficult condition that the government has still not yet met. Because of this, in both the 2006 and 2007 fiscal years, the executive had to face opposition from both the DPR and the people. To make things worse, the Constitutional Court partly annulled the approved budget bill unless education spending was increased.

For the 2006 fiscal year, through an initial deliberation with the DPR, the executive initially agreed to allocate 12 per cent of the national budget to education. However, through the
budget draft and during the debate, the executive maintained that it could only allocate 9.1 per cent of the budget for education spending. This triggered opposition from several legislators. In their opinion, under this arrangement, the 2006 budget was partly unconstitutional. They considered the decision of the Constitutional Court on 19 October 2005 which required the government to revise the education allocation in the 2005 budget. For the same reason, 45 legislators submitted a note of objection to the 2006 budget law to the president (Detikcom 29 October 2005; Suara Karya 29 October 2005). However, the president and his team decided to go ahead with the approved budget given the budget constraints. As predicted, the Constitutional Court again issued the same decision in March 2006 (Tempointeraktif 22 March 2006).

To respond to this decision, the executive offered three options to the DPR during the debates for budget revision (Pikiran Rakyat 13 June 2006). First, the education spending could be increased to 12.6 per cent but the government would have to increase electricity charges, increase the budget deficit to 1.3 per cent of GDP, remove all infrastructure expenses and remove all spending for the reconstruction and rehabilitation of Yogyakarta and Central Java following the earthquake in May 2006. Second, it would increase the education spending slightly above the current level with an additional Rp 3 trillion but the government would have to allocate another Rp 10.9 trillion for the electricity subsidy and Rp 3 trillion for infrastructure spending, increase the budget deficit to 1.3 per cent of GDP and remove the reconstruction and rehabilitation expenses for Yogyakarta and Central Java. Third, it would increase the education spending to 10 per cent of the national budget with an additional Rp 5 trillion, allocate Rp 10.9 trillion for the electricity subsidy and Rp 3 trillion for infrastructure spending which would cause the budget deficit increase to 1.3 per cent of GDP and the removal of the reconstruction and rehabilitation spending for Yogyakarta and Central Java. Considering that all these options would create more problems than they solved, the DPR gave up on its request. What is also important is the fact that the DPR could no longer manipulate populist sentiment. This is significantly because of the presence of the constitutionally protected security of tenure and sufficient partisan support for the president.

175 This decision can be accessed at http://www.mahkamahkonstitusi.go.id (accessed 02 September 2007).
The same is also true for the 2007 fiscal year. In the 2007 draft budget, the executive only allocated 10.3 per cent of state spending to education. This triggered opposition from many fractions especially PDIP (PDIP 2006), GOLKAR and PKS which requested an increase in the allocation that would at least approach the constitutionally sanctioned level (*Hukum Online* 29 August 2006).

In response to the DPR’s opposition, the executive through the Minister of Finance insisted on maintaining the proposed amount. This was because the executive had at the same time agreed with the DPR’s request not to increase the electricity price. Moreover, it put into doubt the capacity of the education sector to absorb the suddenly-increased allocation (*Hukum Online* 06 September 2006; *Hukum Online* 29 August 2006). Through series of debates, the allocation for education was finally increased to 11.8 per cent of state spending. However, this compromise failed to stop opposition from the legislators and the people.

Soon after that, the Association of Indonesian Teachers submitted a judicial review to the Constitutional Court arguing that the budget bill was against the constitution since the education spending was far below the constitutionally sanctioned level (*Hukum Online* 25 January 2007). The Constitutional Court finally decided that as far as the education allocation was concerned, the 2007 budget bill was unconstitutional and required the president and the DPR to revise it accordingly (*Hukum Online* 01 May 2007). In response to this decision, the president again insisted on maintaining the approved budget on the grounds that given the budget constraints, the government had to prioritize budget allocation. Infrastructure development was among the priorities which in the future would help the government allocate more education expenses. He could only promise to increase the budget allocation for education from year to year to approach the constitutionally required level.

Taking the Constitutional Court’s decision into account, the DPR also demanded the executive revise the budget. However, through the debates for the 2007 budget revision, the executive again maintained the existing allocation of 11.8 per cent of state spending. This triggered even stronger opposition from the DPR. Realizing that most fractions would vote for the president, as many as 256 individual MPs submitted a note of objection to the
revised budget (*Detikcom* 28 August 2007; *Pikiran Rakyat* 29 August 2007). Again, as in the previous year, the executive maintained its decision.

The materials presented in this part show that strong opposition from the DPR failed to compromise the executive's reform agenda in the fiscal area. Voices from certain groups to impeach the president for violating the constitution received only scant attention. This is because the budget bill requires joint approval from the executive and the DPR so that the president alone cannot be held accountable. Moreover, this move is constitutionally questionable since the president cannot be removed from office because of policy wrongdoings. Even if the DPR insisted on removing the president, the procedure is no now more legally bound up and complicated. Moreover, the opportunity for such a move was practically very limited since the majority of fractions in the DPR supported the president. Additionally, given strong party discipline, the opposition from many individual legislators was simply too ineffective to change the president's mind and he only needed to consider the voices of the fractions. This enabled the executive to move forward with its fiscal reform agenda. If the executive had given up easily and simply followed what the DPR requested, fiscal sustainability would have been placed under real pressure.

The other achievement in the fiscal policy area under the SBY administration was the control of deficit and how to finance it. As I have discussed previously, the executive was frequently criticized for setting a conservative deficit target. The executive maintained that controlling the deficit had been very difficult in the past and it did not want to compromise macroeconomic stability simply to accommodate what the DPR wanted. However, the executive decided to loosen deficit control in the 2006 and 2007 fiscal years to provide a stimulus for economic growth (Ministry of Finance 2007:VI-1). Budget revenue and spending were then adjusted to meet this target. As for deficit financing, SBY focused more on using treasury bonds than privatization. Therefore, while many analysts point to DPR opposition as the main cause for the slow progress of privatization, it was actually SBY's own choice that mattered. He ordered the Ministry of State Owned Enterprises to review the privatization policy by focusing on restructurization and increasing profits through the application of corporate governance principles (*Surya* 21 May 2007).^{176} This was expected

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^{176} The election of Jusuf Kalla as vice president and his strong influence in the economic arena have raised the concern about the government's nationalist and populist propensity. His proposal to buy back PT
to increase taxes and dividends which would then boost budget revenue (Sugiharto 2005). When Sugiharto was replaced by Sofyan Djalil as the Minister of State-Owned Enterprises, the policy to rely on dividend was sustained. One of the deputies in this ministry was quoted as saying that privatization had to be separated from the target of covering the deficit. Deficit financing is a political decision and it is dangerous to link it to privatization (Sinar Harapan 03 August 2007). Overall, given a much better fiscal position, the SBY administration showed only scant enthusiasm for privatization (Aswicahyono and Hill 2004:280). Therefore, though the Coordinating Minister for the Economy, Aburizal Bakrie (before replaced by Boediono in December 2005), and Minister of Finance, Jusuf Anwar (before being replaced by Sri Mulyani), sometimes expressed their interest in pushing privatization, it was only applicable when the annual budget was under pressure (Bari 2005).

Despite this poor performance, there were nevertheless signs of determination on the part of the executive. This was especially true when pushing privatization was really critical to cover the deficit. One case in point was the privatization of PT PGN to cover deficit in the 2006 annual budget. DPR’s opposition to the privatization of this company failed to stop the executive from moving ahead with the plan. This is mainly because SBY has constitutional protection over security of tenure and sufficient partisan support in the DPR. Opposition from the PDIP was simply ineffective since it had only a very limited share of parliamentary seats (PDIP 2007). PDIP even sent a letter to the Anti-Corruption Commission to investigate allegations of corruption and collusion during the process. Opposition from individual legislators was also ineffective. Given strong party discipline, the president only needed to listen to the fractions and those joining his coalition were ready to support his decision.

The discussion so far leads me to conclude that SBY’s higher executive strength coming especially from constitutional protection over security of tenure and sufficient partisan support had a significant effect on the achievements in the adoption of difficult policy

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177 Indosat confirms this concern though it is based on a legal infringement by Indosat’s new owner during the tender process at the end of 2002 (FPKS 2006).

177 From 2005 to 2007, the contribution of dividends from state enterprises to budget revenue has increased significantly. In 2004, it was only Rp 9.1 trillion. It then increased to Rp 10.6 trillion in 2005, Rp 23.3 trillion in 2006 and Rp 19.1 trillion in 2007 (Ministry of Finance 2005; Ministry of Finance 2006; Ministry of Finance 2007).
reform in the fiscal policy area. His administration maintained prudent fiscal policy and adopted related reforms in the areas of tax policy, subsidy removal, and privatization. This achievement is creditable given the scale of opposition his administration had to face.

5.3.3 Investment policy reform

In this area, SBY adopted many difficult policy reforms in the investment area amidst strong opposition from both the DPR and other organized groups. The first case was the issuance of Government Regulation No.3/2005 (or PP 3/2005) on the Provision and Use of the Electricity Power on 16 January 2005. The PP triggered opposition since it restored the content of Law 20/2002 on Electricity that had been annulled by the Constitutional Court. However, this opposition failed to change his decision. The PP has been upheld up to the time of writing and the president has not submitted a bill on this issue as requested by the DPR. How can this persistence be explained?

Indonesia’s constitution does give the president the authority to issue a PP to implement a law. Therefore, SBY argued that the issuance of the PP 3/2005 is under his prerogative as the president and there is no way for both the DPR and other organized groups to oppose the PP on this ground. The problem is that though the PP refers to Law 15/1985, its content reflects the annulled Law 20/2002. In spite of this flaw, the PP is maintained.

Another case indicating the president’s persistence in spite of strong opposition especially from the DPR is the issuance of PERPRES 36/2005 on Land Provision for Public Interests. This was a serious blow SBY had ever made given the sensitive nature of the policy and the scale of opposition he had to face though the issuance of PERPRES is constitutionally within his prerogative. Along with public opposition, the DPR also mounted strong opposition to this PERPRES. Initially, almost all fractions in the DPR’s Committee II opposed the regulation. This included the major fractions such as PDIP, PKS, PAN, and PKB. Their main concern was that by giving the right for land confiscation to the government for disputes where a mutually agreed compensation could not be reached, the PERPRES contains arbitrary and repressive elements which could deprive people’s basic right of their properties. Moreover, a policy issue as important as land acquittal and
compensation requires more than a PERPRES, that is, a law (UU). After sessions of debates, a compromise among fractions was reached to request the president to revise the PERPRES. The DPR also requested the president to immediately submit a draft bill for land administration and reform. It was finally only the PDIP as the opposition party which persisted in opposing the PERPRES (*Suara Pembaruan* 09 June 2005).

In response to the DPR’s request, SBY refused to revise the PERPRES. He promised only to have it socialized it throughout the country to enable the people to have a better understanding on it. By the time of writing, no draft bill had been submitted to the DPR yet on this matter, two years after the PERPRES was issued. SBY still uses this PERPRES to push forward his reform agenda in the infrastructure area.

The two cases I have presented so far are clear examples of the effect of executive strength. The issuance of PP and PERPRES is constitutionally stipulated. With constitutional protection over security of tenure, SBY had a sense of freedom in pursuing his own agenda especially those under his prerogative. This also means that the DPR has limited room to maneuver against his survival. Moreover, it was clear that only the PDIP which opposed the initiatives. Even if the DPR brought the case to a plenary session to be voted for, the president would certainly maintain his agenda given his consolidated and sufficient partisan support.

Also related to this area, the SBY administration adopted Law 17/2006 on Custom. Initially the DPR opposed some of the articles of this law especially regarding the proposal to increase the authority of the customs office. The DPR expressed its concern considering the notorious corruption and collusion in that office (*Hukum Online* 09 June 2006). However, the executive maintained the importance of such proposal given the challenge this office must face. The law increases the power of the custom office over enforcing strident sanctions for custom infringements. At the same time, the law also increased the sanctions and punishment for custom officers who infringe the law. All fractions finally approved the law. This is again another example of how the executive could win its agenda amidst opposition from the DPR.
Still in the investment area, the most significant achievement of the SBY administration has been the passage of Law 25/2007 on Investment. During the process of debate, strong opposition came from all fractions using populist and nationalist sentiments. However, when the bill was brought to the plenary session on 29 March 2007 to be voted on, only PDIP and PKB which opposed it (Suara Merdeka 27 March 2007; Tempointeraktif 29 March 2007). All other fractions, especially those joining the coalition turned their opposition to supporting the bill. As during the debates, opposition from PDIP and PKB centered on the concern that the law would benefit foreign investors at the cost of local entrepreneurs especially small and medium scale enterprises. It also potentially endangers the welfare of workers, so they argued. Nationalist sentiment such as the issue of sovereignty was also expressed as the law contains liberal spirit in it (Detikcom 29 March 2007; Kompas 23 February 2007). PDIP even considered the law as a legalization of economic liberalization.

The approval of the investment law is another evidence of the effect of executive strength. With a constitutionally protected security of tenure and the support of his consolidated coalition allies in the DPR, SBY once more adopted an important reform agenda against strong opposition from the DPR. Though the GOLKAR and PD fractions as well as other parties behind the coalition also raised criticisms during the debate, they finally supported the bill. Even the PKS and PAN fractions which clearly opposed the articles on the role of local government and the spirit of the law in general, finally approved the bill. Meanwhile, PKB was playing its trump card since it was still unhappy with its representatives in the cabinet. It was again clear that only PDIP which opposed the bill consistently.

After the passage of the investment law, SBY again issued a government regulation in lieu of a law or PERPU 1/2007 on Free Trade and Port Area. This was a smart move. As discussed before, Indonesia’s constitution allows the president to issue a PERPU should exigencies compel though it must be approved by the DPR in the subsequent session. SBY expected to propel the process since he would certainly get DPR approval to transform the PERPU into law (UU) given his consolidated partisan support. Initially, the DPR put up a

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178 At that time, PKB’s true figure in the cabinet was only Erman Suparno. Saefulhak Yusuf who was initially from PKB had turned his coat to PPP. SBY finally removed him from the post in May 2007 and replaced him with another PKB’s true figure, Muhammad Lukman Edy.
strong opposition. It argued that this concession had to be based on a separate law. Seven fractions, namely PDIP, PAN, PKB, PPP, PKS, BPD, and PDS rejected the PERPU arguing that it would create further legal uncertainty. They would certainly reject this PERPU to become law. Only the PD and PBR fractions which supported the PERPU to become law. Meanwhile GOLKAR took a neutral position saying that it is ready for further discussion (Hukum Online 13 September 2007). However, when the DPR held a plenary session on 9 October 2007 to decide the status of PERPU, 8 fractions in the DPR – GOLKAR, PD, PPP, PKB, PKS, BPD, PBR, and PDS – approved it. PDIP again stood alone as the only fraction which opposed the PERPU. Meanwhile, PAN approved it with several conditions though two of its MPs opposed it (Detikcom 09 October 2007). However, since their fraction had approved the PERPU to become law, their opposition was meaningless. The PERPU has now become the Law 44/2007.

This is yet another clear example of the effect of executive strength. With constitutional protection over security of tenure and a consolidated legislative contingent in the DPR, SBY was able to adopt this difficult reform agenda. As in other cases I have discussed, even strong opposition failed to stop the adoption of reform agenda. His consolidated partisan support in the DPR always helped him achieve this. True opposition only came from the PDIP and this was far from sufficient to block his reform agenda.

Beyond all these achievements, SBY failed to push further reform in the labor area. His decision to withdraw the draft revision of Law 13/2003 was a wise move. He could actually push this agenda forward given his strong constitutional power and consolidated partisan support in the DPR. However, the cost of such insistence for the whole economy would have been very high given the strong and well-organized opposition from the labor unions at a very worrying level as well as other forms of street politics. This is nothing to do with his survival but rather with the immediate effects on the whole economy.

179 The opposition from the PDIP centered on the stipulation that the executive would only need to issue a government regulation (PP) to determine certain areas as special economic zones. For this fraction, since the creation of special economic zones implicates state sovereignty over the zones, it had to be regulated individually through a special law. On the other hand, fractions which supported the PERPU requested the DPR to accelerate the approval. This stood in contrast with their initial opposition. PAN supported the law but requested the executive to enforce the law, empower the local people, and develop small-scale enterprises.
The qualitative narratives I have presented so far show that the SBY administration adopted many more reform initiatives through a combination of ‘legislating through parliament’ and ‘legislating around parliament’. The first strategy followed the normal procedure through the DPR while the second one used a short-cut through the passage of high-profile policies without the involvement of the DPR. Both these strategies worked in favor of the president even when the opposition was very strong, not only from the DPR but also from the people and organized groups. His constitutional power – security of tenure – gave him minimal political capital to pursue his own agenda. The agenda was then ‘legalized’ in the DPR by his consolidated coalition allies. This is something Wahid and Megawati could not do given their weak partisan support. This significantly explains the difference between them. The following section will elaborate this argument by assessing the achievement of the SBY administration in fuel subsidy reform.

5.4 Fuel subsidy reform

As discussed in the previous two chapters, adopting a fuel subsidy reform requires strong political capital, the most important one is executive strength stemming from the executive’s security of tenure and partisan support in the DPR. In this section I argue that since SBY had such capital, he could adopt policy reform in this troublesome area. The discussion will focus on the fuel subsidy reform in 2005.

Compared to his predecessors, SBY had to face more daunting problems in reforming the fuel subsidy due to an ever-increasing trend of international oil price hikes since 2004 and the Rupiah depreciation at the same time. The changes caused the fuel subsidy to increase to a level far above the budget allocation. At the same time, a series of natural disasters struck the country. These unfavorable conditions required a quick policy response from the new administration. These conditions provide a good policy setting to assess the effects of executive strength. Hanna (2005:59), for example, even argues that it is not the oil price hike but rather the effective policy-making to tackle it and other related problems that matters.
The challenge for SBY to cut the fuel subsidy was even more difficult given Megawati’s decision to bring fuel subsidy reform back into the political arena in 2003 and also the decision to delay reform throughout 2004. Moreover, taking such an unpopular measure was absolutely difficult given people’s ‘SBY euphoria’. However, something had to be done as the international sport crude oil price had increased to as high as US$ 50/barrel, far above the approved 2004 budget assumption of US$ 24/barrel (OPEC 2005:118). This should have led SBY to increase the fuel price as recommended by his economic team. However, he was not in a safe enough position to undertake such an unpopular measure, in anticipation of the strong opposition from the National Coalition which at that time still outnumbered the People’s Coalition in the DPR. Moreover, taking this measure was clearly in contrast to his Hundred-Days Program, one of which was to improve people’s welfare, no matter how he defines it.

After a long delay, the president and his team finally proposed in early 2005 to increase the fuel price in March 2005. For this proposal to be put into practice, he needed DPR approval. Such approval was even mandatory since the fuel subsidy allocation had far exceeded the allocation in the 2005 budget. This time, the president’s position was sufficiently secure with the election of Jusuf Kalla as the chairman of GOLKAR, dissolving the National Coalition accordingly. Therefore, the only opposition to this proposal would come from PDIP and given its share of seats in the DPR, that would be ineffective.

To get DPR approval, a series of consultative meeting were held involving several ministers and DPR committees especially the Budget Committee, the Committee VII (Energy) and the Committee XI (Finance). Even on 23 February 2005, the meeting went on until dawn. The president was represented by the Coordinating Minister for People’s

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180 What I mean by ‘SBY euphoria’ is people’s high expectation that the SBY administration would bring significant improvement especially to their economic condition. This includes maintaining cheap prices for all basic commodities. Increasing the fuel price is clearly against people’s expectation.
181 Remember that until mid December 2004, GOLKAR was still part of the National Coalition which opposed the president. Meanwhile, the People’s Coalition that supported SBY was too weak to provide him with legislative support. This put SBY in a vulnerable position in the legislative arena.
182 SBY launched a Hundred-Days Program which contained three main agendas. The first was to accomplish a secure and peaceful Indonesia. This would be achieved through solving horizontal conflicts, fighting terrorism and eradicating illegal activities. The second was to accomplish a just and democratic Indonesia. Among the priorities were strengthening the Attorney General, combating corruption and continuing bureaucratic reform. The last one was to achieve a wealthier Indonesia. The agenda included improving investment conditions, maintaining macroeconomic stability, improving people’s welfare, and eradicating poverty.
Welfare, the Minister of Finance, the Minister of Energy and Mineral Resources, and the Minister of National Development Planning. Usually the president is represented only by the Minister of Energy and Mineral Resources for consultation with DPR's Energy Committee and the Minister of Finance for DPR’s Finance Committee. Despite the executive’s convincing argument on policy direction and the compelling need for immediate action to increase the fuel price, the DPR’s Budget Committee insisted on opposing the plan (Tempointeraktif 24 February 2005). Its opposition was based on three main reasons. Firstly, such proposal could only be allowed through a budget revision and the government had not yet submitted the draft budget revision. Usually this can only be accomplished after the semester-one progress report in June. Secondly, the executive was considered unprepared for delivering compensation funds in which data on the eligible and delivery system were of great concerns. Thirdly, the executive had not undertaken an audit of PERTAMINA’s production costs as requested by the DPR. Therefore, to ease budget pressure, the president was instead recommended to cut recapitulation expenses in several banks rather than cutting the fuel subsidy (Tempointeraktif 25 February 2005).

Despite strong opposition from the Budget Committee, the Energy Committee and the DPR as an institution, on 28 February 2005, President SBY issued Presidential Regulation No. 22/2005 to increase fuel price by 29 per cent on average which would be valid since 1 March 2005, right the next day. This decision triggered even stronger opposition from the DPR as well as widespread protests throughout the country asking SBY to resign (Tempointeraktif 02 March 2005). The main reason for this opposition was the fact that both the executive and the DPR had not achieved an agreement on such issue. The DPR again maintained the reasons for its opposition as mentioned previously (Detikcom 01 March 2005). The Head of the Budget Committee was quoted as saying that it was very likely for the DPR to use its investigation and/or interpellation rights to examine this case. The most dramatic incident related to this decision was a physical clash among legislators during the plenary session on 16 March 2005, the first time in Indonesia. The clash was provoked by a unilateral decision of the DPR Speaker from GOLKAR, Agung Laksono, who chaired the meeting. He decided that the plenary session would continue to make a decision through voting. He argued that this was based on the inter-fraction consultation during the session to break the deadlock. Since the consultation only involved the leaders of the DPR and fractions, it was a clever move to take the decision out from the hands of
individual legislators, transferring it to their leaders, and thus, consolidating support for the decision. With strong party discipline, members of the parties joining the coalition would almost certainly vote for the president and this would clearly be a defeat not only for the PDIP but also for legislators who opposed the decision. Due to the clash, the session was delayed (Detikcom 16 March 2005).

Developments after the incidence made it increasingly clear that only the PDIP would really oppose the decision. The PKB fraction finally decided not to involve in any of the coming sessions as part of its commitment to reject the decision. Meanwhile, the parties behind the coalition became more consolidated to support the president despite ripples of opposition from their individual members. When another session was held on 21 March 2005, GOLKAR played the key role in dividing the votes in the DPR. Because of its smart engineering, voting was no longer simply a matter of supporting or opposing the president’s decision as in previous debates. Instead, five options were offered to vote on (Detikcom 21 March 2005). They are:

1. DPR delegates the deliberation on fuel price increase to respective DPR bodies, namely, Committee VII, Committee IX, and Budget Committee.
2. DPR rejects fuel price increase.
3. DPR understands fuel price increase.
4. DPR rejects the decision and gives the opportunity to the executive to discuss with the DPR’s respective bodies.
5. The executive must review its decision through the 2005 budget revision.

This was the tactic employed by GOLKAR – together with PD – as the main backbencher of the executive to split votes among the MPs.183 As was seen later, the tactic worked as planned. The plenary session finally voted for option 5 which was supported by 297 votes. They came from GOLKAR (122 votes), PPP (53 votes), PD (56 votes), PKS (36 votes), PBD (16 votes), and PBR (14 votes). Meanwhile, 56 votes from PAN (43 votes) and PDS (13 votes) voted for option 4 (Detikcom 21 March 2005; Pikiran Rakyat 22 March 2005). PDIP – and PKB before that – walked out of the session due to their disagreement with the game being played.

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183 Based on confidential interview with one of GOLKAR’s leaders on 23 February 2006.
This final decision could not be separated from SBY’s effort to obtain support from fractions other than GOLKAR and PD in which Jusuf Kalla played a key role. The night before the voting, he held a special meeting with the leaders of some major parties. This proved effective in consolidating legislative support in the DPR given the strong party discipline. Fractions which previously strongly opposed the president’s decision such as PKS, PAN, PBR, and PDS finally changed their option and supported it though it was not unconditional. For example, PKS required the president to pay special attention to the improvement of education and health services (Detikcom 21 March 2005).

Based on the DPR’s decision, the executive then proposed the draft budget revision on 24 March 2005. This meant that the fuel price increase was still valid until at least June 2005 when the budget revision was to be decided. However, a day before that, 31 MPs from seven different fractions proposed the use of the investigation right to the Deliberation Board. As stipulated in the DPR’s Rules of Procedure, this proposal was then presented in the plenary session on 24 March 2005. In their opinion, the decision to increase fuel price contained many problems. For example, the executive’s calculation that by increasing the fuel price and then providing a compensation fund to eligible beneficiaries would reduce poverty was not self-evident. On the contrary, it had triggered inflation which caused price increase by more than 10 per cent in almost all products and services. This certainly led to more people becoming poor or poorer. Moreover, the fact that the president took this decision without the approval of the DPR implied that he had infringed the Constitution. This decision had to refer to the budget bill, namely Law 36/2004 on the 2005 National Budget. The executive also had to provide the DPR with a detailed report on the fuel production and distribution costs of PERTAMINA. Also important were the facts that the executive had carried out very limited socialization to the people and that it had failed to establish a well-designed mechanism of the fuel subsidy, improve management capacity, and combat rent-seeking actors in the government bureaucracy to be able to deliver the compensation programs, all of which led to the ineffectiveness of the measure. Considering these flaws, the investigation proposal mainly aimed to assess the legality and constitutionality of the president’s decision to increase the fuel price through Presidential
Regulation No.22/2005,\textsuperscript{184} and to ensure the application of good governance principles in the implementation of the decision.\textsuperscript{185}

Based on this proposal, the DPR's Deliberation Board then set the schedule for another plenary session when each fraction could present its response and decided whether it agreed or disagreed with the use of investigation right. In the plenary session on 31 May 2005, four fractions, namely PDIP, PKB, PDS and PKS,\textsuperscript{186} supported the proposal while the other fractions – GOLKAR, PD, BPD, PAN, PBR, and PPP – rejected it. Among the arguments for supporting the proposal were the multiplier effects of the decision, the unilateral action by the president which is against democracy and constitution, and an ill-prepared compensation mechanism (PDIP 2005; PKB 2005; PKS 2005; PDS 2005). Meanwhile, those who rejected the proposal argued that the decision to increase fuel price was a difficult measure SBY had to take to save the economy and that the DPR had agreed to request the president to review it through the budget revision together with the DPR. Moreover, the fuel subsidy was still ill-targeted and had triggered smuggling to neighboring countries. They also requested the president to conduct an audit of PERTAMINA’s production and distribution costs, immediately start budget revision deliberation, improve compensation mechanism and socialization, ensure fuel availability for all regions, combat smuggling, and deal more seriously with poverty and unemployment (BPD 2005; GOLKAR 2005; PAN 2005; PBR 2005; PD 2005; PPP 2005). Since the decision was based on the fraction’s response and given that the majority fractions rejected the proposal, the investigation proposal failed. Even if the decision was based on voting, the proposal would certainly be beaten as well, given the strong party discipline. The votes from five fractions rejecting the proposal clearly outnumbered the votes supporting it.

\textsuperscript{184} Referring to the Indonesian legal hierarchy, the investigation aimed to examine whether the Presidential Rule to increase fuel price did (not) contradict the law above it, namely the national budget law. President’s decision in this regard must refer to this law, the ignorance of which is consequential.

\textsuperscript{185} For more detailed information on this issue, see DPR’s Minutes of Meeting of the 16\textsuperscript{th} Plenary Session on 24 March 2005

\textsuperscript{186} PKS was and is a clear example of new party with opportunistic behavior and unpredictable maneuver to get what it wants. In one time it supported the executive, while in other time it opposed it. The most common strategy is to oppose unpopular measures in the first place but then support them in floor-voting. Applying this provided it with two advantages: strengthening its political leverage versus the executive and projecting its populist image to the voters.
An interesting statement came from the president himself during this debate. In response to DPR’s strong opposition, SBY himself stated that he was ready to respond to DPR’s any move, including the use of investigation right and the proposal to ask the Constitutional Court to assess whether the president had violated the budget law (Tempointeraktif 01 March 2005). He also confidently said that he was ready to be unpopular by taking this decision (Detikcom 25 February 2005; Tempointeraktif 25 February 2005). Behind this confidence lies his strong political resource. The president’s security of tenure could not be compromised simply because he pursues a certain policy. Moreover, his partisan contingent in the parliament was ready to back up his decision though it sometimes involved tricky deals. My confidential interviews revealed that the president was confident in his action because he had the guarantee from the vice president who had ordered GOLKAR leaders in the DPR to work hand-in-hand with the president’s party (PD) to mobilize support from other partisan blocks to back the decision.187 As discussed previously, it was finally only the PDIP and PKB fractions which consistently opposed the plan while other fractions changed their opposition into supporting the president’s decision. The proposal to use the right of investigation was also finally defeated by the majority fractions which supported the president, paving the way for SBY to continue his reform agenda.

That the DPR would fail to proceed with the use of the investigation right had been predicted by many informed experts. Given the strong party discipline, the president needed only to approach the party leaders who have representatives in the cabinet to get legislative support. Therefore, though the proposal was endorsed by many legislators from different fractions, the final decision was nothing but party direction. Those who proposed the proposal were legislators who felt powerless and disappointed with the way party leaders deal with the president and his decision, making the DPR as the executive’s rubber stamp. Parties having their members in the cabinet finally supported the president’s decision except PKB. This party wanted to exercise its leverage given that its figures in the cabinet were not the true ones. This sent a strong message to SBY that he needs to reassemble his cabinet to more consolidate his partisan support.

187 Confidential interview with some MPs from GOLKAR in Jakarta on 14 February 2005.
With this bold action, the government could reduce budget pressure. Given the simultaneous rise of the international oil price and the depreciation of the Rupiah, the fuel subsidy allocation should have reached as high as Rp 60.1 trillion, three times the initial allocation of Rp 19 trillion. In the executive’s calculation, the fuel subsidy allocation could reach between Rp 76.8 and Rp 93.5 trillion should the oil price in international market increase above US$ 40 per barrel and the Rupiah exchange rate go above Rp 8,900/US Dollar. The depreciation of the Rupiah to Rp 9,300/US dollar would bring the fuel subsidy to as high as Rp 100 trillion (Ministry of National Development Planning 2005:27). This also means that the budget deficit would reach at least -1.3 per cent of GDP, far above the set target of -0.7 per cent of GDP. A price increase by 29 per cent on average reduced the allocation to Rp 39.8 trillion. The budget amount saved was then partly reallocated to the people through the compensation program which amounted to Rp 10.5 trillion in various schemes such as education and health services, cheap rice provision, rural infrastructure development, housing provision, family planning, a revolving fund and other social services.\(^{188}\)

After securing his agenda, SBY then had to prepare for the budget revision, through which the executive and the DPR would determine the amount of fuel subsidy allocation.\(^{189}\) For this purpose, the executive and the DPR had to debate the budget assumptions, the most important of which are the Rupiah exchange rate and the oil price.\(^{190}\) The Rupiah exchange rate was finally increased from Rp 8,600 to Rp 9,300 per US Dollar while the oil price was set at US$ 45, a significant increase from US$ 24 in the initial budget. The changes caused the fuel subsidy allocation to increase from Rp 19 trillion (0.7 per cent GDP) to Rp 76.5 trillion (2.9 per cent of GDP). The executive also for the first time presented PERTAMINA’s production and distribution costs to meet the DPR’s request, which amounted to Rp 29 trillion (Tempointeraktif 28 June 2005). However, as I have discussed

\(^{188}\) A compensation fund of this amount was a significant increase from previous years: Rp 2.2 trillion in 2001, Rp 2.85 trillion in 2002, and Rp 3.1 trillion in 2003 (Tempointeraktif 01 January 2003).

\(^{189}\) As stipulated in Law 17/2003 on State Finance, government can revise annual budget after the first-semester implementation. This means that the president can only submit a budget revision after June each year and it takes at least a month to get approval from the DPR. However, under certain circumstances, budget revision could be undertaken sooner than this.

\(^{190}\) Scholars argue that the crude oil price increase has both positive and negative effects on the economy. It potentially brings positive effect on the trade account, slightly negative effect on balance of payments, and clear negative effect on the budget deficit under the arrangement of decentralization (Sen and Steer 2005:288). With regard to the later, an increase of US$1/barrel will reduce budget balance by Rp 1 trillion (around US$ 100 million) or 0.03 per cent GDP (World Bank 2005a:14).
previously, the changes were far from sufficient to reflect the worsening economic condition. In August 2005, the government again had to amend the revised budget due to significant changes in the Rupiah exchange rate and the international oil price. The Rupiah exchange rate was increased again to Rp 9,500 per US Dollar while the oil price was increased to US$ 50.6 per barrel. All budget items were adjusted to these changes as well.

Amidst these unfavorable macroeconomic conditions, a compromise over the fuel subsidy allocation could not be reached. Initially the executive proposed the allocation of Rp 138 trillion assuming the oil price was US$ 54/barrel. Together with the Budget Committee, it then made several adjustments so that the fuel subsidy allocation could be pushed down to Rp 113.7 trillion (Kompas 09 September 2005). Since this was still burdensome for the budget, they then made further adjustment. This time, two options emerged. First, the fuel subsidy would be maintained at Rp 113.7 trillion which consequently caused the deficit to rise to -1.4 per cent of GDP and the government still needed an additional Rp 23.2 trillion to finance deficit. Second, the fuel subsidy would be reduced to Rp 89.2 trillion to be able to maintain the deficit at -0.9 per cent of GDP. The second option implies that the fuel subsidy would be cut and the price be increased again.191

These options were then brought to the plenary session to be decided. Again, the PDIP expressed its strong opposition. As a compromise could not be worked out, the decision had to be made through voting. All legislators from PDIP voted against the revised budget unless the fuel subsidy was to be maintained at Rp 113.7 trillion. This was supported by only four votes, each one coming from PKB, PAN, PKS and BPD. PKB – and 8 votes from PDS – abstained, trying to strengthen its leverage as in March 2005. Meanwhile, all other fractions – GOLKAR, PD, PPP, PAN, PKS, BPD, and PBR – and 4 votes from PDS supported the second option (Hukum Online 28 September 2005; Kompas 28 September 2005). The change of some parties’ preference in favor of the president’s plan was made possible by a series of inter-fraction meetings before the voting that involved only fraction leaders (TempoInteraktif 27 September 2005). Given the strong party discipline, most MPs simply followed what their fractions ordered. This also caused some MPs to take a different position from their fractions to express their frustration.

191 See http://www.pks-jakarta.or.id/modules.php?op=modload&name=News&file=article&sid=331&mode =thread&order=0&thold=0 (accessed on 16 May 2007)
This was only an initial step and the president and his team then had to give details of the plan to increase the fuel price. Strong opposition expressed by the people, labor unions, business communities, and many other organized groups or sporadic street politics throughout the country failed to change the president’s mind. Even a call from the MPR Speaker to cancel the plan was ignored (Tempo Interaktif 27 September 2005). Instead, he asked those who opposed the plan to focus on the efforts to find solution for the energy problem, including developing an alternative to mineral fuel (Tempo Interaktif 27 September 2005; Tempo Interaktif 28 September 2005; Tempo Interaktif 30 September 2005). He again maintained that he was ready to be unpopular but people had to understand that his decision was the best for the country (Kompas 01 October 2005). Moreover, he promised to compensate for his decision through various compensation programs, including unconditional cash transfer to the eligible (Kompas 22 October 2005; Tempo Interaktif 30 September 2005). His concern then centered on deciding the extent of the price increase, the types of fuel products to be increased, and the time of the increase. This last concern was very critical considering the coming of the fasting month and Idul Fitri for Moslem people sooner after that. A price increase would surely worsen inflation as people normally consume more during this period.

The real surprise finally came on 30 September 2005. Through Presidential Regulation No.55/2005, SBY increased the price of all fuel products including the long protected kerosene for households. More surprising than that was the extent of the increase. Despite his early promise to increase the fuel price by around 50 per cent on average, the price was raised by an average 114 per cent. Gasoline price was increased by 87.5 per cent, automotive diesel fuel price was raised by 95.5 per cent, and the kerosene price was significantly increased by 186 per cent. This was a significant achievement as the extent of the price increase, the types of fuel involved and the timing were all creditable (Sen

While fuel price increase did burden all sections of society, it was actually the better-off groups who suffered the most (Kassim 2005:165). Government data showed that 84 per cent of fuel subsidy went to 60 per cent of the middle and upper class people while 40 per cent of poor people consumed 16 per cent only (Kompas 04 October 2005; Tempo Interaktif 27 February 2005). This included a large proportion of kerosene for households which was converted into industrial fuel. Unconditional cash transfer at Rp 100,000 per head per month was expected to ease the burden of the poor.

The percentage of the increase was applied to solar fuel other than that in the gas station, while the increase in the gas station was 104.7 per cent, ranging from Rp 2,100 to Rp 4,300. The increase only applied to households and small-scale enterprises ranging from Rp 700 to Rp 2,000 while for other segments, the government even decreased the price up to 10 per cent.
Steer 2005:297). Even the IMF welcomed this decision as 'bold and wise' (Tempointeraktif 05 October 2005). This is also a symbolic but significant move to convince investors that his administration is ready to take bitter reform initiatives (Business Asia 17 October 2005). Should the president avoid this decision, the fuel subsidy allocation would have reached more than 5 per cent of GDP compared to the health spending of 0.5 per cent of GDP only (Hanna 2005:58). Thus, it helped maintain the deficit and fiscal sustainability amidst unfavorable macroeconomic conditions.

The decision again triggered strong opposition, not only from the DPR but also from the people. The DPR felt that the president had broken his promise regarding the extent of the fuel price increase (Detikcom 01 October 2005). As in March 2005, several legislators then mobilized opposition within the DPR by proposing the use of either interpellation or investigation right. In this respect, PDIP as the opposition party started off (Detikcom 01 October 2005; Detikcom 03 October 2005; Kompas 02 October 2005). PKB also requested that president cancel the price increase and asked the DPR leadership to schedule a plenary session to decide its formal response (Detikcom 04 October 2005; Detikcom 07 October 2005). PAN joined the opposition, requesting the president to review his decision by increasing the fuel price gradually rather than at the rate decided (Detikcom 09 October 2005). PKS even planned to review its support to SBY though it later backed away from this (Detikcom 17 October 2005). Similarly, the MPR Speaker asked SBY to review his decision as the consequences would be too burdensome for the people (Detikcom 03 October 2005).

In response to this opposition and the DPR's threat to conduct an investigation or interpellation, the president and his team felt no compelling need to launch a counter-attack. The Vice President, Jusuf Kalla, argued that the decision was in line with the DPR approval to allocate Rp 89.2 trillion for the fuel subsidy. At this amount, the fuel price had to be increased significantly as the president had done (Kompas 02 October 2005; Detikcom 07 October 2005). The president instead turned his attention to handling the second Bali bomb blast on 1 October 2005.

195 Azis (2006), for example, argues that the president's decision to significantly increase fuel price was ill-advised. The fuel subsidy could only be partially removed if the government also cut the allocation for sovereign domestic debt. This confuses ends and means.
To complicate the situation, on 7 October 2005, the Constitutional Court sent a letter to the DPR saying that the president’s decision to increase the fuel price was against the constitution. This was because the decision was based on Law 22/2001 on Oil and Gas. The Constitutional Court had undertaken a judicial review of this law resulting in the revision of some articles to maintain state ownership over strategic resources. It challenged the president as his decision potentially applied a purely market mechanism for the fuel price.

This was a serious blow. The president then held a meeting involving all key ministers to discuss the letter. The State Secretary argued at that moment that the letter had no serious implication for either the decision or the president’s tenure since the decision was also based on the budget bill. Moreover, the fact that the president issued the decision to increase the fuel price implies that the government still applied administered, not purely market, mechanism (Detikcom 11 October 2005). Interestingly, the House Speaker and MPR leaders such as AM Fatwa also showed no interest in that letter (Detikcom 10 October 2005). However, this did not stop those who opposed the decision such as PDIP from using it as important political ammunition. Some had even discussed the possibility of presidential impeachment on those grounds.

Considering the issue at hand, PDIP and PKB then sent a letter to the House Speaker requesting the DPR to hold an “Extraordinary Plenary Session” to respond to the decision. For this session to be held, the DPR’s Rules of Procedure require that it must be proposed by at least three fractions. Since GOLKAR, PD, PKS, PPP, PAN, PBR PDS, and BPD were all against the plan to hold the session, the DPR failed to mount the challenge to the president (Detikcom 10 October 2005; Tempointeraktif 17 October 2005). As pay back, the executive offered a salary increase for the DPR which triggered a very negative response from all over the country. Lacking any other rational justification for this, one thing was clear to the public: the executive wanted to tame the DPR (Detikcom 23 October 2005; Detikcom 24 October 2005; Detikcom 25 October 2005; Kompas 24 October 2005; Tempointeraktif 27 October 2005).¹⁹⁶

¹⁹⁶ The executive argued that the increase in the DPR’s salary along with DPR approval to the increase fuel price was simply a coincidence. Together with DPR leaders, they pointed to the tasks each parliamentarian must carry out bear which require extra money.
The fact that SBY was able to win his contentious reform agenda was notable. On the very day when the price increase was applied, another bomb blast hit Bali, known as Bali Blast II. After that, because October 2005 was also the first anniversary of the SBY administration, criticism spread over his inability to bring about the expected changes, a fact which he and the vice-president also realized. His response was to strengthen his team, especially the economic team, through a cabinet reshuffle which he put in place a month later.

Our discussion so far shows how President SBY adopted some painful decisions in pushing the fuel subsidy reform despite strong opposition, not only from the DPR but also from the people as a whole. Most notable is what he did in 2005, increasing the fuel price by a significant rate. In March 2005, the fuel price was increased by 29 per cent on average while in October 2005, it was increased by 114 per cent on average. I have also argued that this achievement is substantially explained by his higher executive strength coming especially from the constitutional protection over security of tenure and a sufficient and consolidated partisan support in the DPR. He was able to show his determination amidst threats of interpellation, investigation, or even impeachment from the DPR. The last threat was constitutionally questionable under the new institutional arrangements since it required the Constitutional Court and the MPR to work it out. In addition to that, with the parliament dominated by SBY’s partisan contingent, the proposal was almost certainly unworkable.

Meanwhile, given the nature of policy making which emphasizes deliberation to reach agreement, his determination would have not been possible if the DPR was still polarized between the National Coalition as opposition on one side and the People’s Coalition as the government supporter on the other side. During the period of this study, people again dubbed the DPR as the president’s rubber stamp as under Suharto (Detikcom 03 October 2005). This is because it failed many times to pose a real policy challenge to the executive and instead ended up supporting the executive’s decision. Moreover, rather than mounting a substantive challenge using a rational policy argument, all fractions in the DPR were still trapped in ‘image politics’ using marketable populist terms. This includes those supporting the president, let alone the opposition force.197 His tough decision enabled the government

197 On many occasions when dealing with the executive’s controversial decision, the MPs were very reactive in posing their opposition though they finally approved the measure. This was especially true in their
to control the fuel subsidy allocation and, therefore, the budget deficit. Overall, the fuel subsidy allocation had been reduced from 3.5 per cent of GDP (Rp 69 trillion) in 2004 and 3.5 per cent of GDP (Rp 95.6 trillion) in 2005 to 2.1 per cent of GDP (Rp 64.2 trillion in 2006) and 1.6 per cent of GDP (Rp 61.8 trillion) in 2007. This achievement is impressive given the unfavorable macroeconomic and political conditions prevailing at that time.

5.5 Conclusion

This chapter has discussed the improved achievements in the economic policy reform under the SBY administration. Though SBY faced many political obstacles, especially opposition coming from fragmented institutional arrangements, he adopted many reform initiatives, especially in areas with political significance such as fiscal policy reform, investment-related policy reform and fuel subsidy reform. At least in the policy areas I am investigating, there was no incidence of policy reversal as under Megawati and Wahid.

This variation is best explained by SBY’s higher executive strength in both constitutional and partisan respects. As a directly elected president with constitutionally protected security of tenure and a more consolidated partisan support, he did not face the same political vulnerability his predecessors had had to face. Consequently, he could adopt economic policy reform relatively more effectively even in the face of the opposition from the DPR and the people. His failure to push labor reform is due to a more rational calculation given the scale and severity of opposition, especially from the labor unions which were highly organized, the ignorance of which could be very consequential for the whole economy. Beyond this, as far as economic policy reform is concerned, his administration made many promising breakthroughs and changes even in difficult areas where the opposition had in the past succeeded in blocking their adoption. His persistence on taking tough policy breakthrough had even come at the cost of his popularity as shown by some surveys (Kompas 20 February 2006; Kingsbury 2007; LSI 2007).

statement to the public and during plenary sessions. My in-depth interview with some MPs and staff in the DPR’s think tank (P3Q) in February 2006 confirms that this was all to build a good political image as if they really represented the people. The MPs would pose criticism to the executive using popular opposition jargons but finally support the measure simply to get credit from the public. New parties especially PKS have been most criticized on these grounds. Moreover, strong party discipline prevented them from doing so.
In presenting this conclusion, let me also say that other alternative explanations of his personal commitment to policy reform and the technocratic style of policy-making are simply inadequate as explanations of the achievements in economic policy reform under his administration. In the early months of his administration, he made a very careful calculation resulting in delays in many quick policy responses. At that time, while he had a personal commitment to reform, he had insufficient political capital to adopt difficult policy reform. Only after the inclusion of GOLKAR in his coalition in December 2004, could he take many significant policy breakthroughs through various combinations of policy instruments. A more measured explanation must therefore refer to the policy-making context in which the degree of executive strength proves very important. Those who argue that the SBY administration benefited from improved economic conditions must also reconsider their argument since it also faced difficult challenge especially in the area of micro economic environment. Even so, what matters is its ability to respond to the changing environment and this makes institutional underpinning more adequate an explanation than others.
6

Conclusion

6.1 Conclusion

This thesis has assessed the effects of the new institutional arrangements on policy outcomes in post-Suharto Indonesia (1999-2007). Looking especially at policy-making capacity, it argues that the new institutional arrangements have brought about many significant effects. It has illustrated this argument by qualitatively investigating the effect of the degree of executive strength – an aggregated measure of a president’s constitutional powers and partisan support – on economic policy reform, especially in areas with strong political opposition. The core argument of this thesis is that the variation in the adoption of economic policy reform among the post-Suharto administrations is significantly explained by the variation in the degree of executive strength. In this way, it brings the long underplayed political institutions back into the study of contemporary Indonesian politics.

Let me now briefly summarize some of the key findings discussed in the previous chapters. A brief comparison of these findings will also be presented to demonstrate the core argument.

The starting point of this thesis is the variation in the degree of executive strength among the post-Suharto presidents. Wahid was a weak president in both constitutional and partisan aspects. Since he was elected and could be dismissed by the MPR, he had no security of tenure. The absence of this protection also prevented him from establishing a consolidated partisan support. These institutional arrangements changed under Megawati. Though she still had no consolidated partisan support in parliament, she had a constitutionally-protected security of tenure due to the tightening of presidential impeachment procedures. Consequently, the degree of executive strength improved under her administration, to at least higher than that of Wahid. SBY exhibited the highest degree of executive strength among the post-Suharto presidents. This is because he was directly elected by the people,
and in addition, he benefited from the tightening of presidential impeachment procedures. Moreover, he had more consolidated partisan support in parliament. This variation in the presidents’ institutional profiles had a very significant effect on their achievements in economic policy reform.

Assessing the two main areas of economic policy reform, namely fiscal policy and investment policy, this thesis found a quite consistent pattern of policy-making across administrations. In both fiscal policy and investment policy areas, the Wahid administration (1999-2001) achieved extremely limited progress, with delay and reversals being a dominant pattern of policy-making. In the budget-making area, there was no reform on the spending side especially for subsidies as well as on deficit control and deficit financing making the target for enhancing fiscal sustainability extremely difficult to achieve. There was also no progress in privatization with no single enterprise being privatized during his administration. In fiscal related areas, his administration could only make minor amendments to tax policies. Similarly, in investment policy area, his administration failed to adopt policy reform in the energy sector. The case of the fuel subsidy reform only confirms this poor achievement.

The Megawati administration (2001-2004), in contrast, adopted many significant economic policy reforms in these two areas of interest with consequential effects on the restoration of macroeconomic stability and fiscal sustainability. The budget-making process was relatively technocratic. Spending was tightened, the deficit was brought under control, and deficit financing relied mostly on domestic resources. This helped enhance fiscal sustainability. Her administration adopted many fiscal-related policy reforms such as the passage of Law 14/2002 on Tax Court, Law 24/2002 on Treasury Bond, and Law 3/2004 on the Amendments of the Central Bank Law. Others were the passage of Law 17/2003 on State Finance and Law 1/2004 on State Treasury. Her administration also achieved significant progress in the privatization area by privatizing some strategic state enterprises. In addition, her administration adopted many significant reforms in investment area by the passage of Law 22/2001 on Oil and Gas, Law 20/2002 on Electricity, Law 13/2003 on Workforce, Law 2/2004 on the Settlement of Industrial Disputes, and Law 7/2004 on Water Resources. The case of the fuel subsidy reform points to this improved achievement though her administration backed down on part of its decision in this area in January 2003.
Under the SBY administration (2004-2007), there were more significant economic policy reforms in both areas. His administration applied a very technocratic approach in the budget-making process by maintaining very tight control over the budget deficit against an increasingly assertive DPR. Reforms were especially significant on the budget spending side as illustrated by the case of the education allocation. Due to these bold measures, macroeconomic stability was enhanced and fiscal sustainability improved even further from what had been achieved under the Megawati administration. It also adopted significant tax amendments by the passage of Law 28/2007 and pushed privatization when required. This achievement was even more significant if we look at the investment area. The passages of PP 3/2005 in response to the annulment of the Electricity Law, PERPRES 36/2005 on the land provision for public interests, PERPU 1/2007 on special economic zones, Law 17/2006 on the Amendments of Custom Law, and Law 25/2007 on Investment were all creditable achievements of his administration. It also adopted significant reform in the fuel subsidy, the most significant one in the post-Suharto era.

Putting these three administrations in comparison, this thesis found that, as far as economic policy reform is concerned, the SBY administration has performed the best compared to his two predecessors. The Megawati administration also performed fairly well, at least better than Wahid but not as well as SBY. This is also to say that the achievement of the Wahid administration in economic policy reform is the lowest one. Table 6.1 summarizes this achievement.
Table 6.1 Comparison of the achievements in economic policy reform among Wahid, Megawati and SBY

<table>
<thead>
<tr>
<th>No</th>
<th>Policy area</th>
<th>Proposed reform</th>
<th>Wahid</th>
<th>Megawati</th>
<th>SBY</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Fiscal policy</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>A. Budget making</td>
<td>Increasing revenue</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Targeting spending</td>
<td>No</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Controlling deficit</td>
<td>No</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Financing deficit</td>
<td>No</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td></td>
<td>B. Fiscal-related reform</td>
<td>Tax reform</td>
<td>Yes</td>
<td>Yes / No</td>
<td>Yes</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Privatization</td>
<td>No</td>
<td>Only to cover deficit</td>
<td>Not a priority</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Others</td>
<td>n.a.</td>
<td>Law 19/2003</td>
<td>n.a.</td>
</tr>
<tr>
<td>2</td>
<td>Investment</td>
<td>Energy sector</td>
<td>No</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Infrastructure</td>
<td>n.a.</td>
<td>Law 22/2001</td>
<td>n.a.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Investment law amendment</td>
<td>n.a.</td>
<td>Law 20/2002</td>
<td>n.a.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Special economic zone</td>
<td>n.a.</td>
<td>PERPRES 36/2005</td>
<td>Yes</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Custom</td>
<td>n.a.</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>3</td>
<td>Fuel subsidy</td>
<td>Cutting fuel subsidy allocation</td>
<td>No</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Increasing fuel price</td>
<td>No</td>
<td>Yes / No</td>
<td>Yes</td>
</tr>
</tbody>
</table>

Automatic adjustment in 2002
Partial reversal in 2003
The table shows almost no difference between the Megawati and SBY administrations. However, a closer look will reveal at least three major differences. First, in the area of fuel subsidy reform – which together with privatization is the most controversial reform agendas – Megawati had to back down on part of her decision in early 2003 due to strong opposition from the DPR. This was not the case for SBY when he adopted reforms in the same area in a very bold manner amidst strong opposition from the DPR, the strongest compared to what Megawati and Wahid had to face. The second important difference is in the area of privatization. While the Megawati administration put privatization as one of the priorities for policy reform, it was only able to push privatization to cover budget deficit. Many other state enterprises were maintained at their status. On the other hand, the SBY administration put scant enthusiasm on privatization; it instead focused on restructuring. However, it was able to privatize some enterprises to cover budget deficit when it was required to do so. The third difference is the way through which policy reform has been adopted. Megawati always followed ‘normal’ procedures by ‘legislating through the DPR’. There was no important reform initiative adopted beyond this ‘normal’ procedure. In contrast, SBY combined a similar strategy with other approaches which by-passed the DPR. He issued several high profile policies using his presidential prerogative. This is a risky but smart move, taken simply to avoid a complex and time-consuming legislative procedure which must comply with the DPR’s Rules of Procedure. Some of these initiatives were then brought to the DPR to be voted for and, given his consolidated partisan support in the DPR, he was able to adopt these initiatives such as in the case of the passage of PERPU 1/2007. This approach triggered very strong opposition from the DPR but it failed to stop the president from moving forward. Megawati – not to mention Wahid – could not apply this approach given her weak partisan support.

Comparing the three administrations simultaneously, a stark contrast is found especially between the Wahid administration on the one hand and the Megawati and SBY administration on the other hand. I have argued in this thesis that while there were some similarities regarding the economic conditions surrounding them and fragmented nature of power, the degree of executive strength held by each president varied highly. What distinguishes Wahid from Megawati and SBY in this respect is his vulnerability to dismissal by the MPR and therefore his lack of independence in making painful decisions. It is these very institutional arrangements that forced Wahid to try to maintain support for
his survival in the parliament at the cost of reform. DPR opposition to any reform agenda almost always led to maintenance of the status quo, even when compelling reform was required.

Megawati and SBY suffered no such institutional vulnerability and this helped them perform better than Wahid. While power was still fragmented among many actors in parliament and outside, they were protected from parliamentary dismissal. Consequently, they could adopt some significant policy reforms compared to what Wahid could do.

Amidst this similarity, one important thing distinguishes SBY from Megawati. He was directly elected by the people with constitutional protection over uninterrupted terms of office. This enabled him to establish a more limited but consolidated coalition. This was not the case for Megawati. She was elected by the MPR. To maintain support for her survival in parliament in her early months, she established an oversized coalition that included all major parties with the self-exclusion of PKB and PK. Thus, her partisan support was not as reliable and consolidated as SBY’s. Though the constitution restored her power soon after her election, her legislative support remained weak. As discussed previously, this difference has proven to be important for the adoption of difficult economic policy reform. Due to the presence of consolidated support in the DPR, SBY was able to adopt many significant policy reforms in the face of strong opposition from both the DPR and the people. As for Megawati, opposition from the DPR sometimes caused her to cancel or review policy reform that had already been announced such as in the case of the fuel subsidy reform in early 2003. Similarly, though privatization made significant progress during her administration, it could not progress beyond meeting the budget target.

Considering these findings, this thesis concludes that the new institutional arrangements have had a very significant effect on policy outcome. In the policy-making arena, this thesis has shown that different institutional arrangements produce different degrees of executive strength which permit different styles of policy leadership. In a period when a president has weak executive strength, the policy-making process is marked mostly by compromise, delay and even reversal. This is clearly a serious problem for situations requiring a timely and decisive response when the cost of delay is high. The opposite is true for periods when a president has a high degree of executive strength.
With this conclusion at hand, I am not arguing that other factors such as interest, idea, personality, or social and economic conditions are not important. Indeed, they are. Interest was especially important such as in the case of fuel subsidy reform in the last year of the Megawati administration and privatization under the SBY administration. However, as other alternative explanations, it is inadequate to explain the variation of the achievements of the post-Suharto presidents in economic policy reform. For example, it is true that the DPR mounted strong opposition to all reform agendas under our investigation. Why then could one administration push through these agendas while other could not? Personality-based explanation also faces the same problem. Though a president as populist as Wahid and as nationalist as Megawati had committed themselves to push through market-oriented reforms, the achievements in economic policy reform had been varied. SBY was also seen as the most technocratic leader with strong commitment to push through economic policy reform. However, his administration failed to push through reform in its early months.

6.2 Contributions and implications

Having concluded that the new institutional arrangements have had a significant effect, this thesis makes at least two major contributions, one practical and one theoretical. At a practical level, the findings of this thesis imply that the new institutional arrangements have been at play with some significant positive effects. Therefore, the calls for the restoration of the old institutional arrangements including the original 1945 Constitution must be carefully taken notice of.198 Such calls are best understood as a hasty response to the problems embedded in the new democratic institutions which are assumed to be unable to bring about the expected results. These problems are partly institutional. For example, this thesis has shown that the absence of sufficient legislative powers, both veto and decree powers, forced all post-Suharto presidents to establish a majority coalition to achieve any legislative agenda. This came with different degree of success and this is related to the presence or absence of the executive’s security of tenure. This thesis would argue that the

198 There were criticisms that the constitutional amendment had gone “too far”, endangering the future of Indonesia. Some elements including the former president, Abdurrahman Wahid, and some retired generals called for the annulment of the amendment. Meanwhile, those who proposed a further constitutional amendment such as the DPD received only limited support from the current parliament (Detikcom 04 July 2006; Detikcom 12 July 2006; Detikcom 29 January 2007; Detikcom 19 July 2007; Kompas 07 August 2003; Kompas 15 February 2005; Kompas 19 June 2006).
government's policy-making capacity could be further improved if the executive has sufficient legislative powers. It is even very important since the president is now directly elected by the people.

The other important aspect is the coming of multiparty system to Indonesian politics since 1999. This thesis has also shown that this new institutional profile has posed serious challenges for an efficient policy-making process especially when timely response was required. With the parliament being more assertive in the policy-making process and transforming itself into a superbody institution (Thohari 2003; Ziegenhain 2008:2), the fragmentation of power in the parliament made the policy-making process less efficient. Moreover, the use of “deliberation to reach agreement” (musyawarah untuk mufakat) principle made it really difficult for a president to push through his or her own legislative agenda. For this reason, there have been extensive debates among scholars to simplify the current party system. It is argued that the number of parties correlates negatively with government effectiveness. The higher the number of parties, the lower government effectiveness is (Kompas 28 June 2007). Worse than that, there exists a strong anti-party sentiment among Indonesians and they aspire to a reduction in the role of parties in Indonesian politics (Tan 2002; Gazali 2007). This is a dangerous development not only for the future of political parties but also for democracy itself. Simplifying the party system is seen as a key answer to this condition. However, this seems politically unfeasible and has been facing strong opposition since 1999. What the DPR and the president have tried to do since at least 2002 is only reduce the number of parties. Entry requirement is tightened resulting in the reduction of election contestants by half in the 2004 election compared to the 1999 election. Another attempt is by increasing the electoral threshold. For the 2004 election, the electoral threshold was 3 per cent. For the conduct of the 2009 election, the

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199 As far as the policy-making process is concerned, it is the DPR’s Rules of Procedure that matter. The executive must submit itself to this while the DPR sometimes manipulates it to deprive presidents of authority though there is recognition that both branches have equal status. For this reason, as I have argued previously, the president must have strong partisan support in the DPR.

200 One example of this is the proposal for an independent candidature in local government elections. In response to public pressure, the Constitutional Court opened up the chance for independent candidates in the election for governor or mayor. For Bhakti (2007), this raises concern about deparpolisasi — marginalizing the role of parties even in election.

201 There is a fatal misunderstanding on the concept of electoral threshold. While its standard meaning is the minimum percentage of votes a party must receive, either nationally or within a particular district, to get any seats in the parliament, in Indonesia it is understood as the minimum percentage of votes a party must receive to take part in the next election.
amendment proposal intends to increase it to 5 per cent which enables only seven parties (GOLKAR, PDIP, PKB, PPP, PD, PKS and PAN) to compete.\textsuperscript{202} However, as seen in Law 22/2007, the amendment failed to push through this proposal and thereby maintain the current arrangement due to opposition from small parties. Law 10/2008 then balances the tension by stipulating the electoral threshold of 3% and the parliamentary threshold of 2.5% of the national valid votes. Another idea for the application of a district system faces even stronger opposition also mainly from the small parties.

Whether these ideas are important for improving government effectiveness or not are still subject to debate and they must be considered carefully. This thesis has shown that, as long as the policy-making capacity is concerned, the current institutional arrangements are supportive of government effectiveness. The presence of a fragmented parliament with many parties having noisy voices over any policy agenda is not too serious a liability for the policy-making process as far as the president has a constitutional protection over security of tenure as were in the cases of Megawati and SBY. The only challenge to a president under this institutional context is how to establish a sufficient coalition to achieve a legislative majority when a president comes from a minority party. Therefore, criticisms over the negative side of the current party system is more to do with the way political elites exercise their power than with government effectiveness in general. Moreover, the danger of having a dominant party as under the New Order regime is far from over.

There are many more related proposals for further institutional reform.\textsuperscript{203} It is difficult to assess the effect of such proposals on certain political outcomes and it is beyond the reach of this thesis to speculate on this. Such proposals are best understood as an acknowledgement of the importance of political institutions.

This practical contribution is important if we link it to the other agenda in contemporary Indonesia, namely, democratic consolidation. Early in Chapter 1 this thesis raised the issue of the importance of government capacity for the prospect of democratic consolidation.

\textsuperscript{202} My personal in-depth interview with MPs from GOLKAR (Jakarta, 23 February 2006) also confirms that it is their interest to simplify the party system with the target of having only three to four parties that will win parliamentary seats in the 2009 election. The reasons are to establish a strong government and enhance party-voter identification.

\textsuperscript{203} Among the examples are the proposals for the introduction of independent presidential candidates and the conduct of presidential election prior to the parliamentary election (Kompas 03 June 2007).
While the majority of Indonesian people have chosen democracy as the best political system, averagely 71 per cent for the period of 1999 to 2006, it is still far from secure for a democratizing country (Mujani 2006). If we adapt to Schedler’s arbitrary yet reasonable measurement of democratic consolidation requiring 66 per cent of the population accepting democracy as the best system (Schedler 2001:84), Indonesia has performed relatively well toward democratic consolidation. However, Mujani (2006) also notes that compared to the average level of democratic consolidation for the established democracies, that is, 84 per cent, more efforts are clearly required. In addition, as far as economic performance is concerned, the prospects of democratic consolidation are far from certain. Many surveys conducted since 1999 to 2007 show that government’s economic performance has consistently been the most important concern for the people (Asia Foundation 2003; CESDA-LP3S 2003; IFES 2003; IFES 2005; LSI 2007). This is empirically justified given the economic conditions people have been facing since the 1997 economic crisis. Under such circumstances, the prospects of democracy are still highly vulnerable and cannot be taken for granted. Boediono (2007:16) calls it ‘a high-risk zone’.

While this concern is noteworthy, again, there is reason for optimism since the government’s capacity has far improved under the current institutional arrangements. For this performance to be further improved to meet people’s expectations, the role of political institutions alone is not sufficient. There are many other factors for this project, some of them even create more uncertainty than reduce it. However, political institutions are an important factor to reduce this uncertainty.

At a more theoretical level, this thesis has made at least three important contributions. First, it has shown that political institutions have had a significant effect on the government’s policy-making capacity. While acknowledging the effect of other factors such as interest, the personality of the president, and social economic conditions, this thesis has shown that political institutions can make a big difference to policy outcomes by providing a structure of incentives, including both opportunities and risks. It is the political institutions that bias the effect of other factors resulting in the variation of political outcomes. Therefore, though

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204 Klingemann (1999 as quoted in Mujani 2006) presents the following figures: Germany 93 per cent, USA 88 per cent, and Japan 88 per cent.

205 In this respect, Gibson (1996:396) might be correct when he anecdotally argues that democracy can be ‘a mile wide but an inch deep’.

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this thesis is more a theory-proposing than a theory-testing one, it has made a significant contribution to the existing literature on Indonesia. This contribution would be even more significant if scholars undertook statistical tests so that a more robust conclusion can be drawn. There is a rich agenda in this field for future research. This will bring political institutions back into the study of Indonesian politics.

Second, at a more ambitious level, this thesis also makes a significant contribution to the comparative literature on the effect of political institutions in general. Along with the shift of debates from “do institutions matter?” to “how do institutions matters”, this thesis has an important contribution to the comparative institutional literature. With very few exceptions, Indonesia is a relatively neglected subject in this area for the reason discussed in Chapter 1. It is left far behind compared to, for example, Latin American countries especially when scholars try to connect certain institutional profile to certain political outcome. Now, with the restoration of democratic arrangements, research on Indonesia such as this can bring more insights to the comparative literature on the effect of political institutions. Its significance cannot be ignored since Indonesia is the world’s fourth most populated with the largest Moslem population having an important role in world politics.

The third important contribution of this thesis is when it is connected to the broader literature on policy reform. This thesis started with an extensive discussion to find a proper institutional optic to understand the achievements in policy reform of the post-Suharto administrations. In this respect, while acknowledging the importance of power concentration, elite insulation or autonomy, elite cohesion, and veto players as alternative institutional approaches to capture the achievement in policy reform, this thesis has offered another optic by looking at the degree of executive strength. Some authors might dub the latter as an individual property such as leadership quality. In contrast to this, this thesis treats it as an institutional attribute, namely, an aggregated measure of a president’s constitutional power and partisan support. Looking back to the Indonesia literature, even when some authors have employed institutional approach to understand the achievements in policy reform, this is a relatively novel approach. By bringing this to Indonesia literature, this thesis has filled another gap in the existing Indonesia literature while at the same time putting Indonesia into a broader literature on institutions and policy reform. Such
contribution will be more enhanced by further research using institutional approach to look at more political outcomes.

6.3 Concluding remarks

In concluding that the new institutional arrangements matter for the achievements in economic policy reform and highlighting some implications of this thesis, I also realize some limitations. The thesis focuses only on policy-making capacity while there are many other aspects that require serious attention. For example, some analysts argue that what matters is implementation (Basri and Patunru 2006:313). Vice-president Jusuf Kalla has also expressed this concern (Kompas 04 December 2007). For this reason, other scholars such as McLeod (2005b) have made recommendation on the importance of reforming the disoriented bureaucracy. Compared to other government institutions, the Indonesian bureaucracy has not been subject to significant reform despite its notorious malfunctioning. Law enforcement is another important aspect. There is a rich agenda for further research in those areas.

Even if one can simply ignore the former limitation, another limitation rises and needs attention. This thesis has only been able to pay attention to economic policy reform which is not the only government priority. There are many other important issues which require further investigation such as decentralization, corruption eradication, judicial reform, civil-military relations, and communal conflicts. These are also important areas where the government is required to improve its performance. Whether government performance in these areas is affected by the new institutional arrangements or not needs further inquiry. However, the implications for the future of democratic consolidation are certainly similar. Again, there is a rich agenda for future research in these areas. What I have shown in this thesis is that institutional arrangements do matter for government policy-making capacity. Moreover, I assume that policy-making capacity is no less important than implementation. In many areas, it is the lack of policy direction coming from poor policy-making that has exacerbated the performance in policy implementation.
Despite these limitations, I hope this thesis makes a significant contribution. It argues for an alternative way of looking at certain policy outcomes by causally connecting them to the political institutions. This has been a relatively neglected approach in the Indonesia literature even after the restoration of democratic system since 1999. Therefore, this thesis is best seen as a pioneering enterprise to assess the effects of political institutions on the more nuanced and micro level issue of governance.\textsuperscript{206} Further research such as this will make even more significant contributions to the Indonesian literature. This is also important for bringing Indonesia to the broader comparative literature especially on the importance of political institutions.

\textsuperscript{206} Putting in the comparative academic works, this thesis can be seen as a response to Power and Gasiorowski's (1997:151) invitation to focus further research on the nexus between institutional variables and governability issues or the quality of democratic life rather than democratic survival.
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Law 15/1985 on Electricity
Law 10/1995 on Custom
Law 25/1997 on Workforce
Law 16/2000 on General Taxation Arrangements and Procedures
Law 17/2000 on Income Tax
Law 18/2000 on Value Added and Luxury Taxes.
Law 19/2000 on Tax Collection by Force
Law 20/2000 on the Amendment of the Land and Building Charges
Law 25/2000 on the National Development Plan (PROPENAS)
Law 22/2001 on Oil and Gas
Law 14/2002 on the Tax Court
Law 17/2002 on the Calculation of the 2000 Budget
Law 20/2002 on Electricity
Law 24/2002 on Treasury Bond
Law 13/2003 on Workforce
Law 14/2003 on the Calculation of the 2001 Budget
Law 17/2003 on State Finance
Law 19/2003 on the State-Owned Enterprises
Law 20/2003 on the National Education System
Law 23/2003 on the Election of the President and Vice-President
Law 24/2003 on Constitutional Court
Law 1/2004 on State Treasure
Law 2/2004 on the Settlement of Industrial Disputes
Law 3/2004 on the Amendment of the Central Bank Law
Law 7/2004 on Water Resources
Law 36/2004 on the 2005 National Budget
Law 2/2006 on the Calculation of the 2003 Budget
Law 17/2006 on the Amendment of the Custom Law
Law 22/2007 on General Election
Law 25/2007 on Investment
Law 28/2007 on the Amendment of the General Taxation Arrangements and Procedures
Law 44/2007 on Free Trade and Port Areas
KEPPRES No.135/2000 on Domestic Fuel Prices
KEPPRES 45/2001 on Domestic Fuel Prices
KEPPRES 73/2001 on Domestic Fuel Prices
KEPPRES 9/2002 on Domestic Fuel Prices
KEPPRES 90/2002 on Domestic Fuel Prices
MPR Decree No.IV/MPR/1999 on Broad Guidelines of State Policy
MPR Decree No III/MPR/2000 on Legal Sources and Hierarchy
MPR Decree No.X/MPR/2001 on the Recommendations for the Reports on the Implementation of the MPR Decree by the President, DPA, DPR, BPK and MA

MPR Decree No.VI/MPR/2002 on the Recommendations for the Reports on the Implementation of the MPR Decree by the President, DPA, DPR, BPK and MA

PERPRES 22/2005 on Domestic Fuel Prices

PERPRES 36/2005 on the Land Provision for Public Interest

PERPRES 55/2005 on Domestic Fuel Prices

PERPU 1/2007 on Free Trade and Port Areas

PP 3/2005 on the Provision and Use of Electricity Power
### Appendices

#### Appendix 1 Results of the 1999 general election

<table>
<thead>
<tr>
<th>Political Parties</th>
<th>Percentage of votes</th>
<th>Number of seat</th>
<th>Percentage of DPR's seat</th>
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<td>7</td>
<td>1.5</td>
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<td>PPIM</td>
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<td>PNI FM</td>
<td>0.35</td>
<td>1</td>
<td>0.22</td>
</tr>
<tr>
<td>PBI</td>
<td>0.34</td>
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<td>0.22</td>
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<td>PNI MM</td>
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<td>0.22</td>
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<td>IPKI</td>
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<tr>
<td>PKU</td>
<td>0.28</td>
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<tr>
<td>PKD</td>
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<td>1</td>
<td>0.22</td>
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<tr>
<td>Others (27 parties)</td>
<td>3.83</td>
<td>..</td>
<td>..</td>
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<td>Total</td>
<td>100</td>
<td>462</td>
<td>100</td>
</tr>
<tr>
<td>Effective number of parties (ENP)</td>
<td>5.15</td>
<td>4.71</td>
<td>4.71</td>
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Source: Author’s calculation from the General Election Commission (available at www.kpu.go.id)
# Appendix 2 Structure of the First National Unity Cabinet

<table>
<thead>
<tr>
<th>No.</th>
<th>Position</th>
<th>Name</th>
<th>Affiliation</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>President</td>
<td>Abdurrahman Wahid</td>
<td>PKB</td>
</tr>
<tr>
<td>2</td>
<td>Vice President</td>
<td>Megawati Soekarnoputri</td>
<td>PDIP</td>
</tr>
<tr>
<td>3</td>
<td>Coordinating Minister for Political Affairs and Security</td>
<td>General Wiranto</td>
<td>ABRI</td>
</tr>
<tr>
<td>4</td>
<td>Minister of Home Affairs</td>
<td>Lt. Gen (ret) Surjadi Soedirjda</td>
<td>ABRI</td>
</tr>
<tr>
<td>5</td>
<td>Minister of Foreign Affairs</td>
<td>Alwi Sihab</td>
<td>PKB</td>
</tr>
<tr>
<td>6</td>
<td>Minister of Defense</td>
<td>Juwono Soedarsono</td>
<td>Non-partisan</td>
</tr>
<tr>
<td>7</td>
<td>Minister of Law and Legislation</td>
<td>Yusril Ihza Mahendra</td>
<td>PBB</td>
</tr>
<tr>
<td>8</td>
<td>Coordinating Minister for the Economy, Finance and Industry</td>
<td>Kwik Kian Gie</td>
<td>PDIP</td>
</tr>
<tr>
<td>9</td>
<td>Minister of Finance</td>
<td>Bambang Sudibyo</td>
<td>PAN</td>
</tr>
<tr>
<td>10</td>
<td>Minister of Mining and Energy</td>
<td>Lt. Gen. (ret) Susilo Bambang Yudhoyono</td>
<td>ABRI</td>
</tr>
<tr>
<td>11</td>
<td>Minister of Industry and Trade</td>
<td>Yusuf Kalla</td>
<td>GOLKAR</td>
</tr>
<tr>
<td>12</td>
<td>Minister of Agriculture</td>
<td>M Prakosa</td>
<td>PDIP</td>
</tr>
<tr>
<td>13</td>
<td>Minister of Forestry and Plantation</td>
<td>Nur Mahmudi Ismail</td>
<td>PK</td>
</tr>
<tr>
<td>14</td>
<td>Minister of Transportation</td>
<td>Let. Gen (ret) Agum Gumelar</td>
<td>ABRI</td>
</tr>
<tr>
<td>15</td>
<td>Minister of Maritime Exploration</td>
<td>Sarwono Kusumaatmadja</td>
<td>PKP</td>
</tr>
<tr>
<td>16</td>
<td>Coordinating Minister of People’s Welfare and Poverty Eradication</td>
<td>Hamzah Haz</td>
<td>PPP</td>
</tr>
<tr>
<td>17</td>
<td>Minister of Manpower</td>
<td>Bomer Pasaribu</td>
<td>GOLKAR</td>
</tr>
<tr>
<td>18</td>
<td>Minister of Health</td>
<td>Achmad Sujudi</td>
<td>Non-partisan</td>
</tr>
<tr>
<td>19</td>
<td>Minister of National Education</td>
<td>Yahya Muhaimin</td>
<td>PAN</td>
</tr>
<tr>
<td>20</td>
<td>Minister of Religious Affairs</td>
<td>Tolchah Hasan</td>
<td>PKB</td>
</tr>
<tr>
<td>21</td>
<td>Minister of Settlement and Regional Development</td>
<td>Erma Witoelar</td>
<td>Non-partisan</td>
</tr>
</tbody>
</table>

State Ministers

<table>
<thead>
<tr>
<th>No.</th>
<th>Position</th>
<th>Name</th>
<th>Affiliation</th>
</tr>
</thead>
<tbody>
<tr>
<td>22</td>
<td>Minister of Research and Technology</td>
<td>A.S. Hikam</td>
<td>PKB</td>
</tr>
<tr>
<td>23</td>
<td>Minister of Cooperatives and Small and Medium Enterprises</td>
<td>Zarkasih Nur</td>
<td>PPP</td>
</tr>
<tr>
<td>24</td>
<td>Minister of Environment</td>
<td>Soni Keraf</td>
<td>PDIP</td>
</tr>
<tr>
<td>25</td>
<td>Minister of Regional</td>
<td>Ryaas Rasyid</td>
<td>Non-partisan</td>
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<tr>
<td>No.</td>
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<td>Party</td>
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<td>-------------------------------------------</td>
<td>------------</td>
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<tr>
<td>26</td>
<td>Minister of Tourism and Arts</td>
<td>Hidayat Jaelani</td>
<td>Non-partisan</td>
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<tr>
<td>27</td>
<td>Minister of Investment and State-Owned Enterprises</td>
<td>Laksamana Sukardi</td>
<td>PDIP</td>
</tr>
<tr>
<td>28</td>
<td>Minister of Youth Affairs and Sports</td>
<td>Mahadi Sinambela</td>
<td>GOLKAR</td>
</tr>
<tr>
<td>29</td>
<td>Minister of Public Works</td>
<td>Rafik Boediro Soetjipto</td>
<td>Non-partisan</td>
</tr>
<tr>
<td>30</td>
<td>Minister of Women’s Affairs</td>
<td>Khofifah Indar Parawangsa</td>
<td>PKB</td>
</tr>
<tr>
<td>31</td>
<td>Minister of Human Rights</td>
<td>Hasbahal M. Saad</td>
<td>PAN</td>
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<tr>
<td>32</td>
<td>Minister of Transmigration and Population</td>
<td>Al Hilal Hamdi</td>
<td>PAN</td>
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<tr>
<td>33</td>
<td>Minister of State Administrative Reform</td>
<td>Vice Admiral Freddy Numbery</td>
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</tr>
<tr>
<td>34</td>
<td>Minister of Social Affairs</td>
<td>Anak Agung Gde Agung</td>
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<tr>
<td>35</td>
<td>Attorney General</td>
<td>Marzuki Darusman</td>
<td>GOLKAR</td>
</tr>
<tr>
<td>36</td>
<td>Commander of Armed Forces (ABRI)</td>
<td>Admiral Widodo A.S.</td>
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<tr>
<td>37</td>
<td>State Secretary</td>
<td>Ali Rahman</td>
<td>Non-partisan</td>
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### Appendix 3 Structure of the second National Unity Cabinet

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<th>Position</th>
<th>Name</th>
<th>Affiliation</th>
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<tbody>
<tr>
<td>1</td>
<td>President</td>
<td>Abdurrahman Wahid</td>
<td>PKB</td>
</tr>
<tr>
<td>2</td>
<td>Vice President</td>
<td>Megawati Soekarnoputri</td>
<td>PDIP</td>
</tr>
<tr>
<td>3</td>
<td>Coordinating Minister for Political Affairs and Security</td>
<td>General Susilo Bambang Yudhoyono</td>
<td>ABRI</td>
</tr>
<tr>
<td>4</td>
<td>Minister of Home Affairs</td>
<td>Lt. Gen (ret) Surjadi Soedirdja</td>
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</tr>
<tr>
<td>5</td>
<td>Minister of Foreign Affairs</td>
<td>Alwi Sihab</td>
<td>PKB</td>
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<td>6</td>
<td>Minister of Defense</td>
<td>Mahfud M.D.</td>
<td>PKB</td>
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<td>7</td>
<td>Minister of Justice and Human Rights</td>
<td>Yusril Ihza Mahendra</td>
<td>PBB</td>
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<tr>
<td>8</td>
<td>Coordinating Minister for the Economy</td>
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</tr>
<tr>
<td>9</td>
<td>Minister of Finance and State-Owned Enterprises</td>
<td>Prijadi Praptosuhardjo</td>
<td>Non-partisan</td>
</tr>
<tr>
<td>10</td>
<td>Minister of Energy and Mineral Resources</td>
<td>Purnomo Yusgiantoro</td>
<td>Non-partisan</td>
</tr>
<tr>
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<td>Minister of Industry and Trade</td>
<td>Let.Gen. (ret) Luhut B. Panjaitan</td>
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<tr>
<td>12</td>
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<td>Bungaran Saragih</td>
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<td>13</td>
<td>Minister of Transportation and Telecommunication</td>
<td>Let. Gen (ret) Agum Gumelar</td>
<td>ABRI</td>
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<tr>
<td>14</td>
<td>Minister of Maritime and Fishery Affairs</td>
<td>Sarwono Kusumaatmadja</td>
<td>PKP</td>
</tr>
<tr>
<td>15</td>
<td>Minister of Manpower and Transmigration</td>
<td>Al Hilal Hamdi</td>
<td>PAN</td>
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<td>16</td>
<td>Minister of Health and Social Welfare</td>
<td>Achmad Sujudi</td>
<td>Non-partisan</td>
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<td>17</td>
<td>Minister of National Education</td>
<td>Yahya Muhaimin</td>
<td>PAN</td>
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<td>18</td>
<td>Minister of Religious Affairs</td>
<td>Tolchah Hasan</td>
<td>PKB</td>
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<td>19</td>
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<tr>
<td>20</td>
<td>Minister of Culture and Tourism</td>
<td>I Gde Ardhiaka</td>
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**State Ministers**

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<tr>
<th>No</th>
<th>Position</th>
<th>Name</th>
<th>Affiliation</th>
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<td>21</td>
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<td>A.S. Hikam</td>
<td>PKB</td>
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<tr>
<td>22</td>
<td>Minister of Cooperatives and Small and Medium Enterprises</td>
<td>Zarkasih Nur</td>
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<td>Minister of Environment</td>
<td>Soni Keraf</td>
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<td>Minister of Women’s Affairs</td>
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<td>PKB</td>
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<td>25</td>
<td>Minister of State Administrative Reform</td>
<td>Ryaas Rasyid</td>
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<td>26</td>
<td>Attorney General</td>
<td>Marzuki Darusman</td>
<td>GOLKAR</td>
</tr>
<tr>
<td>27</td>
<td>Commander of Armed Forces (ABRI)</td>
<td>Admiral Widodo A.S.</td>
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<tr>
<td>No.</td>
<td>Position</td>
<td>Name</td>
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<td></td>
<td></td>
<td>Junior Minister</td>
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<tr>
<td>29</td>
<td>Junior Minister of Forestry</td>
<td>Nurmahmudi Ismail</td>
<td>PK</td>
</tr>
<tr>
<td>30</td>
<td>Junior Minister for the Acceleration of Eastern Indonesian Development</td>
<td>Manuel Kaisepo</td>
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</tr>
<tr>
<td>31</td>
<td>Junior Minister for National Economic Restructurization</td>
<td>Cacuk Sudarjanto</td>
<td>Non-partisan</td>
</tr>
</tbody>
</table>

**Source:** Author’s compilation from Simandjuntak, P.N.H., 2003. *Kabinet-Kabinet Republik Indonesia dari Awal Kemerdekaan sampai Reformasi* [The Cabinets of the Republic of Indonesia from its Independence to Reform Era], Djambatan, Jakarta; various publications.
## Appendix 4 Structure of the Gotong Royong Cabinet

<table>
<thead>
<tr>
<th>No</th>
<th>Position</th>
<th>Name</th>
<th>Affiliation</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>President</td>
<td>Megawati Soekarnoputri</td>
<td>PDIP</td>
</tr>
<tr>
<td>2</td>
<td>Vice President</td>
<td>Hanzah Haz</td>
<td>PPP</td>
</tr>
<tr>
<td>3</td>
<td>Coordinating Minister for Political Affairs and Security</td>
<td>General (ret) Susilo Bambang Yudhoyono</td>
<td>ABRI</td>
</tr>
<tr>
<td>4</td>
<td>Minister of Home Affairs</td>
<td>Lt. Gen (ret) Hari Sabarno</td>
<td>ABRI</td>
</tr>
<tr>
<td>5</td>
<td>Minister of Foreign Affairs</td>
<td>Hasan Wirayuda</td>
<td>Non-partisan</td>
</tr>
<tr>
<td>6</td>
<td>Minister of Defense</td>
<td>Matori Abdul Jalil (former PKB)</td>
<td>Non-partisan</td>
</tr>
<tr>
<td>7</td>
<td>Minister of Justice and Human Rights</td>
<td>Yusri Ihza Mahendra</td>
<td>PBB</td>
</tr>
<tr>
<td>8</td>
<td>Coordinating Minister for the Economy</td>
<td>Dorodjatun Kuncorojakti</td>
<td>Non-partisan</td>
</tr>
<tr>
<td>9</td>
<td>Minister of Finance</td>
<td>Boediono</td>
<td>Non-partisan</td>
</tr>
<tr>
<td>10</td>
<td>Minister of Energy and Mineral Resources</td>
<td>Purnomo Yusgiantoro</td>
<td>Non-partisan</td>
</tr>
<tr>
<td>11</td>
<td>Minister of Industry and Trade</td>
<td>Rini M Soemarno Suwandi</td>
<td>PAN</td>
</tr>
<tr>
<td>12</td>
<td>Minister of Agriculture</td>
<td>Bungaran Saragih</td>
<td>PDIP</td>
</tr>
<tr>
<td>13</td>
<td>Minister of Forestry</td>
<td>M Prakosa</td>
<td>PDIP</td>
</tr>
<tr>
<td>14</td>
<td>Minister of Transportation</td>
<td>Lt. Gen (ret) Agum Gumelar</td>
<td>ABRI</td>
</tr>
<tr>
<td>15</td>
<td>Minister of Maritime and Fishery Affairs</td>
<td>Rohmin Dahuri</td>
<td>Non-partisan</td>
</tr>
<tr>
<td>16</td>
<td>Coordinating Minister for Social Welfare</td>
<td>Jusuf Kalla</td>
<td>Golkar</td>
</tr>
<tr>
<td>17</td>
<td>Minister of Manpower and Transmigration</td>
<td>Jacob Nuwa Wea</td>
<td>PDIP</td>
</tr>
<tr>
<td>18</td>
<td>Minister of Health</td>
<td>Achmad Sujudi</td>
<td>Non-partisan</td>
</tr>
<tr>
<td>19</td>
<td>Minister of National Education</td>
<td>Abdul Malik Fajar (Muhammadiyah)</td>
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<tr>
<td>20</td>
<td>Minister of Religious Affairs</td>
<td>Said Agiel Munawar (NU)</td>
<td>Non-partisan</td>
</tr>
<tr>
<td>21</td>
<td>Minister of Settlement and Regional Infrastructure</td>
<td>Soenarno</td>
<td>Non-partisan</td>
</tr>
<tr>
<td>22</td>
<td>Minister of Social Affairs</td>
<td>Bahtiar Chamsyah</td>
<td>PPP</td>
</tr>
</tbody>
</table>

**State Ministers**

<table>
<thead>
<tr>
<th>No</th>
<th>Position</th>
<th>Name</th>
<th>Affiliation</th>
</tr>
</thead>
<tbody>
<tr>
<td>23</td>
<td>Minister of Research and Technology</td>
<td>Hatta Radjasa</td>
<td>PAN</td>
</tr>
<tr>
<td>24</td>
<td>Minister of Cooperatives and Small and Medium Enterprises</td>
<td>Alimarwan Hanan</td>
<td>PPP</td>
</tr>
<tr>
<td>25</td>
<td>Minister of Environment</td>
<td>Nabiil Makarim</td>
<td>Non-partisan</td>
</tr>
<tr>
<td>26</td>
<td>Minister of Culture and Tourism</td>
<td>I Gde Artika</td>
<td>Non-partisan</td>
</tr>
<tr>
<td>27</td>
<td>Minister of State Administrative Reform</td>
<td>Feisal Tamin</td>
<td>Non-partisan</td>
</tr>
<tr>
<td>28</td>
<td>Minister for the Acceleration of Eastern Indonesian</td>
<td>Manuel Kaisepo</td>
<td>Non-partisan</td>
</tr>
<tr>
<td>No.</td>
<td>Ministry/Role</td>
<td>Name</td>
<td>Party</td>
</tr>
<tr>
<td>-----</td>
<td>--------------------------------------------------</td>
<td>-------------------</td>
<td>-------</td>
</tr>
<tr>
<td>29</td>
<td>Minister of National Development Planning/Head of BAPPENAS</td>
<td>Kwik Kian Gie</td>
<td>PDIP</td>
</tr>
<tr>
<td>30</td>
<td>Minister of State-Owned Enterprises</td>
<td>Laksamana Sukardi</td>
<td>PDIP</td>
</tr>
<tr>
<td>31</td>
<td>Minister of Women Empowerment</td>
<td>Sri Redjeki Soemaryoto</td>
<td>Golkar</td>
</tr>
<tr>
<td>32</td>
<td>Minister of Communication and Information</td>
<td>Syamsul Mu'arif</td>
<td>Golkar</td>
</tr>
<tr>
<td>33</td>
<td>State Secretary</td>
<td>Bambang Kesowo</td>
<td>Non-partisan</td>
</tr>
<tr>
<td>34</td>
<td>Attorney General</td>
<td>Muhammad Abdurrahman</td>
<td>Non-partisan</td>
</tr>
<tr>
<td>35</td>
<td>Head of National Intelligence Agency</td>
<td>AM Hendropriyono</td>
<td>ABRI</td>
</tr>
</tbody>
</table>

Source: Author’s compilation from Simandjuntak, P.N.H., 2003. *Kabinet-Kabinet Republik Indonesia dari Awal Kemerdekaan sampai Reformasi* [The Cabinets of the Republic of Indonesia from its Independence to Reform Era], Djambatan, Jakarta; various publications.
Appendix 5 The result of the 2004 Election

<table>
<thead>
<tr>
<th>Political parties</th>
<th>Percentage of vote</th>
<th>Number of seat</th>
<th>Percentage of seat</th>
</tr>
</thead>
<tbody>
<tr>
<td>GOLKAR</td>
<td>21.58</td>
<td>127</td>
<td>23.09</td>
</tr>
<tr>
<td>PDIP</td>
<td>18.53</td>
<td>109</td>
<td>19.82</td>
</tr>
<tr>
<td>PKB</td>
<td>10.57</td>
<td>52</td>
<td>9.45</td>
</tr>
<tr>
<td>PPP</td>
<td>8.15</td>
<td>58</td>
<td>10.55</td>
</tr>
<tr>
<td>PD</td>
<td>7.45</td>
<td>56</td>
<td>10.18</td>
</tr>
<tr>
<td>PKS</td>
<td>7.34</td>
<td>45</td>
<td>8.18</td>
</tr>
<tr>
<td>PAN</td>
<td>6.44</td>
<td>53</td>
<td>9.63</td>
</tr>
<tr>
<td>PBB</td>
<td>2.62</td>
<td>11</td>
<td>2.00</td>
</tr>
<tr>
<td>PBR</td>
<td>2.44</td>
<td>14</td>
<td>2.54</td>
</tr>
<tr>
<td>PDS</td>
<td>2.13</td>
<td>13</td>
<td>2.36</td>
</tr>
<tr>
<td>PKPB</td>
<td>2.11</td>
<td>2</td>
<td>0.36</td>
</tr>
<tr>
<td>PKPI</td>
<td>1.26</td>
<td>1</td>
<td>0.18</td>
</tr>
<tr>
<td>PPDK</td>
<td>1.16</td>
<td>4</td>
<td>0.72</td>
</tr>
<tr>
<td>PNIM</td>
<td>0.81</td>
<td>1</td>
<td>0.18</td>
</tr>
<tr>
<td>PP</td>
<td>0.77</td>
<td>3</td>
<td>0.54</td>
</tr>
<tr>
<td>PPDIC</td>
<td>0.75</td>
<td>1</td>
<td>0.18</td>
</tr>
<tr>
<td>Others (8 parties)</td>
<td>100</td>
<td>..</td>
<td>..</td>
</tr>
<tr>
<td>Total</td>
<td>94.11</td>
<td>550</td>
<td>100</td>
</tr>
<tr>
<td>Effective number of parties</td>
<td>8.55</td>
<td>7.10</td>
<td>7.11</td>
</tr>
</tbody>
</table>

Source: Author’s calculation from the General Election Commission (www.kpu.go.id)
### Appendix 6 Structure of the United Indonesia Cabinet

<table>
<thead>
<tr>
<th>No</th>
<th>Position</th>
<th>Name</th>
<th>Background</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>President</td>
<td>Susilo Bambang Yudhoyono</td>
<td>PD</td>
</tr>
<tr>
<td>2</td>
<td>Vice President</td>
<td>Jusuf Kalla</td>
<td>GOLKAR</td>
</tr>
<tr>
<td>3</td>
<td>Coordinating Minister for Political, Legal and Security Affairs</td>
<td>Adm. Widodo A.S.</td>
<td>Non-partisan (ABRI)</td>
</tr>
<tr>
<td>4</td>
<td>Minister of Home Affairs</td>
<td>Mohammad Ma’ruf</td>
<td>Non-partisan (ABRI)</td>
</tr>
<tr>
<td>5</td>
<td>Minister of Foreign Affairs</td>
<td>Hasan Wirajuda</td>
<td>Non-partisan</td>
</tr>
<tr>
<td>6</td>
<td>Minister of Defense</td>
<td>Juwono Sudarsono</td>
<td>Non-partisan</td>
</tr>
<tr>
<td>7</td>
<td>Minister of Justice and Human Rights</td>
<td>Hamid Awaluddin (Andi Mattalata)**</td>
<td>Non-partisan (GOLKAR)**</td>
</tr>
<tr>
<td>8</td>
<td>Coordinating Minister for the Economy</td>
<td>Aburizal Bakrie (Boediono)*</td>
<td>GOLKAR (Non-partisan)*</td>
</tr>
<tr>
<td>9</td>
<td>Minister of Finance</td>
<td>Jusuf Anwar (Sri Mulyani Indrawati)*</td>
<td>Non-partisan (Non-partisan)*</td>
</tr>
<tr>
<td>10</td>
<td>Minister of Energy and Mineral Resources</td>
<td>Purnomo Yusgiantoro</td>
<td>Non-partisan</td>
</tr>
<tr>
<td>11</td>
<td>Minister of Industry</td>
<td>Andung Nitimiharja (Fahmi Idris)*</td>
<td>Non-partisan (GOLKAR)*</td>
</tr>
<tr>
<td>12</td>
<td>Ministry of Trade</td>
<td>Mari Elka Pangestu</td>
<td>Non-partisan</td>
</tr>
<tr>
<td>13</td>
<td>Minister of Agriculture</td>
<td>Anton Apriyantono</td>
<td>PKS</td>
</tr>
<tr>
<td>14</td>
<td>Minister of Forestry</td>
<td>M.S. Kaban</td>
<td>PBB</td>
</tr>
<tr>
<td>15</td>
<td>Minister of Transportation and Communication</td>
<td>Hatta Radjasa (Jusman Syafii Djamal)**</td>
<td>PAN (Non-partisan)**</td>
</tr>
<tr>
<td>16</td>
<td>Minister of Maritime and Fishery Affairs</td>
<td>Freddy Numberi</td>
<td>Non-partisan</td>
</tr>
<tr>
<td>17</td>
<td>Coordinating Minister for Social Welfare</td>
<td>Alwi Shihab (Aburizal Bakri)*</td>
<td>PKB (GOLKAR)*</td>
</tr>
<tr>
<td>18</td>
<td>Minister of Manpower and Transmigration</td>
<td>Fahmi Idris (Erman Suparno)*</td>
<td>GOLKAR (PKB)*</td>
</tr>
<tr>
<td>19</td>
<td>Minister of Public Works</td>
<td>Djoko Kirmanto</td>
<td>Non-partisan</td>
</tr>
<tr>
<td>20</td>
<td>Minister of Health</td>
<td>Fadila Supari</td>
<td>Non-partisan</td>
</tr>
<tr>
<td>21</td>
<td>Minister of National Education</td>
<td>Bambang Sudibyo</td>
<td>PAN</td>
</tr>
<tr>
<td>22</td>
<td>Minister of Religious Affairs</td>
<td>M. Maftuh Basyuni</td>
<td>NU-Non partisan</td>
</tr>
<tr>
<td>23</td>
<td>Minister of Social Affairs</td>
<td>Bahtiar Chamsyah</td>
<td>PPP</td>
</tr>
</tbody>
</table>

**State Ministers**

<table>
<thead>
<tr>
<th>No</th>
<th>Position</th>
<th>Name</th>
<th>Background</th>
</tr>
</thead>
<tbody>
<tr>
<td>24</td>
<td>Minister of Research and Technology</td>
<td>Kusmayanto Kadiman</td>
<td>Non-partisan</td>
</tr>
<tr>
<td>25</td>
<td>Minister of Cooperatives and Small and Medium Enterprises</td>
<td>Suryadharma Ali</td>
<td>PPP</td>
</tr>
<tr>
<td>26</td>
<td>Minister of Environment</td>
<td>Rachmat Witoelar</td>
<td>GOLKAR</td>
</tr>
<tr>
<td>27</td>
<td>Minister of Culture and Tourism</td>
<td>Jerol Wacik</td>
<td>PD</td>
</tr>
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</table>

269
<table>
<thead>
<tr>
<th>No.</th>
<th>Ministry/Office</th>
<th>Name</th>
<th>Party</th>
</tr>
</thead>
<tbody>
<tr>
<td>28</td>
<td>Minister of Women Empowerment</td>
<td>Meutia Farida Hatta</td>
<td>PKPI</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Swasono</td>
<td></td>
</tr>
<tr>
<td>29</td>
<td>Minister of State Administrative Reform</td>
<td>Taufik Effendi</td>
<td>PD</td>
</tr>
<tr>
<td>30</td>
<td>Minister for the Acceleration of Development in Backward Regions</td>
<td>Saifullah Yusuf (Muhammad Lukman Edy)**</td>
<td>PKB (then PPP) (PKB)**</td>
</tr>
<tr>
<td>31</td>
<td>Minister of National Development Planning/Head or BAPPENAS</td>
<td>Sri Mulyani Indrawati (Paskah Suzetta)*</td>
<td>Non-partisan (GOLKAR)*</td>
</tr>
<tr>
<td>32</td>
<td>Minister of State-Owned Enterprises</td>
<td>Sugiharto (Sofyan A. Djalil)**</td>
<td>PPP (Non-partisan)**</td>
</tr>
<tr>
<td>33</td>
<td>Minister of Public Housing</td>
<td>Muhammad Yusuf Ashari</td>
<td>PKS</td>
</tr>
<tr>
<td>34</td>
<td>Minister of Information and Communication</td>
<td>Sofyan A. Djalil</td>
<td>Non-partisan (Non-partisan)**</td>
</tr>
<tr>
<td>35</td>
<td>Minister for Youth and Sport Affairs</td>
<td>Adhyaksa Dault</td>
<td>PKS</td>
</tr>
<tr>
<td>36</td>
<td>State Secretary</td>
<td>Yusril Ihza Mahendra (Hatta Radjasa)**</td>
<td>PBB (PAN)**</td>
</tr>
<tr>
<td>37</td>
<td>Attorney General</td>
<td>Abdul Rahman Saleh</td>
<td>Non-partisan (Non-partisan)**</td>
</tr>
<tr>
<td>38</td>
<td>Cabinet Secretary</td>
<td>Sudi Silalahi</td>
<td>PD</td>
</tr>
</tbody>
</table>

* First reshuffle (5 December 2005)
** Second reshuffle (7 May 2007)

**Source**: Author’s compilation from various sources