Accounting for Indonesian Local Governance

A Field Experiment on Variant Business Conditions in Central Java, West Sumatera, Bali and NTB

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The Puzzle

The Puzzle

What explains (local) government change?

What explains variant policy outcomes
 across time & space?

Propositions in the Literature:

1) different **economic pressures**?

2) different **institutions**?

3) differences in which **interests are voiced**?

4) different **leadership?**

1) Economic Pressures

1) Subnational Competition (Tiebout 1956)

Mobile/informed taxpayers vote with their feet

2) Global Competition for FDI (WB, Kaufman)

Investors seeking 'stable' governance

3) Economic Shocks (Gourevitch)

Asian Crisis driving governance change

Different Policies = Different Economic Pressures

2) Institutions

1) Political Institutions (Classic-Mod Scholars)

Free elections, checks & balances

2) Economic Institutions (Weingast, Williamson)

Property Rights, openness to trade

3) Embedded vs New Institutions (North, Putnam)

Different Policies = Different 'Sets of Rules'

3) Voiced Interests

1) Citizens' voice hold governments to account (Hirschman, Kaufman, Shah, Putnam)

2) Organizing of interests (special vs common) (Geddes, Olson, Lowi)

Different Policies = Differently Voiced Interests

4) Leadership

1) Classical (Aristotle, Machiavelli, Mill)

2) Management (HBR, Hersey & Blanchard)

3) Policy Reform (Grindle, Rodrik, Olken)

4) Coalition Building (Dahl, Stoner-Weiss)

Different Policies = Different Executive Leadership

Applied to the Indonesian Case

1) Econ: Restricted Mobility & Information (Tiebout)

2) Inst: Invariant across jurisdictions (Laws & Rules)

3) Voice: Variant organized interests across jurisdictions

4) Lead: Variant local leaders across jurisdictions

Focus /Explanatory Variables:
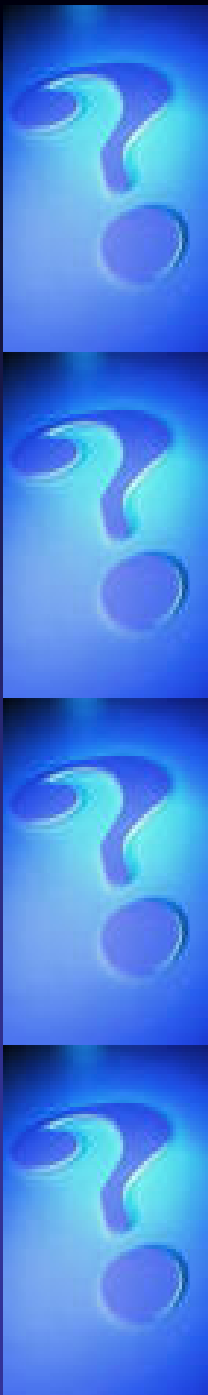(A) *Voiced Interests* and (B) *Executive Leadership*

The Question

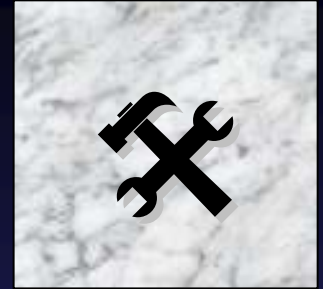# *Research Question/ Hypotheses*

RQ: How do we explain that Local Governance

in *some Indonesian districts* creates better

Business Conditions (BC) than in others ?

HY: This relates to variant degrees to which

1) Interests are organized / voiced / represented !

2) Chief Executives lead / build policy coalitions !

Methodology

Decentralised Indonesia – Ethnic & Socio-Cultural Diversity

Methodology – Data Collection

Data from 8 Districts & Jakarta (4/2005 – 6/2006):

→ 1000+ Local Business Questionnaires (125/District)

→ 130 In-depth Interviews (15/District + Jakarta)

→ Secondary Data (Government Reports, KPPOD, News)

→ Direct Observations (One-Stop Services / Local Markets)

Methodology - Case Selection

Distinct Cases & Repetition - "Nat. Experiments" (Yin 2003)

Case Selection: (1) Distinct in *Independent Variables*
(2) "c.p." Controlling for other influences

8 District Cases = 4 District Sets

2 Sets for <u>Leadership</u> (Sum / Java) – 2 for <u>Voice</u> (Bali/NTB)

Central Java	Gov. Lead.	Civic Voice	Control Variables	Business Climate ?
Kebumen	**High**	*Similar*	*Similar*	⇨ **Assessment ???**
Klaten	**Low**			⇨ **Assessment ???**

See: King/Keohane/Verba (1994), Yin (2003a,b), Geddes(1990)

Empirical Data
"Field Experiment"

Local Business Conditions Vary

Variation of tax policies & licensing practices!

→ New Distortionary Taxes in Bima /Lombok / Pesisir

→ Variant Capture Practices during Licensing

→Variant One-Stop Licensing Services

→Variant Tender Practices & Road Qualities

→Variant Bribe Payments for Entry into Public Service

Business Climates vary strongly across Indonesia's Districts

PERINGKAT DAYA TARIK INVESTASI 156 KABUPATEN DI INDONESIA

Legend:
- Faktor Kelembagaan
- Faktor Sosial Politik Budaya
- Faktor Ekonomi Daerah
- Faktor Tenaga Kerja
- Faktor Infrastruktur Fisik
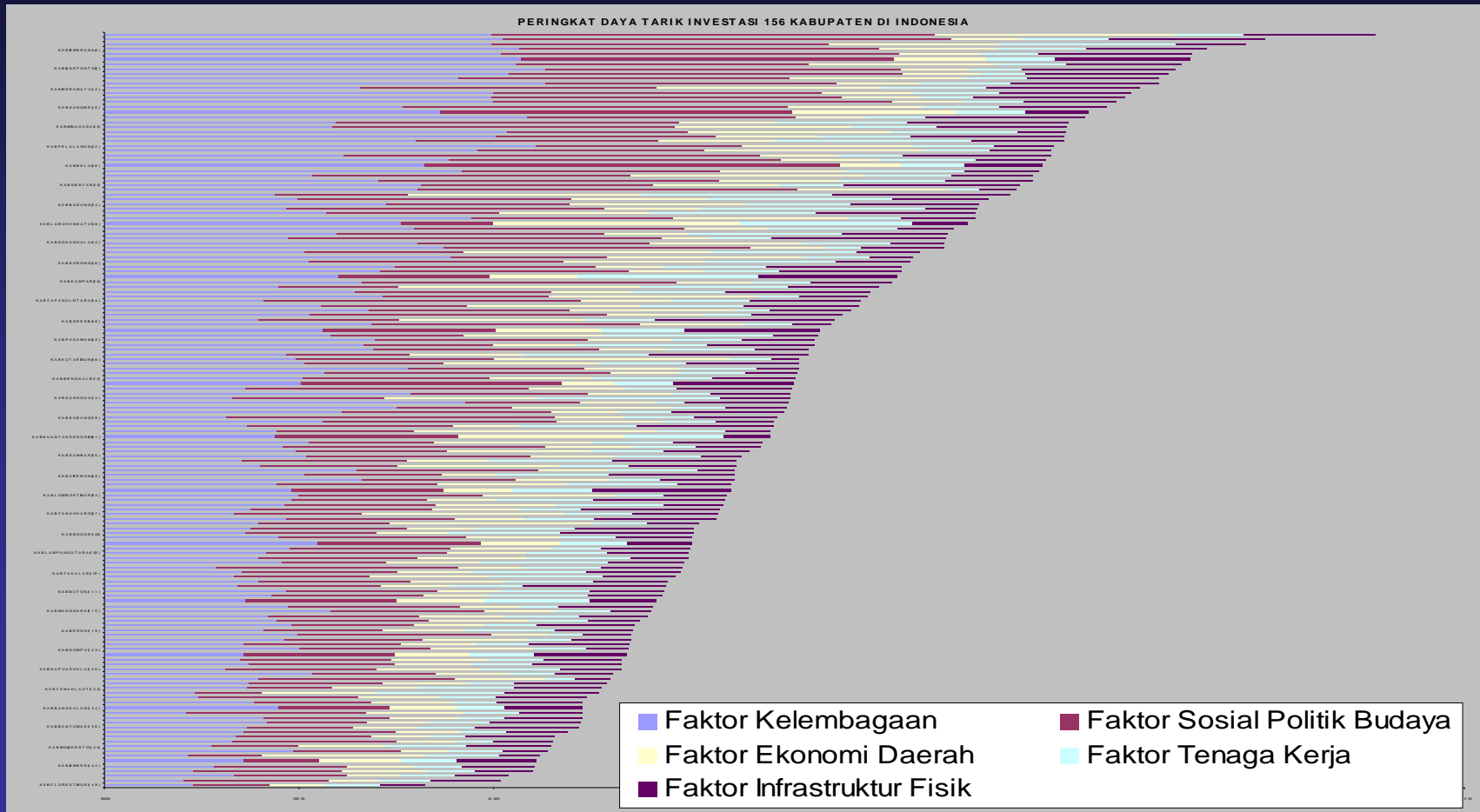
Source: KPPOD 2005

Variation of License Provision

"One Stop Services"

Solok

(1) Solok
'Good' (3.8)

Klaten

(6) Klaten
'Very Poor' (0.8)

Another Angle: "Debt Trap"

Reported Bribing Conventions of New Public Servants (PNS)

Respondent	1) Klaten			2) Kebumen			3) Solok			4) Pesisir Selatan		
1	70	(Academic)	↑	0	(Business)	↓	0	(Business)	↓	20	(Business)	↑
2	50-60	(Official)	↑	5-10	(Business)		0	(Business)	↓	Exist	(Business)	
3	75	(NGO)	↑	0	(Official)	↓	0	(NGO)		30	(Media)	↑
4	75	(NGO)	↑	5-10	(Media)	↓	0	(Business)	↓	10-20	(NGO)	↓
5	90	(Media)	↑	Exist	(Academic)		0	(Media)	↓	20-25	(Business)	
6	50	(Business)	↑	Exist	(Business)		0	(Official)	↓	25-30	(Business)	
7	5-90	(Media)	↑	10-20	(NGO)		0	(Academic)	↓	Exist	(Official)	
8	50-100	(Business)		-	-	-	0	(NGO)	↓	20-25	(Official)	
9	50-70	(Business)		-	-	-	0	(Business)	↓	-	-	-
10	50	(Business)		-	-	-	-	-	-	-	-	-
Tendency	*Range: 5-100 ; Ø: 64; ↑*			*Range: 5-20 ; Ø: 6; ↓*			*Range: 0; Ø: 0; ↓*			*Range: 10-30; Ø: 23; ↑*		

Respondent	5) Gianyar			6) Karang Asem			7) Lombok Timur			8) Bima		
1	Exist	(Business)	↓	5-10	(Business)	↓	20-50	(NGO)	↑	Exist	(Business)	
2	30-40	(Business)		- 20	(Business)	↓	30-40	(Media)	↓	40	(Official)	↑
3	Exist	(Parliament)		10-20	(Business)		30	(Business)		30-40	(Business)	
4	0	(Business)	↓	Exist	(Business)	↓	25	(Business)		40-50	(NGO)	
5	Exist	(NGO)		12	(Media)		50	(Business)		20-30	(Business)	↑
6	Exist	(Media)		5-24	(Academic)		30	(Business)		30	(Parliament)	↓
7	-	-	-	30	(Parliament)		50	(Academic)	↑	20-40	(Media)	
8	-	-	-	Exist	(Business)	↑	20-50	(Parliament)	-	40-50	(Academic)	↑
9	-	-	-	30-50	(NGO)		-	-	-	30-45	(NGO)	↑
10	-	-	-	-	-	-	-	-	-	35-50	(Business)	
Tendency	*Range: 0-40; Ø: 18; ↓*			*Range: 5-50; Ø: 17; ↓*			*Range: 25-50; Ø: 36; ↑*			*Range: 20-50; Ø: 36; ↑*		

1) Leadership
Sumatera & Java Set

Leadership Sets

Kebumen & Solok – distinctively higher Leadership

District	Set	Province	Proximity to Jkt	Geography	Dominant Ethnic Group	Leadership (Media Coverage) ex ante	Leadership AC (KPPOD) 1-9 ex ante	Leadership (Own-Survey) 1-9 ex post	Voiced Interests (Chamber & Media) ex ante	Schooling (Yrs) 1999 ex ante	Literacy (%) 1999 ex ante
					Geography & Culture	**LEADERSHIP**			**VOICED INTERESTS**		
Kebumen	1	Central Java	800 km	Central	Javanese (99.6%)	strong (CNN++)	5.2	6.7	not significant	6.2	85%
Klaten	1	Central Java	800 km	Central	Javanese (99.3%)	weak	3.4	3.7	not significant	7.3	83%
Solok	2	West Sumatera	1200 km	West	Minangkabau (96.3 %)	strong (Bung Harta)	7.3	7.5	not significant	6.8	95%
Pesisir	2	West Sumatera	1200 km	West	Minangkabau (94.6 %)	weak	5.3	5.0	not significant	7.4	94%

District	Set	Province	PCI 2003	Poverty 2001	Transfers 2001	Dominant Ethnic Group	Population 2001		PDIP 1999	Golkar 1999	Big Five 1999
					Control Variables				**Political Parties**		
Kebumen	1	Central Java	1,806,573	28%	286,681,905,070	Javanese (99.6)	1,162,280		39%	12%	51%
Klaten	1	Central Java	3,214,130	24%	298,096,331,879	Javanese (99.3)	1,108,140		56%	12%	68%
Solok	2	West Sumatera	3,310,817	12%	167,470,881,914	Minangkabau (96.3 %)	434,680		6%	33%	39%
Pesisir	2	West Sumatera	3,800,692	13%	138,498,034,104	Minangkabau (94.6 %)	388,720		13%	25%	38%

Business Climate Indicators (2005)	Central Java	
	Kla	Keb
(a) Licensing - Capture	Poor (2.2)	Poor (2.3)
(b) Licensing - Adm. Time	Poor (2.6)	Poor (2.7)
(c) Distortionary Taxes	None (+)	None (+)
(d) Quality of OSS	V-Poor (0.8)	Poor/Fair (2.3)
(e) Road Quality	5.5	6.0
(f) Fair Tendering	2.3	4.0
(g) Entry Bribe	64	6

Business Climate Indicators (2005)	West Sumatra	
	Sol	Pes
(a) Licensing - Capture	Good (1,4)	Poor (2.2)
(b) Licensing - Adm. Time	Good (1,4)	Fair (1.8)
(c) Distortionary Taxes	None (+)	Road Levies (-)
(d) Quality of OSS	Good (3,8)	V-Poor/Poor (1.4)
(e) Road Quality	7.5	6.6
(f) Fair Tendering	5.8	5.7
(g) Entry Bribe	0	23

2) Voiced Interests
Bali & NTB Sets

Voice Sets

Gianyar & Bima – distinctively higher 'Voice Proxies'

District	Set	Province	Geography & Culture			LEADERSHIP			VOICED INTERESTS		
			Proximity to Jakarta	Geography	Dominant Ethnic Group	Leadership (Media) ex ante	Leadership AC (KPPOD) 1-9 ex ante	Leadership (Own-Survey) 1-9 ex post	Voiced Interests (Chamber & Media) ex ante	Schooling (Yrs) 1999 ex ante	Literacy (%) 1999 ex ante
Gianyar	3	Bali	1200 km	Central/East	Balinese (97.2%)	weak	6.6	4.6	Handicraft Assoc.	7.6	82%
Karang	3	Bali	1200 km	Central/East	Balinese (95.8 %)	weak	6.2	4.7	not significant	4.7	68%
Bima	4	NTB	1600 km	East	NTB Bima (81,8 %	weak	4.3	5.8	KADIN & Econ Forum	7	82%
Lombok	4	NTB	1600 km	East	NTB Sasak (96.5)	weak	3.9	5.7	not significant	5.5	75%

District	Set	Province	Control Variables							Political Parties		
			PCI 2003	Poverty 2001	Transfers 2001	Dominant Ethnic Group	Population 2001			PDIP 1999	Golkar 1999	Big Five 1999
Gianyar	3	Bali	5,885,810	6%	230,931,353,292	Balinese 97.2	391,540			87%	7%	94%
Karang	3	Bali	3,636,563	19%	123,543,156,920	Balinese 95.8	359,510			78%	12%	90%
Bima	4	NTB	2,251,138	34%	209,619,357,523	Bima-Bugis (8	505,030			6%	52%	58%
Lombok	4	NTB	2,160,519	37%	255,143,196,896	Sasak (96.5)	971,220			9%	44%	53%

Business Climate Indicators (2005)	Bali	
	Gia	Kar
(a) Licensing - Capture	Poor (2.5)	Good (1.4)
(b) Licensing - Adm. Time	V-Poor (4.3)	Poor (2.5)
(c) Distortionary Taxes	None (+)	None (+)
(d) Quality of OSS	Fair (3.1)	None (0)
(e) Road Quality	7.8	8.0
(f) Fair Tendering	5.4	6.1
(g) Entry Bribe	18	17

Business Climate Indicators (2005)	NTB	
	Lom	Bim
(a) Licensing - Capture	Fair (1,6)	Fair (1,6)
(b) Licensing - Adm. Time	Fair (1,8)	Good (1,5)
(c) Distortionary Taxes	Export Tax (-)	Export Tax (-)
(d) Quality of OSS	Poor/Fair (2,4)	None (0)
(e) Road Quality	`6.9	5.5
(f) Fair Tendering	3.9	4.8
(g) Entry Bribe	36	36

Explaining Empirical Results

Indicators (2005)	Kla	Keb	Sol	Pes	Gia	Kar	Lom	Bim
	L	**L**			**V**			**V**
(a) Licensing - Capture	Poor (2,2)	Poor (2,3)	Good (1,4)	Poor (2.2)	Poor (2.5)	Good (1,4)	Fair (1,6)	Fair (1,6)
(b) Licensing - Adm. Time	Poor (2.6)	Poor (2.7)	Good (1,4)	Fair (1.8)	V-Poor (4,3)	Poor (2,5)	Fair (1,8)	Good (1,5)
(c) Distortionary Taxes	None (+)	None (+)	None (+)	Road Levies (-)	None (+)	None (+)	Export Tax (-)	Export Tax (-)
(d) Quality of OSS	V-Poor (0.8)	Poor/Fair (2,3)	Good (3,8)	V-Poor/Poor (1,4)	Fair (3,1)	None (0)	Poor/Fair (2,4)	None (0)
(e) Road Quality	5.5	6.0	7.5	6.6	7.8	8.0	`6.9	5.5
(f) Fair Tendering	2.3	4.0	5.8	5.7	5.4	6.1	3.9	4.8
(g) Entry Bribe	64	6	0	23	18	17	36	36

Voiced Private-Sector Interests

Overall: Prevailing Collective Action / Power Problems

1) 'Local Iron Triangles' & Uncontested Markets

2) Low performance of local parliaments (DPRD)

3) Weak Local Chambers (KADIN)

4) Voice depends on Social/Economic Status

5) History of 'Authority & Control' - Initially Rough
Soil for Young Democracy (Mobilizing by Elites)

Perception of Local Parliaments
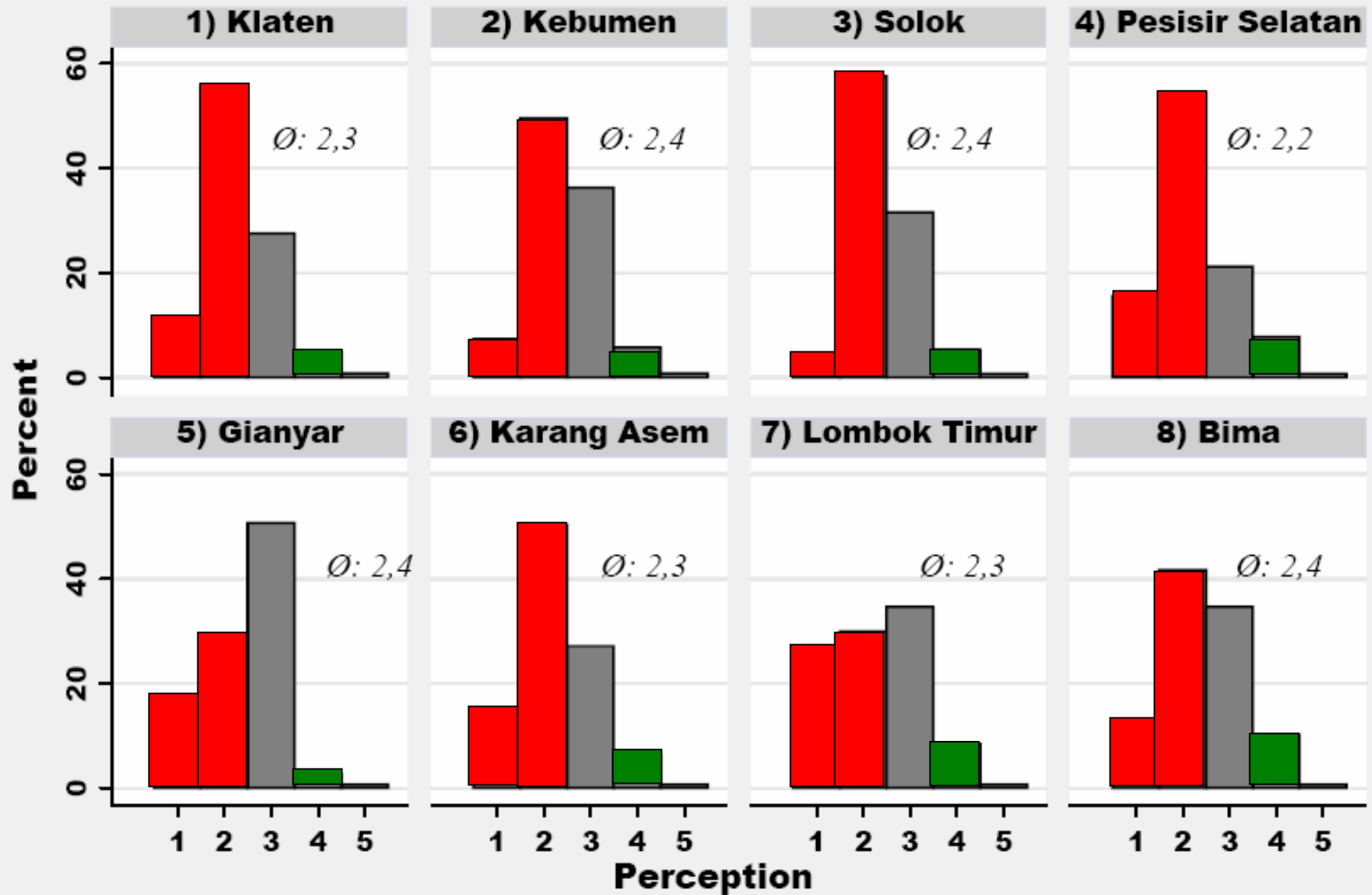
Impact of Executive Leadership

*Overall: Possible Counterbalance
        In times of civic and legal weakness…*

1) Can curb PNS Bribing Conventions (Debt Trap)

2) Can curb Iron triangles (more market contestability)

3) Can compensate (in the short term) for weak law enforcement and national oversight problems

4) Solok: Strong push for better (One-Stop) Services

5) Kebumen: Strong push for media-based transparency

Quantitative Analysis

Regression Results

	(1) Lic- Index	(2) P-Tender	(3) Road-Qual	(4) Regulations
LEAD	1.94*** (7.48)	0.39*** (7.06)	0.48*** (6.67)	0.12*** (2.67)
VOICE	0.89*** (4.09)	0.30*** (6.33)	-0.07 (-1.22)	-0.01 (-0.21)
PCI_03	-1.05** (-2.34)	-0.04 (-0.43)	-0.15 (-1.22)	-0.16** (-2.15)
AGRO_03	-0.13 (-0.58)	0.04 (0.76)	-0.11* (-1.82)	-0.09** (-2.13)
TRANSF_03	-0.41 (-0.76)	0.01 (0.09)	-0.10 (-0.69)	-0.06 (-0.73)
EAST_INDO	1.31 (1.38)	0.33* (1.63)	-0.10 (-0.39)	0.00 (0.02)
POVERTY_01	-0.34 (-0.81)	-0.04 (-0.48)	-0.08 (-0.69)	-0.06 (-0.86)
F	26.7	33.43	8.86	2.39
R2	0.49	0.54	0.24	0.10

N= 205 Districts ; Data-Sources: KPPOD, Asia Foundation, World Bank

Licensing & Voice
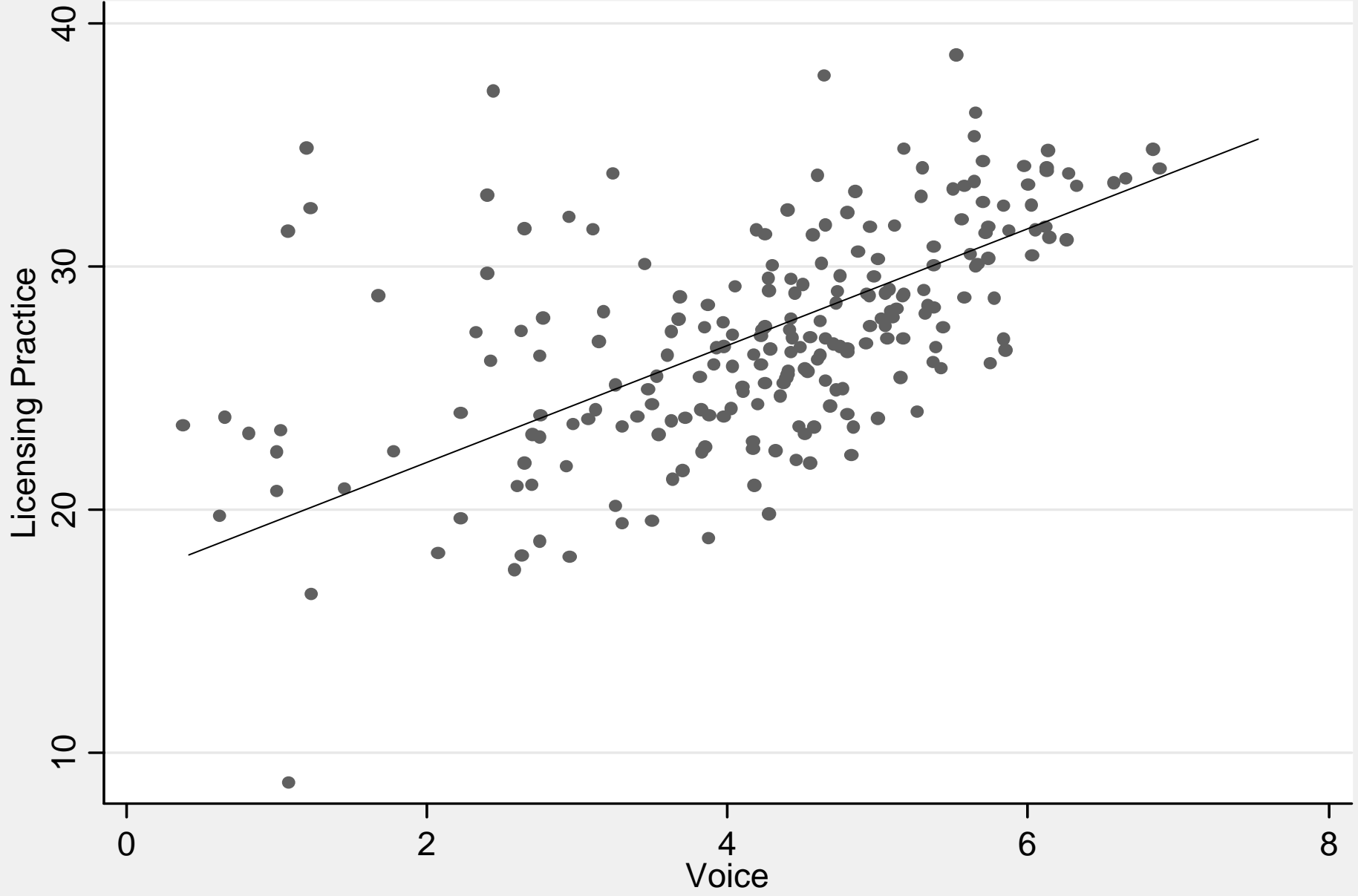
Licensing & Leadership
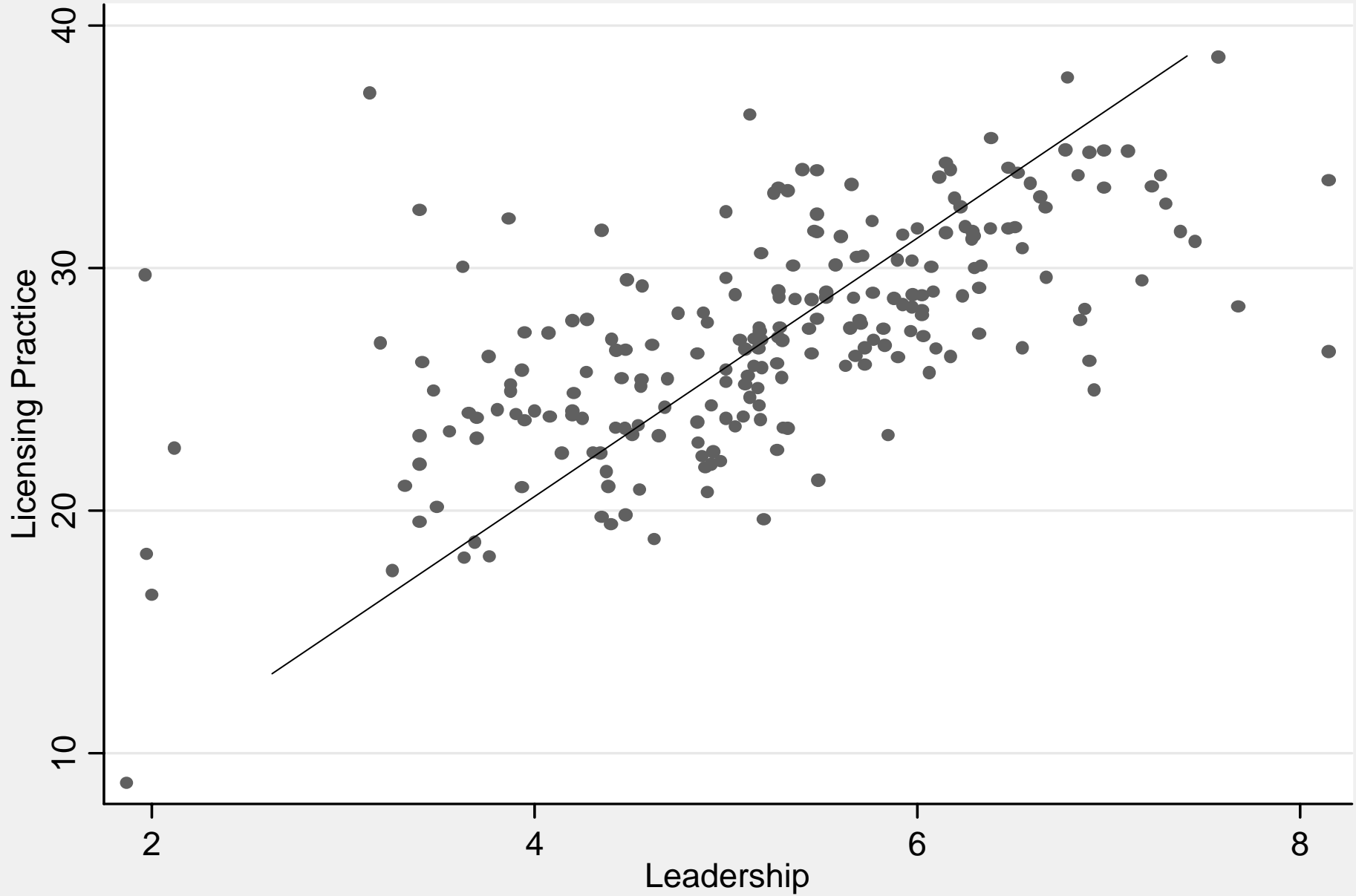
In Summary …

1. Business Conditions <u>vary strongly</u> (sample/population)

2. Unsatisfactory Business Conditions partly caused by:
   <u>Dept Trap</u> / <u>Parliament Detachment</u> / <u>Vague Tax Law</u>

3. <u>Executive Leadership</u> appears to explain variance better than <u>Private-Sector Voice</u> – at least during first 5 Years

4. Decentralization : Voice of Private-Sector still <u>uncertain</u>; yet Leadership has become <u>contestable</u> across districts…

5. In the <u>immediate term</u> – Leadership <u>may</u> compensate for low voice /law enforcement /national monitoring

Thank You Very Much For Your Kind Attention !