

**THE ECONOMIC AND POLITICAL DIMENSIONS
OF INDONESIAN DEVELOPMENT**

GADJAH MADA UNIVERSITY

JOGJAKARTA

**Address upon taking the Chair
at the Faculty of Economics
Gadjah Mada University**

**Delivered before the Open Meeting of the Board of Professors
of Gadjah Mada University
on 24 February 2007**

DOKUMENTASI & ARSIP	
BAPPENAS	
Acc. No. :	cs442 / 08
Class :	56.31
Checked :	22-7-2008

By:

Prof.Dr. Boediono

*Honourable Chairman, Secretary and Members of the Board of Curators of the
Gadjah Mada University,*

*Honourable Chairman, Secretary and Members of the Board of Professors of the
Gadjah Mada University,*

Honourable Rector and Vice Rectors of the Gadjah Mada University,

Civitas Academica and honoured audience,

It gives me immense pleasure to stand here and present some thoughts to this Honourable Assembly. What I am going to discuss is an issue that, in my opinion, touches on the welfare of all of us as citizens of this nation, and on the welfare of our children and grandchildren. The issue is the reform agenda we are currently engaged in.

It is almost nine years since the Indonesian people embarked on a path of democracy and pluralism. This decision was ours alone, taken consciously as a people and not dictated by outsiders. Now, after a series of historically decisive social-political events and even natural disasters, and while reform euphoria has not abated, we need to pause to ask ourselves where these events and developments are taking us, will we reach the goal we dreamed of when we took those historical actions? Are we on the right track? Is there anything that we need to correct?

These weighty questions cannot be answered in one hour. However, in all modesty I invite you to explore with me key aspects of these questions despite only be able to provide partial answers.

I will start by recalling what we wanted when we launched *reformasi*. Based on these recollections and the results of recent research, I will define what it means to be on “the right track”. Because only by agreeing what we mean by “the right track” are we able to answer whether we are indeed “on the right track”. With the time

remaining I will identify the critical points on our journey and what we need to prepare.

The Demands of Reformasi

Let us pose the question: What were the basic motives that encouraged us as a nation to carry out such fundamental changes to our social and political structure more than eight years ago?

To put ourselves in the correct perspective we need to recall the events leading to that critical time. After more than 30 years the New Order had successfully raised living standards and social well-being in Indonesia. Income per capita rose from a mere USD70 in the mid-sixties to over USD1000 in the mid-nineties. There was extensive investment in infrastructure that served the people and supported economic activity. Poverty fell dramatically and social indicators including life expectancy, nutrition, maternal and child mortality, participation in education, availability of clean water and housing, all showed significant improvement. Indonesia was an example of successful development.¹

With clear improvements in the standard of living, why was there increasing restlessness and demand for change within the community, or more specifically, within the elite of the community? The answer is found elsewhere. In the midst of this progress, in particular during the last decade of the New Order, perceptions grew that corruption, abuse of authority in government and crony-ism in the business circles was becoming widespread. Despite press restrictions, stories of corruption flourished and cases were revealed. The nation's sense of justice was violated. However, there were insufficient channels for criticism, dissent, protest and correction in the

¹ Hill (1996), World Bank (1993).

political system. Thus restlessness and dissatisfaction accumulated, ready to explode as soon as there was a trigger.²

At last that trigger arrived. The financial crisis that began in mid 1997 deteriorated into 1998 developing into a severe economic crisis that impacted all elements of society. Prices of basic necessities rose dramatically and lay-offs were widespread.³ The restlessness that hitherto had been limited to the elite turned into dissatisfaction and ultimately mass riots. Indonesia entered a multidimensional crisis that led to fundamental political change.

It is not easy to extract the people's aspiration from the events, tension and tumult, of that time. Yet when we examine reform motives, four demands stand out: (1) economic recovery, (2) improved governance, (3) supremacy of law, and (4) democracy. In short, the people wanted an Indonesia that was prosperous, free of KKN (corruption, collusion and nepotism), law abiding and democratic.⁴ No easy demands, but this was what the people wanted.

The "Right" Track

Now let us return to the question: Are we on the right track? Allow me to provide the answer. With some important caveats on which I will elaborate, the answer is: yes, we are on the right track. This does not mean that we are sure to reach the goal. There is no such guarantee. At each stage in our journey, we as a nation will come to cross roads that will require the correct decision. Let us now look at what we mean by "*the right track*".

² O'Rourke (2002)

³ Johnson (1998)

⁴ O'Rourke (2002) or Budiman et al, eds (1999)

The identification of these patterns and their explanations constitute a major part of the study of historians and social scientists. At the moment there are numerous studies, theoretical and empirical, that can help us look at the options ahead. For Indonesia one choice is easy, our reform momentum has already put us on the path of democracy. In the political-economic literature views have crystallized on the broad outlines of the transformation of a country from a low income, closed and non-democratic society to a prosperous, open and democratic one.

Economic Foundations. One of the views that has crystallized concerns the economic foundations of democracy. It says that during the initial phase of its journey a low-income, closed and not yet democratic society should concentrate on economic development.⁵ Intuitively this makes sense since people at low income levels will be preoccupied with meeting daily necessities. The need or (using economic jargon) the “demand” for democracy will blossom at higher standards of living and higher levels of education.⁶ The experience of various countries also indicates that once the demand for democracy has gained momentum, there is no stopping it.⁷ We might debate this, but in my opinion Indonesia has reached this point.

A number of studies also indicate that economic progress is itself a decisive factor in the continuation of democracy. A well known study, based on empirical evidence from 1950-1990, concludes that democratic regimes in countries with incomes per capita of 1,500 dollars (calculated on the basis of 2001 *Purchasing Power Parity* (PPP)-dollar) has a life expectancy of just 8 years. At incomes per

⁵ Barro (2000), p.104-7. Bremmer (2006) mentions that the non-income factors (such as education) are also significant in preparation of democracy. But in general these factors are correlated with income.

⁶ Fukayama (2006).

⁷ Bremmer (2006).

capita of 1,500-3,000 dollars, democracies survive an average 18 years. At incomes per capita of over 6,000 dollars the survival of a democratic system is much higher and the probability of its failure is only 1/500.⁸ What is Indonesia's position? When we calculate on the basis of 2006 PPP-dollars the per capita income in Indonesia now is estimated to be approximately 4,000 dollars while the critical limit for democracy is 6,600 dollars. Thus we are not yet 2/3 the way towards safety. We shall discuss this later.

A number of other empirical studies, in particular by economists, conclude that democracy is not the decisive factor in economic performance.⁹ In the opinion of these experts, in particular for low income countries, the rule of law is more critical than democracy per se. If this is correct then low income countries should be able to increase economic growth, through the rule of law even when they are not democratic. However, as I indicated earlier, with increasing prosperity the demand for democracy grows. And, at this later stage democracy becomes increasingly important to the sustainability of economic development. A well-known development economist says that democracy is a *meta* institution needed to create a climate conducive to the growth of high quality institutions, i.e. efficient and with good governance.¹⁰ This is important as the consensus among experts and practitioners is that institutional quality or governance is key to development success. If good institutions determine the success of development, and democracy is conducive to the growth of such institutions, then democracy becomes the decisive factor in economic development. At higher levels of economic welfare, economic growth relies on the flexibility of

⁸ Zakaria (2003), p.69-70. Przeworski and Limongi (1997).

⁹ Barro (2002), Friedman (2005), Chapter 13.

¹⁰ Rodrik (2000).

economic systems, technological progress and improved factor quality, all of which are rooted in the initiative and innovation of economic actors. And we know that initiative and innovation are fostered in a democratic atmosphere.¹¹

So what is our general conclusion? At an initial phase, economic development is the priority because this reduces the risk that democracy will fail. As development progresses democracy will be demanded and at the same time improves economic performance and the sustainability of growth. However democracy is a plant that takes a long time to grow. The earlier we sow the seeds the better.

Dilemma.¹² The fundamental dilemma in democracy, known since Plato, is how to balance rationalism with populism, an effective government with a representative government, technocracy with democracy. This is a concrete, acute, dilemma for a newly developing democracy, such as Indonesia. On one hand, we wish to step up economic development which requires quick decision making based on rational, consistent and long term economic calculations— often involves short term pain for long term gain. On the other hand, the political system, not having reached stability, does not support such quick and decisive decision making. The risk that rational policymaking will be distorted is high as narrow interests and short term thinking dominate discourse in legislative and even executive institutions, and without an effective counterweight. This is why experts are of the opinion that economic policymaking, within limits, needs to be insulated from political tumult. The independence of the Central Bank, now generally accepted, is one solution to this

¹¹ See Schumpeter (1976) and Wittman (1989)

¹² For further analysis see Boediono (2005).

dilemma. Whether analogous solutions can be found in the areas of fiscal, industrial and trade policy, or the environment, is being debated by experts.

The important thing is that a strategic balance between technocracy and democracy has to be found by every nation in every phase of its journey. During the New Order, with all its pluses and minuses, economic policy was protected from the short-term political process at least for the first two decades. But this approach is no longer appropriate and we must find a new format and strategy. Finding this answer cannot be put to the side or left to short-term political decision making. The stakes are too high.

Reformers. History indicates that the success of a nation's transformation into a prosperous, democratic and open society is driven by reformers. These reformers initiate and spearhead the process of national reform. Without them, a nation's transformation runs the risk of stagnating or even going off track. Economic growth helps their cause, but it must meet 2 additional conditions, namely that: (1) such growth is enjoyed by the majority of the people (i.e. that it is broad based); and (2) that growth depends more on the work, initiative and ingenuity of its citizens than on the sale of natural assets, foreign aid or other accumulated wealth transfers. To support the development of reformers, high growth is not sufficient, these conditions must also be met.

Who are these reformers and what is their role in the reform process?¹³ History shows us that these groups can come from different backgrounds. In England the critical group were entrepreneurs – the *bourgeoisie*. The term *bourgeoisie* has a bad

¹³ Zakaria (2003) and Bremmer (2006) offer examples from a number of countries. Some of the illustrations used here are drawn from these sources.

connotation in this country because it is linked to Marx's theory, where the bourgeoisie are the class that controls the means of production and exploits labour. In the non-Marxist theory the role of bourgeoisie is more neutral. In fact economic historians looking at England generally find that this group were the key to social reform, breaking down existing feudal structures, subsequently becoming the spearhead of modernisation and democratisation.¹⁴ This pattern was followed in several other European countries. In the United States of America the process was faster as there was no feudal structure to be broken down.

However, in countries like Germany and Japan the *bourgeoisie*, at least initially, were not major drivers of reform. They were not as strong and independent as their colleagues in England or the USA. In Germany, the bureaucracy (consisting former aristocrats) were the reform leaders. In fact, Germany in the 19th century had the most modern bureaucracy in the world, and through bureaucratic reform they created a stable rule of law and a modern social security system. In Japan reformers originated from among the Samurais who became the engine of modernisation. In Germany and, to an even greater extent, Japan modernisation did not immediately give birth to democracy. In these two countries democracy only took root after World War II. And their democracy did not completely originate from within, but was to an important extent the result of reforms driven by conquering countries, especially the USA.

Today's developing countries do not want to wait for the natural development of reformers as described. In addition a developing country should not rely on just one or two social groups as reformers. The best outcome is to encourage the establishment of a broad coalition, consisting of democrats from all social segments. This group of

¹⁴ Landes (1999).

reformers includes reform elements from entrepreneurs, intellectuals, professionals, bureaucrats, youth, and NGO activists. They would be bound together by a platform, focused on the fight for democratic values including human rights, openness, freedom of enterprise, good governance, and the rule of law. In some developing countries, including Indonesia, such groups are establishing themselves and playing a role, although their influence remains limited. Nevertheless, they are the strategic elements of the modernisation and democratisation process.

A Risky Journey. The process of modernisation and democratisation is a long and risky journey.¹⁵ Some say that it is best characterized as a J-curve with large risks of failure early but gradually progress takes over.¹⁶ Others, picture it as a path characterized by vicious and, occasionally when lucky, virtuous circles.¹⁷ Others picture it as a journey along a road full of intersections requiring correct decisions.¹⁸ History is not compassionate. Only a nation with vision, conviction, perseverance and intelligence will complete its journey. Others do not move from their initial position, become failed states or disappear from the map of history. Darwin's law also applies among nations.

Our Journey Forward

In my previous remarks I focused on risks faced by a nation wishing to become modern and democratic. Let us now take a closer look at these risks, and link

¹⁵ Huntington (1968): "Modernity breeds stability, but modernization breeds instability."

¹⁶ Bremmer (2006).

¹⁷ Friedman (2002), Chapter 13.

¹⁸ Zakaria (2003).

them to the conditions faced by our nation. I shall discuss three critical categories of risk, namely:

- (1) Social cohesion
- (2) Economic performance, and
- (3) Reformers

Social Cohesion. The most fundamental condition for a successful transformation is a nation's ability to sustain its existence and integrity. Ultimately this depends on the strength of the country's social cohesion. There are nations that – due to its history, culture and social structure – have social cohesion that is resilient to pressure and shock. Japan and Korea with their homogeneous cultures are examples. Other nations, such as India and Indonesia, due to the variety of their cultures and heterogeneity of their societies, intrinsically possess lower resistance. Other nations are even less fortunate, such as Yugoslavia and Iraq, with long histories of internal conflict. In such cases when a strong unifying person is gone, conflicts arise and the nation splinters.

We must be careful, in particular during the initial vulnerable phase, to maintain the correct balance between social cohesion and rapid change. Change brings stress and strain. The proper balance rests on the statesmanship and wisdom of a country's leaders or elite.

Indonesia's social cohesion is probably somewhere in the middle. We are fortunate because there is no history of deep-seated animosity among groups, races and religions, found in Yugoslavia and Iraq. We are fortunate because the freedom fighters and our founding fathers forged a national awareness that constitutes our nation's political capital. Yet we must also be aware that our nation is characterized by a diversity of cultures, religions, traditions and even temperaments that can lead to

rifts. Separatism is not something alien to us as it has been with us since independence, although it has never become a dominant force. The risk is that democratisation, decentralisation, modernisation and openness, if not managed wisely, will create centrifugal forces. Conversely, education, broad based economic growth and good governance strengthen social cohesion.¹⁹

What must also keep in mind that national awareness is the political capital that we inherit from our predecessors, and although strong, it can decline without a conscious effort to rebuild it. The nation building efforts of the founding fathers are not complete and probably never will be. We must continue their efforts, despite (or more correctly, because of) globalisation. We long for a nationalism that signifies that, whatever our differences, we remain brothers or sisters, that a political opponent is a sparring partner and not a foe to be eliminated. Like the *Dalang* (Puppet Master) says: *Tego larane ora tego patine. Dudu sanak dudu kadang, yen mati melu kelangan.* [Able to bear one's suffering, but not able to bear one's death. Although he is not my relative, I will miss him when he dies]. Only when we reach this state of national maturity can we relax a little in our nation building efforts. But that is a luxury that will have to be enjoyed by our children and grandchildren.

Economic Stagnation, Decline and Crisis. Another big risk in a nation's journey is the risk of economic stagnation, economic decline or even more serious, an economic crisis. If this happens there is a good chance the process will stall half way to the goal. Earlier I cited a study indicating that democracies in countries with low per capita incomes (lower than 6,600 PPP-dollars 2006) are vulnerable to failure. I also mentioned that a priority for these countries is to grow as fast as possible to

¹⁹ Friedman (2002), Chapter 12.

reduce this risk. Economic stagnation, and even more so economic decline, increases the risk of democratic failure a risk that is already high. An economic crisis will almost certainly bring down a political regime – pushing the country off track.

Indonesia's own experience provides evidence. Let us reflect for a moment.²⁰ The era of Parliamentary Democracy, between 1950-1958, was characterized by political instability with frequent Cabinet changes and ineffective economic policies. The problem of twin deficit – the simultaneous existence of deficit in the State Budget and in the balance of payments – were not handled properly, economic stability deteriorated and growth was sluggish.²¹ Because it could not provide tangible benefits, the political system gradually lost its legitimacy. Economic failure brought our first democratic experiment to an end.

The political system that replaced it, Guided Democracy - and its counterpart in the economic sector, namely the Guided Economy – from 1959-1965, promised to deliver a stable government and a bigger role for the state in economic life. However this system, again, did not deliver results for the people. Inflation rose out of control, production deteriorated and daily life became difficult. It was in fact an economic crisis that ultimately resulted in political change.²² The generation who experienced that era (including me) remember how difficult daily life was. However, in the midst of these difficulties, we, in particular the young, felt an extraordinary pride in our nation, as respected and sometimes feared in international arenas. However that did not alter the fact that economic crisis brought that political order to an end.

²⁰ The largest part of the material cited from the 1950s till the present is taken from Boediono (2005).

²¹ Higgins (1957)

²² The best source for this era is the *Bulletin of Indonesian Economic Studies* that was published every four months since 1965.

The New Order era from 1966-1998 was the longest era of political stability in the history of independent Indonesia. Such political stability made it possible to carry out consistent economic policy. The results included economic growth averaging 7% for three decades with relative stability, the development of large scale infrastructure that unified Indonesia and significant improvements in social and human development indicators. These economic improvements in turn strengthened political stability, until the economic crisis in 1997. This was a social-economic performance that, if we are honest, was impressive.²³

This Order subsequently collapsed due to the confluence of three developments: increasingly suffocating political climate, the spread of crony-ism and corruption, and in the final phase, the difficult conditions of life during the crisis itself. The crisis revealed institutional weaknesses and vulnerability that had been obscured by high growth. Important government suffered from paralysis or near-paralysis and as a consequence were unable to develop and implement coherent policies to respond to the rapidly evolving situation. This in turn triggered a chain reaction that brought Indonesia even deeper into crisis.

The New Order has taught us at least three lessons. First, a continuing economic performance accompanied by improved welfare for the general public is a necessary condition for the survival of a political order. Second, long term survival requires more than solid economic performance, and in particular openness and good governance (sufficient conditions). Third, yet another evidence that a serious economic crisis is followed by a change in the political order.

History is process of challenge and response. At the end of the Parliamentary Democracy era people longed for a strong administration. The response was the

²³ Hill (1997)

Guided Democracy with its promise of a stable government. Yes, the government stabilized, but economic life became harsher. And, by the end of this era the most dominant demand was for improved economic condition. The New Order era responded to this and delivered impressive economic and social improvements, but failed to respond to other demands, namely a longing for democracy, openness, the eradication of corruption, collusion and nepotism (KKN) and better law enforcement.

With this the *Reformasi* Order was born, and don't forget that Gadjah Mada University was there assisting in the delivery! This latest Order has tried to address the challenges before us. Thus far there have been four presidents who, based on their styles and in view of the situations they faced, have tried to carry out reform as best possible. During this period changing presidents has not changed the political order, a good omen for political stability. Democracy has flowered, although some elements do not function as we would like. Openness and the freedom of opinion, with pluses and minuses, are part of our daily life and Indonesia is acknowledged as having made some of the best progress in the region. The eradication of KKN continues although some doubt its sustainability. The framework for legal reform is taking shape and initial reform steps are being taken, although legal certainty remains a major complaint of investors.

In my opinion, we are on the correct reform path, although a lot of homework is unfinished. The major risks we face are losing our passion and stamina for the journey, losing faith or patience, or being carried away by the euphoria of tumultuous "democracy" and losing track of the actual objectives of reform. If these happen, this would be (another) tragedy in the history of our nation. Experience shows that these risks are not theoretical.

Let us connect the discussion of our current condition with the empirical research I referred to. The reality is that our per capita income is in the zone where the continuation of democracy is at risk. Indonesia's per capita income in 2006 (based on the 2006 Purchasing Power Parity (PPP)-dollars) is approximately 4,000 dollars, still some distance from the safety zone of 6,600 dollars. The best strategy is to quickly leave this dangerous zone. Let us do some arithmetic. Assume that we, with our best efforts, succeed at growing 7% per year, and that our population growth rate is 1.2% per year. If so our income per capita would grow by approximately 5.8% per year. With this growth we would cross the threshold into the safe zone in 9 years. If our GDP grows by less than 7% the time to reach safety will naturally take longer. What we need to underscore is that 9 years is a long time to guard Indonesia's democracy that is just now flowering. The risks I indicated earlier are still with us. Without sacrificing democracy, we need to eliminate the constraints to economic growth that democracy or its excesses creates. At this stage of development we must have the courage to take a clear position regarding the appropriate balance between technocracy and democracy. Such a position is required for the sake of the survival of democracy itself.

Class of Reformers. As I mentioned, a critical aspect in democratic development is the development of a reliable group of reformers who promote and guard democracy. I would like to stress that we should interpret democracy broadly covering not only the formal mechanisms of democracy (free and open elections, multiple parties, a division of power between the executive, legislative and judicial institutions, and the role of the press and social organisations), but also the *basic values* that give soul to democracy. The distinction between these formal mechanisms

and democracy in its broader sense is important. We can sometimes feel that we have complied with nearly all the formal requirements for democracy, but we do not enjoy the benefits as promised by its conceivers or as enjoyed by other countries where democracy is more settled. In such a case we can have democracy without soul.

Without a reliable class of reformers democratisation risks producing democracy without a soul, a democracy that stalls mid-way, proceeds without direction or, worse, gives birth to the antithesis of democracy. These have all happened.

Let me provide some examples.

Historical experience. Haiti is a republic that has formally been democratic for over 200 years after obtaining independence from France in 1804. Haiti is a poor country with a per capita income of USD 450 subject to disorder every time there is a change of government (who govern in ways that are far from the norms of democracy). The major problem, in my opinion, is that there have never been a solid group of reformers able to guard democracy and its basic values.

Contrast Haiti with India. At the time of independence India was also a poor country (income per capita approximately USD 50) socially backward and feudal. However, India was fortunate because under British rule sufficient of its elite enjoyed modern education and occupied positions in the colonial bureaucracy. Some of them became players in industry and trade. At independence this elite decided to adopt democracy and guard it. If there is one person who is the manifestation of that commitment it was Nehru. Nehru was a true democrat. Social reality was far removed from the ideals of democracy. When observers in the 1950s and 1960s contrasted India's mediocre economic performance with the spectacular growth in the People's Republic of China, Nehru and India's elite remained strongly committed to

democracy.²⁴ As a result, Indian democracy with its strengths and weaknesses is a living reality for sixty years, while democracy in China remains an aspiration, even today.

History also records how democracy can be “hijacked” because its reformers were not sufficiently strong in the face anti-democratic forces.²⁵ Germany during the Weimar Republic (1919-1933) was democratic and not poor. However, a lengthy economic crisis (hyperinflation followed by depression) and the powerlessness of the government to handle this crisis led to the rise of Hitler and his Nazi party. They promised to end to this misery, winning a majority of votes in the election. The economic crisis seriously weakened the middle class, the bearer of the democratic banner. Through a democratic process Hitler took the helm of the country, and then murdered democracy.

What about Indonesia? The group of reformers in Indonesia is probably smaller than in India. But it is growing rapidly, in particular during the Reformasi era and especially among the young. We also have an advantage compared to India – social stratification is less and social mobility is greater. Therefore we should not be pessimistic regarding the prospects for democracy in Indonesia. The question is how to encourage our reformers and strengthen modernisation and democratisation. Allow me to present some initial thoughts.

Economic growth. The most effective way to strengthen reformers is, once again, to accelerate broad based economic growth, which fosters the development of the middle class. Equally, economic decline and crisis must be avoided because these

²⁴ Das (2002), Chapters 19 and 21.

²⁵ Friedman (2002), Chapter 11.

forestall the development of the middle class. I have already mentioned that there is another condition to fulfil, namely that growth should have its roots in the entrepreneurship that develops when there is a healthy climate for competition.²⁶ Healthy competition is important because it determines the kind of middle class that emerges. The experience of countries, perhaps in some sense including our own, suggests that economic growth originating from the sale of natural wealth (such as oil) alone can create a middle class, but it is a middle class of consumers. It is not certain that such a group will be committed to democracy. The same caveat goes for growth based on crony-ism and collusion between those in power and businesses and other monopolistic practices. These too can deliver high growth for a time, but this growth will not be sustainable because it does not create a middle class willing to fight for democracy, good governance, legal certainty on so on. What emerges are not reformers but rent seekers, and not a market economy but false or ersatz capitalism, more compatible with an oligarchy than democracy.

The development of Small and Medium Enterprises (SMEs). In addition to an improved investment climate and healthy competition the government can accelerate the growth of reformers through special programs that remove the constraints faced by small and medium enterprises and improving their access to finance, technology, infrastructure and market services. These small and medium entrepreneurs are the embryo of the middle class. SME development is therefore a critical element in the development of democracy.

Indigenous-Non indigenous. A sensitive issue in Indonesia since independence is the relationship between pribumi (indigenous) and non-pribumi (non-indigenous) entrepreneurs. I do not pretend to be have a solution for this complex issue. I can only

²⁶ Parente and Prescott (2000)

say that the issue should be discussed openly and that we need to find the answer together. In my view, given the importance to Indonesia's long-term development, there is no other solution than bringing the strengths of these two groups together. This effort must become part of a larger integration, by gradually but systematically removing socio-economic-cultural divides between the two groups. Each group, or more correctly the elite of each group, has to be more open, more willing to take initiative, more willing to reach out to one another and to honestly look for meeting points, while involving the younger generation. Government should encourage this process by acting fairly and conscientiously. Thailand and the Philippines, in their different ways, are clearly ahead of us, while Malaysia is probably not so far removed. We must view the solution here as an integral part of our long journey as a nation.

Education. Another important element in the establishment of a reliable group of reformers is education. This was central to what happened in India. This also occurred in Indonesia during the Dutch era, although to a far lesser degree. With all the problems of the colonial era, quality education created a competent elite. In an era of independence, with all our facilities and opportunities, there is no reason why we should not be able to do the same or even better. It is regrettable that this has not happened. Why? The key, I think, lies in the finding the right educational material and an effective learning-teaching process. We need to work on both. There are two important caveats. First, the provision of quality education for the nation's elite must be based on open selection based on performance or merit and not on privilege or position. Second, for democracy to take root, the education of the elite must be accompanied by quality basic education open to all. In education, there is also a lot of home work.

Openness. The development of reformers is supported by openness to the outside world. The more open and integrated a country is with the global community, the faster the growth of reformers. The flow of information, people, goods and services and investment is a catalyst for their development. Indonesia is currently a country very open to the flow of information. As far as we can see there is no systemic obstacle to foreign reporters, academics, entrepreneurs, professionals and NGOs entering Indonesia. All this should spur the growth of reformers. Indeed, there are security risks, and there always will be. But, for the sake of higher objectives, these risks should be managed proportionally. The participation of Indonesia in forums, regional as well as global, will continue to open our minds to best practice and help us develop institutions that support modernisation and democratisation. Foreign investment, in particular from countries that uphold good governance, should be welcomed, not only to support economic growth, but to enhance the quality of business and government institutions. Frequently our business community learns best practice from interaction and partnership with foreign companies. Also keep in mind that bureaucratic reform is sometimes triggered or accelerated by complaints or protests from foreign companies. On the issue of openness, in my opinion, we are on the right track. Let us not put the clock back.²⁷

Recapitulation

Let us now recapitulate the discussion.

We started with the question about where this journey for nearly nine years is taking us? Are we on track to achieve the objectives of reform? The answer,

²⁷ The tragedy of the decline of Argentina due to closing up itself is related dramatically by Rojas (2002).

with a number of important caveats, is: yes, we are “on the right track.” We have made our choice, namely we have chosen the path of democracy. With this choice, and learning from our experience and the experience of other countries that have followed this road, we have a picture of our future.

During the initial phase economics is likely to be the most decisive factor. The probability of democratic failure is very high at low incomes and diminishes progressively as incomes become higher. An economy can grow without democracy, so long as it upholds the rule of law. At a higher levels of income democracy in turn sustains increasing welfare. The mutually reinforcing relationship between economic growth and democracy becomes stronger.

In every phase, the role of the reformers, namely the coalition of forces across community groups unified by support for modernisation and democracy is critical. This group will flourish in an economy that enjoys broad based growth, and founded on good governance and a healthy business climate.

The fundamental risk for Indonesia is how to preserve the existence and integrity of the nation during this journey. We possess sufficient political capital, but it must be continuously fertilised and reinforced. Strengthening our awareness as a nation and our nation building must continue to be an integral part of Indonesian development. Our participation in the globalisation must not divert our attention from this nation building.

The second big risk is that income levels are still low and the risk of democratic failure high. In view of this Indonesia should assign the highest priority to stepping up economic growth and to avoiding an economic crisis. To support economic performance, we must have the resolve to find the balance between technocracy and democracy. If we can rely on research, Indonesia will need at least

nine years to reach the “safety zone” for democracy. In the meantime, vulnerabilities remain and the democracy that is just starting to blossom will need to be guarded.

The third big risk is that a reliable group of reformers will not develop. If they do not our transformation can stagnates or worse move in the wrong direction. Our experience and the experience of other countries indicate that KKN, crony-ism and monopolistic practices are a major risk. We do not want to repeat our bitter experience. It is reformers who guard the reform process and keep it on the right track. The development of this group needs to be encouraged by: (1) taking care that economic growth is broad based and supported by good governance and a healthy business climate; (2) encouraging the development of small and medium enterprises; (3) fostering the integration of indigenous and non-indigenous groups; (4) providing quality education to reformers; and (5) maintaining openness in our interactions with the outside world.

That is the central argument of the discussion today. All these measures can only bear fruit in the long term. Our generation has to plant, our children and grandchildren will harvest.

Acknowledgements

There are too many parties who deserve to receive my appreciation and gratitude to mention them one by one. To reduce the risk that I will forget to mention anyone, allow me to offer my sincere thanks to friends and colleagues in the Faculty of Economics and Gadjah Mada University for their cooperation and friendship. I grew up and was formed on the Blue Campus. Gadjah Mada University is an inseparable part of me. I also wish to express my gratitude to my colleagues and friends in government agencies in Jakarta for their cooperation and friendship. With

all our limitations, we have endeavoured to do our best for the people. My family has asked me not to thank them. They said it is not necessary. They have only asked that I give more time and attention to them. For now, it seems that I will be unable to do this. Finally I wish to thank all those present for setting aside time to attend today's event.

May God always shower His blessings upon us.

Thank you.