How Good are Good Transitions: Indonesia after Suharto, for instance

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Three big issues I left Indonesia wondering…

• Would “democracy” (or, the result of Suharto’s departure) be able to restore growth or would Indonesia muddle into uncertainty and/or populism?
• Would democratic governance lead to better governance?
• Would “democracy” be better for “the poor” than authoritarian rule?
Growth experience

- Growth slowed, but re-accelerated (before recent crisis) and stayed pretty high
- The deceleration of 1999-2008 versus pre-crisis is less than would have been expected by as much as 2 ppa
- The question was replacing “closed ordered deals” (to be explained) with something else that can create investor certainty.
Episodes of Indonesia’s growth

Figure 1: Five periods of growth in Indonesia, 1960–2008
(constant rupiah GDP per capita, 1997=1)

- $g(1960–67)=-0.58\%$
- $g(1967–87)=4.85\%$
- $g(1987–97)=5.98\%$
- $g(1999–2008)=3.70\%$
- Peak to trough $-14.82\%$
Given Indonesia’s massive and rapid transition to electoral democracy what would have been expected to happen to growth?
Three factors on growth

- *Growth* is condition, not a characteristic of countries

- Regression to the mean: short men have sons that are taller than them

- Do *big* political transitions create growth effects (potentially different from stable effects)
Table 7: Summary of Indonesia’s post crisis, post transition growth relative to benchmarks (1999)

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<tr>
<td>Indonesia’s pre-crisis growth rate, 1987-1997 to 1999-2008</td>
<td>5.98</td>
<td>3.70</td>
<td>-2.28</td>
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<tr>
<td>Median, all developing countries, 1999-2007</td>
<td>2.56 (1999-2007)</td>
<td>3.29</td>
<td>+.72</td>
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<td>Countries with large democratic transitions starting with above average (&gt;2 ppa) growth (table 3, predicted=5.54-3.53)</td>
<td>2.01 (2000-2007)</td>
<td>3.28</td>
<td>+1.27</td>
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<tr>
<td>Predicted value from regression among 52 countries with large democratizing transitions</td>
<td>1.28 (2000-2007)</td>
<td>3.28</td>
<td>+2.0</td>
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Difference between *de jure* and *de facto* in policy implementation

Figure 1c: Doing Business and Enterprise Survey: Operating License
(Actual and Predicted Values)
Favored and disfavored firms

For disfavored firms, anything goes.

No delay at all for favored firms.
“Doing Business” with deals

Indonesia:
Law: 168 days
10th: 0
25th: 3
75th: 30
90th: 30
Difficult transition in a “deals” world

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<th>Closed (deals specific and available to a small group)</th>
<th>Open (deals specific, but open to everyone)</th>
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<td>Ordered</td>
<td>(deals predictable and done deals stay done)</td>
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<td>Disordered</td>
<td>(unpredictable, before and after)</td>
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Will electoral democracy in the political sphere improve “governance”

• ICRG—an international source on rankings of countries for international investors—ranks a number of dimensions of “governance”

• Same technique as above, compare before and after of countries with big democratizing transitions to non-changers and autocratizing

• Do countries with big POLITY improvements get improved “governance”?
Huge improvements in ICRG rating of democratic accountability and corruption—less of bureaucracy

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<td>Bureaucratic Quality (0 to 4 range)</td>
<td>2.00</td>
<td>2.00</td>
<td>0.00</td>
<td>0.37</td>
<td>0.26</td>
<td>1.11</td>
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<td>Control of Corruption (0 to 6 range)</td>
<td>1.25</td>
<td>3.83</td>
<td>2.58</td>
<td>0.73</td>
<td>0.02</td>
<td>1.18</td>
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<tr>
<td>Democratic Accountability (0 to 6 range)</td>
<td>1.00</td>
<td>4.83</td>
<td>3.83</td>
<td>1.50</td>
<td>-0.39</td>
<td>1.69</td>
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Official national headcount poverty (BPS figures)
Is this pace of poverty reduction “disappointing”—given growth and democracy?

The responsiveness of poverty to growth seems low—a 40 percent increase in per capita GDP for only a 34 percent reduction in headcount poverty

Mechanically, headcount poverty (based on consumption expenditure data) is (a) growth, (b) distribution (how “pro-poor” the growth) and (c) the magnitude of transfers
Three points

• Narrowly defined poverty is too narrow a measure against which to judge progress

• No one really knows what promotes “pro-poor” growth (except by negative)

• There was no reason to believe electoral democracy would improve “penurious” definitions of poverty—it is not a vote getter
“Poverty” is not a good binary indicator

Source: World Bank, 2006
Pro-poor growth?

• Nice slogan, but….

• Obviously avoiding deals that favor the super-rich…

• And “labor intensity”
  – But, huge controversy about what might promote that…contradicting claims
Two strands of evidence on “democracy” and “targeting”

• Theoretical predictions of voting models with three groups suggest that “sharp” targeting is a “rich-poor” coalition (low taxes-sharply targeted benefits) while a “poor-middle” coalition produces universal benefits with higher taxes

• Recent experiment in Indonesia (ABHOS 2009)
Comparing community targeting and proxy means testing

• Community corresponded less well with “perfect” targeting of the consumption expenditure poor
• Communities and sub-village heads were much happier with community based targeting