

## Transcript

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Jointly with Tasman Asia Pacific and Tasman Institute



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*Coordinating Minister for Political and Security Affairs*

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**COORDINATING MINISTER FOR POLITICAL AND SECURITY AFFAIRS  
OF THE REPUBLIC OF INDONESIA**

## **“A SECOND WAVE OF REFORM FOR INDONESIA”**

**PRESENTATION BY**

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**REPUBLIC OF INDONESIA**

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Ladies and Gentlemen, Dear Friends,

Thank you, Dr. Porter, for your kind words of introduction. I am grateful to you and the Tasman Institute, and also to Dr. Roger Peacock and Ms. Jenny McGregor, Executive Director of the Asialink Center, for inviting me to address this prestigious meeting.

It is good to be here in Australia, a country that is hugely important for Indonesia. And I am especially honored for this opportunity to address such a distinguished group of friends of Indonesia here at the University of Melbourne. I know that many Indonesians have studied here, and many of them have returned home to become pioneers and leaders in the Indonesian society. So thank you Australia thank you University of Melbourne!

You know, my son, who is studying here in Australia (and who recently greeted me with the words "G'day, mate"), told me that he was rather amused to see me, a former general, talking about economics. I told him a secret: that I was actually using this forum as a warm-up for my oral examination for the Doctorate degree which I am now working on at the University at Bogor in Indonesia. I know I can count on all of you in this auditorium to keep this a secret also. In earnest, as a Coordinating Minister for Politics and Security Affairs, I always ask my staff to liberate themselves from the narrow confines of their respective disciplines and to probe the linkages between politics and security affairs with a range of social, economic and cultural variables. Only in this way can we develop a truly democratic concept of human security, one which will integrate traditional concerns of law and order with present day issues of social justice, social inclusion and poverty reduction.

I have decided to title my presentation: "A Second Wave of Reform for Indonesia". I believe that embarking on this "second wave of reform and reconstruction" is necessary for Indonesia if we are to complete the journey of "reformasi" which began after the economic crisis hit Indonesia hard in 1997. But before we talk about the second wave of reform, we need to first appreciate what the economic crisis did to our national mindset. For three decades before the crisis, we were somewhat blinded by our economic achievements, particularly in boosting productivity, attracting foreign capital, and maintaining long-term sustained growth.

But this confidence concealed a number of serious problems: corruption, collusion and nepotism (popularly known in Indonesia as "KKN"), a decline of productivity, poorly regulated financial systems and the inefficiency and rigidity of a centralized political structure. Astonishingly, we were all looking ahead and making even more ambitious plans for the future. We were drawn by the examples of Japan and Korea, which provided real-life examples of what is economically achievable in the region within the space of just a few decades.

The economic crisis forced us to rethink our own development experience and future strategy.

The fall of the New Order put to rest the notion that the Indonesian problem was largely an economic one. Very soon the country was pulled deep into a series of interlocking crisis, which spanned the entire spectrum of national life. Indonesia's banks and businesses, its political institutions, its social organizations, its inter-family support

mechanisms all came under extreme pressures triggered by the economic crisis. Many institutions, which only yesterday seemed to be permanent fixtures of society, seemed obsolete and incapable of accommodating change. It soon became clear that the economic crisis marked the end of an era, the beginning of a new politics, and the beginning of the era of Reformasi.

Indonesia's greatest task now is to translate the high hopes of "reformasi" into practical realities. This task, in my view, comprises several major challenges.

First, is to move away from economic growth as the key foundation for political legitimacy. A new political legitimacy must be built on a new democratic social contract, broad based economic growth and a well-defined separation of powers.

The second challenge is to dismantle cronyism and extreme asset concentration. We have to evolve an economy where entrepreneurship and risk-taking, not patronage and privilege, are the key to economic and social success. For example, by 1996, just a year before the crash, it was estimated that around ten families in Indonesia owned over 60 percent of all industrial assets. The economic situation was such that Indonesia had joined the ranks of those Asian economies, which were, in Krugman's terminology, "running faster just to stand still". Our economic reforms must do away with this kind of practices.

The third challenge is to contain and to reverse the consequences of previous closed political system. It was not only in the arena of investment efficiency and returns to capital that Indonesia found itself running on the spot. The same was true of the political system. As Indonesia grew richer, a larger share had to be distributed to political cronies in increasingly elaborate forms, from resource monopolies in wood and cloves, to liberal licensing of private banks and the diversion of profits of state enterprises and banks to private coffers. The fourth challenge is the creation of a balanced reform agenda. The end of growth meant the end of the era. It left a stunned Indonesia the difficult legacy of rebuilding both its political system and its business institutions at the same time. But there was more. As the country struggled to stem the worst effects of the crisis, net private capital flows were substituted by net official ones. Foreign investment was replaced with foreign aid. Aid came with conditions and an overwhelming emphasis on economic reform and the repayment of foreign debt. The implications remain with us to this day. Just at the time that Indonesia needed to reconfigure its political systems, heal deep seated but previously concealed social division, and rebuild its social capital, it came under increasing pressure from

external lending institutions and governments to pay disproportionate attention to the economic dimensions of reform.

Crises have inevitable implications for income distributions, themselves often stable over long periods. Effective recovery and political stability involve finding not only an economically sound but also a socially just sharing of the financial costs of the crisis between different segments of the community.

This brings us full circle to the question of the legitimacy of the political system, which faces the hard task of bringing about a consensus on what such a socially just solution might be. A political system erected on the very assumption of continuing and socially indifferent economic growth is the least appropriate instrument for striking bargains of the above kind. In such circumstances, a disproportionate emphasis on the economic aspects of the reform program is likely to be both paradoxical and counterproductive. It is important to realize that societies caught in the grip of a deep economic crisis are also highly divided societies. As Amartya Sen reminds us, "when we go up we go up together, when we fall we fall separately". Social divisions, ethnic frustrations and religious differences were kept at bay through the largesse of government spending and by the repression of the political system. Once the economic dam had burst and the political system was overthrown, latent social divisions came to the surface. Separatism, violent social conflict, inter-religious strife, and simple criminality found open expression in many parts of Indonesia. It was not only social divisions, which rose to the surface.

Those challenges can be summarized as an effective management of three simultaneous tasks of a systemic transition, namely:

1. The transition from authoritarianism to democratic governance
2. The transition from a patrimonial or crony form of market economy to a rules based, competitive market economy
3. Healing social divisions and maintaining national integration during the course of the transition.

Taken together, this involved taking a much more comprehensive view of the reform process and priorities than in the case of the more usual financial crisis. There are at times delicate balances to be struck between the needs of economic liberalization and demands of social justice, between the promotion of civil society and the strengthening of representative state institutions, between the requirements of democratic freedom and the maintenance of social peace and ethnic harmony, between the sequence of political and economic reform and between the national interest and local government authority.

Although Indonesia has not recovered fully from the interlocking crisis of the last five years, it has gone a long way towards the establishment of institutional structures, which are likely to prevent another unexpected systemic collapse. An important feature of the political and economic and security reforms undertaken over the last five years is to make Indonesia significantly more resilient towards severe economic shocks of the future. Much remains to be done, but much has been achieved.

Let me outline the key steps already taken in political, economic, and constitutional reforms, laying the foundation of democratic good governance and improving an enabling environment for business. To begin with, the transition to democratic systems of government has begun with relatively very little social violence and disturbance. Indonesia was able to accomplish three different successions to the Presidency in less than five years in a remarkable spirit of peace and stability, and along strict constitutional lines.

There has also been an enormous growth of civil society, including the emergence of political parties almost from the very start of the post New Order period. Reporting restrictions on the media were largely lifted and Indonesia experienced an explosion of public debate and surfacing of public opinion not seen for over three and a half decades. The Decentralization Laws 22 of 1999 and 25 of 2000 have given further weight to the de-concentration of political power. The speed and the depth of decentralization attempted in Indonesia in the midst of such an acute economic shock remains remarkable. Indonesia's rapid decentralization, almost at one stroke, changed the policy landscape.

There has been significant progress in constitutional reforms, including direct elections of the President and Vice President and the recognition of the principle of separation of powers and the creation of a Constitutional Court. The establishment of an independent Judicial Commission to oversee Supreme Court appointments and transfer of functions, over a five year period, from the Ministry of Justice to the Supreme Court relating to the administration of the judiciary.

Despite divided public opinion on a range of difficult issues such as privatization of state owned enterprises, fuel subsidies, employment and labor regulations, economic reform has moved steadily towards a resolution of these problems. Over the last two years, the pace and volume of assets divested through IBRA has increased, fuel subsidies have been abolished and the labor law amended to ensure

greater flexibility in labor markets. At the same time, there are signs of renewed lending by the banks as their capital adequacy ratios continue to improve and interest rates fall. These measures combined with the opening investment opportunities in the power and communication sectors should all help the recovery of the real economy.

All the reform measures will help to lower the probability of a future system-wide crisis of the kind suffered in the years following 1998. It will also go a long way towards ensuring that future investment flows, both domestic and foreign, will bring about growth of productivity and not just be founded on increasing the volume of factor inputs. They set the stage for raising Indonesia's competitiveness in regional and world markets of the future and thereby reverse a tendency that plagued the country over the last decade.

There are now increasing signs of renewed investors' interest in Indonesia. This is welcome and necessary. However, to be sustained, this return of capital flows must be founded not so much on push factors from external markets but on pull factors emanating from the Indonesian reform and restructuring effort.

Dear friends of Indonesia,

Indonesia is now entering Year 5 of our democratic transition. It has not been an easy 5 five years, but I can happily say that Indonesia has reached a point of no return.

But we need to maintain the momentum of "reformasi". This is why we need what I would call the "Second Wave of Reform and Reconstruction".

Under this framework of second wave reform and reconstruction, let me spell out some issues of immediate priority.

First, fostering democratic consolidation which focus on the further promotion of values and praxis of democracy, better respect for human rights, and the development of civil society on the one hand; and, on the other hand, maintaining stability, security and law and order.

Second, fostering economic recovery and reconstruction, particularly by focusing on reducing unemployment and poverty as well as increasing investment for developing economic and social infrastructures. We also need to create a favorable climate for foreign direct investments, such as through tax and custom reforms, maintenance of security and order, legal reforms and law enforcement, and labor relation reforms.

Third, fostering social harmony and the resolution of communal conflicts, such as in Maluku, North Maluku, Poso, and Central

Kalimantan. Between 1999 to 2002, we experienced high intensity communal conflicts. However, due to serious efforts by the Government, the situation in most of these conflict areas have been returned to relative normalcy. My Government will do all we can to maintain the stable condition in these areas.

Fourth, promoting legal reforms and law enforcement especially in fighting corruption and establishing good governance. We have begun laying the groundwork to this end, including the assignment of ad hoc judges to the commercial court, amended bankruptcy law, money laundering law, corruption law, the establishment of an independent commission for auditing the wealth of the state officials, and the implementation a number of measures of the principles of good governance, both corporate and public good governance.

Finally, the maintenance of national security. Two major sources of threat to Indonesia's national security are armed separatism and terrorism. We are trying to contain and subdue armed separatism within Indonesia, both through military and law enforcement measures as well as by addressing the social discontent and injustice, which gave fuel to local grievances. We have also become a frontline state in the global coalition against terrorism, and we are actively developing a comprehensive counter-terrorism capacity. Finally, let me conclude by reaffirming the spirit of reformasi is still very much alive and thriving in Indonesia. Reformasi is the ultimate call of history for our generation. I feel very privileged to have been part of this process. We owe it to ourselves to transform the vision of reformasi and the hopes of 220 millions of Indonesians into reality.

I thank you.

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*Coordinating Minister for Political and Security Affairs*  
**Melbourne**  
**10 October, 2003**