Strategies of Development:

Indonesia and Malaysia 1960 – present

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May 2005

Table of Contents

List of Tables

I. Specific Policies

A. Policies in the Four Aspects

Aspect 1: Social

Indonesia

During the so called New Economy from 1966 to the end of the Suharto regime, Indonesia was less successful at improving overall social conditions than it was in strengthening the economy, and the Asian economic crisis of 1997 unravelled much of the progress Indonesia was able to achieve during this period. Petroleum fueled the initiatives, as during this period Indonesia was earning good revenue from oil exports and employing it to advance its development goals (Wie, 2002 pg. 201-203).

Education was one of these goals, and during this period Indonesia endeavored to expand education initiatives, particularly for primary school children. By the mid-1980s Indonesia had achieved nearly universal primary education, a feat made possible as a result of a concurrent and very successful birth control program which slowed population growth (Wie, 2002 pg. 201-203). The program was called, the PKBI ("Perkumpulan Keluarga Berencana Indonesia" – the Indonesian Family Planning Association), and was founded specifically to aid families in planning the number of children they'd like to have. During its initial years of operation, its primary activities included advocacy and a broad information program that included marriage counseling, infertility therapy, and birth spacing clinics. The program was initially supported by the actions of individuals and international sponsors, and opposed by the national government (Sarwono, 2003 pgs. 19-22). But when Suharto declared population control and family planning to be a key element of his New Order government the PKBI was formalized and supported by the national government, and its well-established framework became extraordinarily amenable to the diffusion of what was now official government policy regarding population planning (Sarwono, 2003 pg. 28).

While the effort to expand primary education was quite successful, the effort to expand secondary and tertiary education was mixed. Because enrollment rates were so low initially in the 1960s, the achievement appeared superior to results in other Southeast Asian countries, but by the end of the time period in question, enrollment at both levels lagged far behind that of other South East Asian countries and still does (Wie, 2002 pg. 201-203).

One of the proudest achievements of Indonesia's post-Sukarno New Order government during this time of resounding growth was the fact that it met its goal of reducing absolute poverty. From 1976 to 1996 estimates of absolute poverty declined from 40% to 11% (56 million to 23 million people), a feat unmatched in other developing world countries. The World Bank lauded Indonesia for being the nation that had best eliminated absolute poverty during this time period (Wie, 2002 pg. 225). Indonesia committed to a broad-based rural development strategy, which targeted the rural areas in which the majority of Indonesia's poor lived and worked –particularly rural Java – and ensured that economic growth wouldn't be immiserating for the poorest sector of society. At the same time, increased production in the rice sector spawned a whole new industry of off-farm jobs in processing, transport, and commerce. The economic growth led to a corresponding boom in both the construction and manufacturing sectors. Both of these phenomena led to higher household incomes and a reduction in overall poverty (Wie, 2002 pg. 227)

While statistically, Indonesia's Gini ratio remained constant over this time period, it is widely believed that economic disparity between the rich and poor actually increased and that urban-rural and even Western-Eastern divisions grew more entrenched. Two factors that may have contributed to an exacerbation of social inequity are the effects of foreign direct investment (FDI) which led to a class of highly-paid employees, and the importance of large-scale capital- and resource-intensive industries during the early phases of industrialization (Wie, 2002 pg. 227). Econometric studies show from 1970-1990 average incomes not only grew more quickly in the cities, but that for the capital city, Jakarta, the effect was even more pronounced, owing to large-scale investment projects in the greater Jakarta region and Bandung, and to a lesser extent, the city of Surabaya (Wie, 2002 pg. 227).

From the 1960s through the present, improved nutrition, environment, and health care through local public health clinics led to lower infant mortality rates. However, infant mortality remains higher in Indonesia than in other Asian – particularly East Asian – countries to this day (Wie, 2002 pg. 203).

Social development played second fiddle to overall economic development however. Wie points out that the Indonesian government concentrated first on economic development before turning its attention to social development, but because it started its economic development about a decade after its southeast Asian neighbors its statistics do not currently compare favorably to social indicators in neighboring countries (2002 pg. 203). The sequence of development may be more related to the fact that many social programs were initiated and sustained with the revenues from export of oil during the oil shock years of the late 1970s. Suharto channeled the oil revenues into “populist programs, subsidies for staple goods, and various charity programs identified personally with [president Suharto], thus enabling him to disperse benefits in broadly patrimonial ways” (Case, 2001 pg. 100).

Malaysia

Malaysia much more successfully channeled economic growth into an opportunity to strengthen the middle class and escape the post-colonial pattern than did Indonesia. In fact, Harold Crouch wrote in 1996, 'Malaysia's rapid economic growth … since independence transformed its class structure. The most striking changes have been the rapid growth of the urban middle class and the decline in rural occupations (quoted in Drabble, 2000 pg. 271).

Abandoning the laissez-faire policies which had characterized the 1960s, Malaysia made a conscious effort to redress serious income inequity issues by means of a targeted economic plan called the NEP ("New Economic Policy"). Initiated in 1970, the NEP's principal goals were to restructure the economy and society to eradicate the close race/social function correlation inherited from the colonial period, and to eradicate poverty irrespective of race (Drabble, 2000 pg. 197). While in the early years of the NEP income distribution worsened, it improved radically from 1976-1984, during which time the Malays (*bumiputeras)* made great gains against the Indians and particularly the Chinese ethnic groups (Drabble, 2000 pg. 277). The gain in income for Malays came as a result of the expansion of export-oriented industrialization and the rural development programs in East Malaysia. During this time, petroleum exports provided the government with a steady source of (quite substantial) income, which it used as transfer payments in its effort to lessen the economic gap between bumiputeras and non-bumiputeras (Drabble, 2000 pg. 278)

By the end of the NEP in 1990, poverty in Malaysia remained overwhelmingly rural. Rice farmers were more often than not below the poverty line, and holders of small rubber plantations were only marginally better off. At the same time, the urban-rural divide remained essentially distinct: urbanites experienced the largest economic gains over this period as the entire urban landscape was modernized into shopping centers, high-rise office buildings, and the like. The rural poor are increasingly supported by remittances from their children, who have left the farms to find work in industry in the cities (Drabble, 2000 pg. 282).

Malays of all classes did not hesitate to press for better educational opportunities following independence. Accordingly, the Malaysian government launched development projects that built roads and improved communications throughout rural areas, to promote Malay access to schools and connected outlying communities to the state-provided schools. Being able to physically travel to schools encouraged Malays to do so, and as a result, from 1960 to 1970 school enrollment in eligible age groups leapt by 97% in Peninsular Malaysia, and by an impressive 217% in Sabah and Sarawak. Of those, a growing proportion of students was women: by 1973 women made up 45% of the student body (Drabble, 2000 pg. 284). Higher education initiatives began in the late 1960s just before the NEP, with similar effects: enrollment increased from 13,000 in 1965 to 194,000 in 1990 (Drabble, 2000 pg. 284). The educational system involved quotas that favored bumiputeras, and led to the emergence of a bumiputera middle class. While generally a successful policy, the educational initiative failed to foster the national solidarity the government had envisioned. Segregation of schools along ethnic lines not only engendered significant differences in learning experience between races but also dampened aspiration and competitive spirit, and by the mid 1980s an education-occupation mismatch had begun to develop, and several occupations, particularly engineers, required recruitment from overseas (Drabble, 2000 pg. 285-286).

Table 1 below summarizes each nation’s policy strategy.

	Indonesia	Malaysia
Social Strategy:	broad rural development to reduce overall poverty	strengthen the middle class through export-oriented industrialization
Education:	universal primary education (achieved by 1986)	increase access to schools through roads and communication equipment
Demographics:	successful birth control program that reduced population growth	—
Health initiatives:	built clinics, improved nutrition by placing price controls on staple foods	—

Table1: Social Policy Comparison

Aspect 2: Economic

Indonesia

The broad economic policy frameworks of Indonesia, Malaysia, and the rest of Southeast Asia followed similar trajectories during the second half of the 20th century. John Minns describes it as follows:

> "The [capitalist] nationalists of postwar Southeast Asia saw their key task as being to break away from the role of raw material supplier assigned to their countries by colonialism, in the belief that failure to do so was likely to lead to deepening poverty in a world dominated by industrial societies. Both nationalism and future prosperity demanded industrialization. Yet the human and physical resources required to begin the process were in short supply, and the lack of a substantial indigenous bourgeoisie or significant amounts of capital drove every country in the region to make

> some attempt at state planning and/or ownership between the 1950s and the 1980s (2001 pg. 27).

In Indonesia's case, president Suharto realized immediately that economic growth would be essential to the political stability of Indonesia during his administration, and relied on neoclassical economists to guide the nation. They reversed the statist policies Suharto's predecessor Sukarno had implemented and in doing so attracted foreign investment and developmental aid. But the initial wave of foreign investment came from Japanese investors that pushed indigenous Indonesians out of the textile industry as the Japanese aligned themselves with the ethnic Chinese. This sparked a wave of protests in 1974 now known as the Malari riots, and Suharto was forced to curb foreign investment (Case, 2001 pg. 99).

With few exceptions, the Indonesian economy under Suharto's management was carefully deregulated and liberalized in ways that promoted economic growth but did not force him to relinquish control of either the state or the state economy. The oil shock of 1974 was a windfall for Indonesia, as the four-fold increase in prices provided an excellent source of revenue with which to encourage and control development. Suharto did so craftily, taking advantage of the ethnic Chinese, whom he used to promote businesses, secure in the fact they posed no political threat. As of 1985, workers were absorbed into a single labor union, SPSI ("All Indonesia Workers Union"), which the military largely kept in check and kept labor prices artificially low. This combination of a mostly-liberal economy wed to tight control of social forces was known as the "Pancasila Economy" (Case, 2001 pg. 100).

Suharto saw the need to allow economic freedom – within the limits he set – in order to provide incentives for growth, but he made clear that control would be maintained from above to shape the new economy. In a major speech delivered in April 1970 he stated that having taken measures to restore fiscal equilibrium, abolish an unfair "quota" system for exports/imports, and regulate both monetary matters and the banking system, his administration intended to promote growth. That growth would come as a result of an emphasis on individual responsibility and initiative, market forces, and greater freedom for business, but at all times the government would "supervise and control the factors and circumstances which influence market forces" (quoted in Chalmers and Hadiz, 1997 pg. 54-55).

Indonesia under the GOLKAR New Order State depended for its economic growth on two principal factors: oil revenue and international assistance (Budiman, 1988 pg. 126). The foreign aid led to Indonesia's massive $25.4 billion international debt at the end of 1982, a figure that led to a 28% debt-service ratio. While this is not as serious a debt-service ratio as those seen in some Latin American countries in the same time period, Malaysia's debt service ratio at the same time was only 15%, and worse, Indonesia's ability to pay off that debt was entirely dependent on oil revenue (Budiman, 1988 pg. 126). As such, Budiman posits that the astonishing economic growth Indonesia exhibited throughout much of the 1970s was due not to increases in capability and productivity under capitalism but rather to an economic boom resulting from oil revenue. Oil shocks in 1982 promptly reduced the rate of economic growth in GDP terms from 8.6% to 2.24% (1988 pg. 126-127).

Statist nationalism thus set the agenda from the 1960s through the mid-1970s. Oil money had led to an expansion of state controls in nearly all areas of economic activity and the development of a patrimonial system in which successful capitalists depended almost completely upon the state for protection. Foreign capital had little influence in this environment, and the World Bank lacked leverage in Indonesia at the time to press for more market reforms. Its 1981 Report recommended that in order to reduce economic inequalities and promote entrepreneurship Indonesia would have to move towards a program of economic deregulation and free trade (quoted in Chalmers and Hadiz, 1997 pgs. 91-6).

Overall, the world oil market may have been more influential than World Bank policy memos. Falling oil prices through the the mid 1980s unleashed a fiscal crisis that Suharto was forced to contend with by taking the World Bank's advice (quoted in Chalmers and Hadiz, 1997 pgs. 91-6). He reacted to the need to re-energize the economy by further deregulating it. He opened up the banking system and the Jakarta Stock Exchange to foreign investors, who took full advantage of the opportunity, and reformed tariffs using the APEC meeting in Jakarta (1994) to prompt free trade reforms in Southeast Asia. The combination of policies spawned a plethora of small and medium-sized enterprises engaged in light manufacturing of labor-intensive goods like shoes, furniture, and office supplies (Case, 2001 pg. 101).

That is not to say the Indonesian economy under Suharto was ever completely free. Beginning in the early 1980s Suharto pressed his children into business ventures with monopoly licenses and sole distributorships. The nepotism continued even after liberalizing the banking system, when Suharto shifted to a new bevy of tools like state contracts, selective cheap credit to political and economic allies, and discounted shareholding (Case, 2001 pg. 101). This so-called “crony capitalism” may have been the undoing of the Indonesian economy. Indonesia was one of the hardest-hit Southeast Asian nations in the financial crisis of 1997-1998, during which its GNP shrank by a massive 15%. The modern service and manufacturing industries suffered the most, which affected the new urban middle class. Suharto, stripped of the resources he needed to dole out and restore order, lost political power and stepped down. Surprisingly, his resignation placated the masses, who did not proceed to press for market reforms and an end to crony capitalism (Case, 2001 pg. 104-5).

Suharto's immediate successors, B.J. Habibie and Megawati Sukarnoputri, made no abrupt changes to economic policy. Not until 1999 with the election of Abdurrahman Wahid, an Islamist, was there an effort to right the economy. Wahid cooperated with the IMF in order to garner financial support, and made an attempt at economic reform. These reforms were often blocked by appeals for ethnic or religious favoritism, or Wahid's own ineptitude in the implementation of policy – he frequently sidestepped the rules in ways that heightened suspicion about the transparency of his government (Case, 2001 pg. 106-7). Foreign investors had a difficult time entering the Indonesian market under such circumstances, finding their offers rebuffed by appeals to "economic nationalism" (as was the case in the aborted sale of automobile assembly subsidiary Astra). Political pressure forced Wahid to permit local authorities to retain a greater share of the economic returns from the gas and mineral sectors, revenue which flowed unimpeded to Jakarta under Suharto's watch. This has hampered the ability of foreign investors to enter those markets as well (Case, 2001 pg. 107).

Monetary policy during this time period targeted different goals at different points of Indonesia's economic expansion. Suharto from the beginning was averse to fiscal deficits. Management of monetary policy was largely driven by external factors that caused the Indonesian government to react (Cole and Slade, 1996 pg. 66).

From 1968, when Suharto revamped the banking system, until 1973, monetary policy targeted the stabilization of prices, the defense of Indonesia's limited foreign exchange reserves, the continued rehabilitation of the banking system, and the reconstruction of an economy left in tatters by the Sukarno administration (Cole and Slade, 1996 pg. 40-1). State banks extended credit through programs in which the private banking sector was excluded. At the same time, Indonesia opened its unreliable foreign exchange management system and developed it into one of the most open foreign exchange regimes in the world. A dual exchange rate mechanism favored exports but forced exporters to spend earnings on certain specified imported capital goods. This system was converted to a fully unified fixed exchange rate in 1970 (Cole and Slade, 1996 pgs. 42-3). From 1973 to 1982, monetary policy shifted to a program of credit ceilings and interest rate controls. This was a major disincentive to save in banks deposits, and led to extensive borrowing overseas while doing little to control inflation. As a result, the Indonesian government scrapped the credit and interest rate ceilings, and moved to more indirect methods of managing Indonesia's macro-economy, including issuing of government paper and other financial instruments (Cole and Slade, 1996 pg. 65-6).

From 1960-1982 foreign aid to Indonesia helped finance many of the credit programs to rural farmers, while the oil boom from throughout the 1970s until about 1983 prompted the damaging credit controls described above and retarded development of a strong financial sector. In sum, Cole and Slade note two broad trends over the past half-century of Indonesia's economic development. The first is Indonesia's overall reluctance to move to fully market-determined interest rates and foreign exchange; the second is that in times of real or perceived threat to its foreign reserves, the Indonesian government has not hesitated to force banks to transfer foreign reserves to the central bank. As a consequence, banks have been forced to remain liquid and be prepared for occasional shocks. This has perhaps dampened local investment overall (Cole and Slade, 1996 pg. 67, 76).

From when Suharto took office until 1983, Indonesia's tax system was "grossly defective" (Gillis, 1994 pg. 14). Tax policy had been micro-managed for decades to promote non-revenue goals like income redistribution and regional development. Tax incentives were implemented to guide personal consumption and investment decisions, including specific tax exemptions and and tax-rate differentiation, six-year tax holidays designed to encourage private investment in specified sectors and to specific geographical regions, as well as five- to ten-year customs duty exemptions for the imports of firms also eligible for the tax holidays. Tax incentives targeted activities as specific as the construction of bowling alleys or the financing of traveling chess champions (Gillis, 1994 pg 17-18). The Indonesian government collected very few taxes from the non-oil sectors of the economy, partially because it could afford not to in the context of massive oil tax revenues. But the casual Indonesian small-business owner could scarcely pay taxes anyway, as years of targeting programs made the tax code incomprehensible and highly subjective (Gillis, 1994 pg. 18-19).

Stephen Smith points out that for a brief period in 1981 Indonesia experimented with countertrade, a policy that effectively legitimizes an inefficient form of barter, trading goods for goods in a balance with one other country over time. The government mandated that foreign contractors awarded construction or procurement contracts in Indonesia export an equal value of Indonesian commodities from a list of approved products (fish, rubber, tin, coffee, etc.) or purchase them themselves. Malaysia retaliated to ensure Indonesia's policy didn't cause a loss of exports for Malaysia. Both nations abandoned this counter-productive policy shortly thereafter (Smith, 1994 pgs. 139-141).

Malaysia

The Malaysian experience was similar, best characterized by heavy-handed state intervention and a reticence to leave the fate of the national economy up to the market. The IMF wrote in 2001, "As an emerging market economy, Malaysia is clearly a success story." (Meesook et al., 2001 pg. 1). Malaysia inherited an essentially intact and smoothly-functioning bureaucratic system when the British granted its ex-colony independence in 1963. The economy grew slowly and steadily in the next decades at a rate that varied from province to province but that approached 8.6% GDP growth in Peninsular Malaysia in the 1980s (Drabble, 2000 pg. 187). Malaysia's planning mechanism was a series of medium- to long-term development plans that the administration implemented effectively. Malaysia's economic policy passed through three distinct phases: From 1958-1970 the emphasis was on import substitution industrialization (ISI); from 1970-1980 the emphasis shifted to export-oriented industrialization (EOI); and from 1980-1985 Malaysia briefly experimented again with ISI, and abandoned it thereafter for export-oriented industrialization. Successive Malaysian five-year plans elaborated the successive policies, and the New Economic Plan (NEP) defined the political context of economic development from 1970 onwards (Drabble, 2000 pg. 186-87).

From the onset of the NEP, Malaysia's strong economy had one of the highest investment ratios in the region, and as a result the country's economy shifted from agriculture and mining to increased manufacturing (Meesook et al., 2001 pg 1). Liberalization measures increased competition and productivity, particularly in the growing electronics sector and other export industries. But the development plans were financed publicly, leading to increasing and unsustainable public budget deficits. The Malaysian government was forced to pause long enough to bring those deficits under control before proceeding to diversify the economy under a policy framework of continued deregulation and liberalization (Meesook et al., 2001 pg. 1).

In spite of growing social cohesion as a whole as a result of the NEP, over the period from the 1960s to the 1980s different geographical regions of Malaysia developed differently: while Peninsular Malaysia began to develop a manufacturing sector and light industry, the provinces of Sabah and Sarawak relied more on the export of raw materials – particularly wood and agricultural products – and thus continued to be more exposed to the fluctuating prices of the world market (Drabble, 2000 pg. 186-87).

During this time, Malaysia's trading partners shifted. While the USA remained the primary consumer of Malaysian exports, Malaysia began to export less to Europe and more to the ASEAN countries. At the same time, greater exports of manufactured goods lessened Malaysia's vulnerability to world market price shocks. From 1970 to 1990, manufactured goods as a percent of total exports climbed from 12% to 60%. The Malaysian government instituted a trade regime that was liberal by international standards, but tended to emphasize the internal market over exports (Drabble, 2000 pg. 188-189).

Malaysia's growth continued to be strong through the 1990s until the financial crisis of 1997. Real output growth was on average 8½% per year, unemployment was less than 3%, and the treasury maintained "robust" supplies of international reserves (Meesook et al., 2001 pg. 1). Prices and the exchange rate were stable and predictable, which encouraged foreign borrowing but also generated large current account deficits as short-term capital inflows made up the difference, including through the stock market (Meesook et al., 2001 pg. 3). But systemic weakness in several areas led to a crisis in 1997. These weaknesses included rapid credit growth leading to excessive investment, which generated price bubbles in both the stock market and real estate markets in the context of weak supervision and regulation. Private investors engaged in the active but largely unregulated offshore market for the ringgit exposed the market to information asymmetries and encouraged risk taking (Meesook et al., 2001 pg. 3). The crisis, once unleashed, would force Malaysia's economic growth to a halt. The Malaysian economy righted itself only after radical macro-economic changes implemented against the advice of the IMF and World Bank, among these: converting the currency from a floating to a pegged exchange rate, capital controls to stem the exodus of out-flowing portfolio funds, and sharp hikes in interest rates (Meesook et al., 2001 pg. 7-8).

Malaysia's tax structure has been modified and adjusted many times over the period from 1960 to the present, but Malaysia has always wielded the tax system as a powerful mechanism to alter investment incentives. In particular, Malaysia has frequently made use of tax holidays and rapid tax write-offs of investment costs. Prior to the 1989 tax revision, all companies in Malaysia were subject to a 40% income tax and an additional 5% development tax. Companies whose income exceeded M$2 million were assessed a supplementary 3% excess profits tax. The 1989 reform softened these policies, reducing the income tax by 5% and phasing out the development tax over 5 years. Malaysia has always taxed real properties but not capital gains (Boadway et al., 1995a pg. 341-2). At the same time, indirect taxes have accounted for up to half of government tax revenues, including excise duties, export duties, and sales taxes.

Duties levied against imports decreased in importance from 1960 to the present and have targeted some consumers and not others. The principal duties are levied on petroleum and fuel oil imports and tobacco products (Boadway et al., 1995b pg. 377). Malaysia levies excise duties on a small number of domestically manufactured commodities, principally petroleum products and fuel oils, alcoholic beverages, motor vehicles, and tobacco products; exceptions are granted for particular users, activities, and goods in all cases (Boadway et al., 1995b pg. 377). Malaysia taxes exports as well, but at relatively low rates. Export taxes account for only 10% of total tax revenue and have dropped considerably since the 1960s (Boadway et al., 1995b pg. 377-8). Malaysia introduced a 5% sales tax in 1972 and raised it to 10% afterwards. Local manufacturers are taxed directly and foreign manufacturers are taxed at the port. Certain goods are exempt, including food and other necessary goods, petroleum products, construction materials, and certain pieces of machinery. Sales taxes on imports have dropped since 1972 (Boadway et al., 1995b pg. 378).

Prior to independence, the Malaysian currency was fixed to the pound sterling. Malaysia severed its link to the pound sterling in 1972 and moved to a managed float exchange regime that saw the exchange rate of the ringgit begin to rise slowly, and at the beginning of the time period studied, decided to peg its exchange rate to a basket of currencies instead of one single currency. This basket included the currencies of all of Malaysia's trading partners. Furthermore, this peg was increasingly managed in an unpredictable way: from 1981 to 184, the composite index used to determine the peg fluctuated between 103.5 and 109.5. As such, the IMF decided to classify the Malaysian exchange rate regime as managed float rather than basket pegging (Yan, 1991 pgs. 157-159).

The state development goals of intervention to promote economic restructuring involved careful macro-economic management. But by the 1980s the Malaysian economy had a large fiscal deficit due to worsening terms of trade, high real interest rates and an increasing debt service burden. All these were the result of excessive state investment in the productive sector. As a consequence, the Malaysian government was forced to reduce public spending, reduce popular demand for imported goods, and use monetary policy to facilitate growth and provide liquidity for private investment. It reduced interest rates and restructured its long-term foreign debt. (Pangestu, 1991 pgs. 135-138).

Table 2, following, summarizes economic policy implemented in both Indonesia and Malaysia during this time period.

	Indonesia	Malaysia
Overall regime	State-controlled industrialization	State-controlled industrialization
Development Aid	Yes: led to 28% debt service ratio	Yes
Foreign Direct Investment	Yes	Yes - strongest investment ratio in SE Asia
Market reform?	Deregulation and market liberalization	Deregulation and market liberalization
Monetary policy	price stabilization and defense of foreign reserves	State spending, external borrowing.
Exchange rate policy	dual rate that favored exporters; managed peg XR, then managed float.	Managed basket peg, then managed float XR
Tax policy	Manipulated regularly to target specific sectors or industries identified by the gov't	Excise duties on petroleum exports; tax policy used as a tool to target sectors

Table2: Economic Policy Comparison

Aspect 3: Political

Indonesia

Indonesia from 1966 and the emergence of the so-called "New Order state" developed under the aegis of a strong state overwhelmingly in the hands of the military, which gained strength until Suharto's eventual ouster at the turn of the millennium. The state-military complex controlled both political as well as economic life and permitted no challenges to its authority (Budiman, 1988 pg. 113). The New Order State under General Suharto restructured the political system to its liking, relying for political support on its traditional base: a coalition of anti-Communist forces from within the military, the Moslems, and the bourgeoisie Soeharto had pushed aside in his tenure during the transition from colonialism (Budiman, 1988 pg. 117).

Sukarno's administration developed GOLKAR ("the functional group"), a previously inconsequential right-wing political union, into a powerful political machine that permitted complete control over the state. First, it required that all state employees become members of GOLKAR, which permitted the party apparatus to infiltrate even the local levels of government, where it coerced villagers to support GOLKAR in elections (Budiman, 1988 pg. 120).

The political consolidation of GOLKAR forced all political opposition to aggregate around two camps, one which concentrated the non-GOLKAR Muslim vote and one which concentrated all remaining non-GOLKAR, non-Muslim votes. The New Order State meddled incessantly in the internal affairs of those parties to ensuring popular figures did not become candidates. For example, all political parties were required to get permission from GOLKAR in order to hold conventions. Finally, after the 1971 elections, all political positions such as cabinet members were required to come from GOLKAR, further desiccating political support for the non-GOLKAR parties (Budiman, 1988 pg. 120).

GOLKAR received strong support from Chinese nationals living in Indonesia. An historically wealthy and entrepreneurial class of non-Muslims, as well as supporters of the Dutch before nationalization, the Chinese in Indonesia have suffered sporadically from rising anti-Chinese sentiment and outbreaks of violence. GOLKAR was able to take advantage of the anti-Chinese sentiment by fostering the business interests of the Chinese, who would never be capable of mounting a legitimate political threat to GOLKAR, and who could be violently repressed simply by stirring up nationalist sentiment or ethnic-based hatred (Budiman, 1988 pg. 121-122).

At the same time, the Indonesian government cultivated an indigenous bourgeoisie, composed mostly of relatives of GOLKAR's top party members, whose businesses are dependent on official state patronage. The bourgeoisie in sum then became Chinese entrepreneurs dependent on the state for survival, a client bourgeoisie connected by blood ties to the GOLKAR elite, and a relatively small but independent bourgeoisie dependent, to a certain extent, on state patronage. Thus the New Order State was able to control politics by controlling the business elite (Budiman, 1988 pg. 122).

The labor movement met with fierce opposition throughout Suharto's tenure as president, and only began to take hold in the aftermath of the 1997 financial crisis when the International Monetary Fund forced Indonesia to adopt Western-style labor rights as part of a $14.1B economic bailout. Suharto's suppression of unions was an integral part of his strategy to promote exports by luring international investors to a country whose labor was kept artificially inexpensive. After Suharto's bloody crackdown of Communists in 1965 he permitted only one union, and appointed that union's leaders directly (Arnold, 2004).

Suharto's autocratic and paternalistic regime relied upon strong measures of repression whenever necessary. Suharto was an adept manipulator of political power, and repressed dissent using the military while simultaneously ensuring his friends and supporters were amply rewarded. He systematically repressed political challengers as well as potential challengers, including those in the military who might pose a threat to him. Organizations that might have permitted a forum for questioning or challenging the regime were banned, controlled from the inside by placed appointees, or depoliticized, a clever method of co-opting movements by drawing them into the state mechanism, particularly GOLKAR. This was the status quo, and it was heartily supported by Western governments, until the financial collapse of 1997 and the subsequent change in government (Martin et al., 2001).

Malaysia

Malaysia's government is a form of parliamentary democracy, an inheritance from its days as a British colony. But in the first four decades since it was granted independence, Malaysia had only four Prime Ministers, of which two had shortened terms only because of health issues. The tendency in Malaysia has thus been to foment a strong executive branch and maintain it by whichever subterfuge or back-room political bargaining is necessary to maintain the status quo (Yap, 2001 pg. 57). The general elections of 1969 in which the UMNO, a political party that favored ethnic Malays, suffered severe losses led to race riots and a suspension of democracy for 21 months. A broader alliance called the Barisan Nasional (BN) has ruled Malaysia ever since, and both political and economic policy has prioritized the quelling of racial tension by providing economic opportunities for ethnic Malays ("bumiputeras") (Economist Intelligence Unit, 2004 pg. 9). Fiona Yap reports that the suspicion and fear that divides the bumiputeras, who dominate the political sphere and comprise 60% of the population, and the ethnic Chinese, who dominate the economy and comprise 30% of the population, has led to incidents as recently as August 2000, when the UMNO youth organization staged a rally to protest a perceived attempt by the Malaysian Chinese Organization Election Appeals Committee to question Bumiputera rights and privileges (2001 pg. 61).

In 1987 the Malaysian government made a shift towards more pronounced authoritarianism when a split in the UMNO party nearly cost Dr. Mahathir Mohamad, who had been president of the party and Prime Minister of the nation, his political power. He reacted quickly to shore up his political base, making it more difficult within the UMNO to challenge an incumbent leader, stripping the judiciary of much of its independence and power, sacking the chief justice and suspending five Supreme Court judges to further intimidate the judiciary, and increasing the powers of the attorney-general, which left the government in a position of greater control (Economist Intelligence Unit, 2004 pg. 9).

Dr. Mahathir retired in October 2003 after 22 years at the helm of the Malaysian government. The nature of Malaysian politics during that period were overwhelmingly shaped as a result of his strong leadership and his manipulation of the political system and its parties. Malaysian politics since the departure of Mahathir has approached a generational gap which has seen the emergence of younger politicians and calls for greater democratic freedom. The current government faces the challenge of endemic corruption within the government, a strengthening conservative Islamic movement, and possibly worsening race relations, all of which have the potential to destabilize the nation (Economist Intelligence Unit, 2004 pg. 10). On the other hand, current prime minister Badawi has shown himself to be a more conciliatory leader willing to work with the West, a radical departure from Dr. Mahathir’s more aggressive stance and occasionally provocative statements (Economist Intelligence Unit, 2004 pg. 16).

As a result of the Trade Unions Act of 1959, Malaysian trade unions were prohibited from forming multi-sector unions, a condition that remains in place to this day. The subsequent Industrial Relations Act of 1967 further reduced the ability of trade unions to negotiate for better terms of treatment for participating workers, by forbidding unions from pressing for better working conditions in any sector considered “pioneering.” The definition of which sectors are pioneering is arbitrary, which has weakened the Malaysian labor movement’s collective bargaining power. Worse yet, the Industrial Relations act prohibited proposals for collective bargaining on the following issues: recruitment, retrenchment, dismissal and reinstatement, transfers, promotions, allocation of duties, and strikes over the afore-mentioned items. Finally, once referred to an industrial court or in the aftermath of a court decision, unions lose the right to strike. As a consequence, one act severely reduced labor unions' ability to defend workers on issues such as social security payments, industrial accidents, and similar fundamental issues (Rasiah, 1995).

Table 3, following, provides a summary of the political characteristics of both regimes during the study period.

	Indonesia	Malaysia
Government type	Presidential democracy	Parliamentary democracy
Gov't focus	anti-communism, pro-West.	pro-West, concerned with maintaining ethnic harmony
Gov't characteristics	State-military control and an autocratic leader	Autocracy with a strong executive branch
Gov't functioned by…	co-opting the unions and controling the indigenous elite	providing growth and stifling criticism
State - Labor relations	antagonistic, co-opted	antagonistic; union power mostly eviscerated

Table3: Political Environment Comparison

Aspect 4: Environmental

Indonesia

Indonesia's policy makers paid little attention to conserving the nation's ample natural resources until the 1980s. Through the first two decades post-Independence, islands other than Java were considered largely open for exploitation, a vast untapped resource, and little was done to preserve, control, or manage their exploitation (Hill, 1996 pg. 144). While the family planning program took some pressure off the natural resources, environmental issues were considered secondary to the more fundamental challenges of the New Order economy. Agricultural development proceeded without respect to conservation strategies: forest resources were promoted for export, rice development proceeded with the goal of self-sufficiency regardless of the impacts of excessive fertilizer usage, and the intensified cultivation of upland vegetables led to deteriorated soils and even landslides. Regulations, when issued, were rarely enforced, and at any rate most regulations were complex and fell to ill-equipped staff to be enforced (Hill, 1996 pg. 144).

Not until the 1980s did the need to manage environmental resources more carefully become more apparent, and this happened as a result of the worldwide concern for newly recognized phenomena like global climate warming, and through messages delivered by NGOs and international organizations like the World Bank. Professor Emil Salim, a notably adept minister in the Indonesian government, championed the cause in recognition that environmental and economic policies did not have to be mutually exclusive; this in spite of the limited government resources at his disposal (Hill, 1996 pg. 145).

Export of forest products grew quickly through much of Indonesia's recent economic history as a result of high world prices. By 1970 the value of timber exports was second only to rubber. In 1980 the government instituted a ban on the export of logs and promoted local processing facilities in conjunction with a reforestation program. This led to a decrease in the export of raw lumber and an increase in the export of plywood, which through 1986 comprised about half of the nation's manufactured exports. Nevertheless, inefficient management techniques and high timber wastage has led to deforestation rates of over 850,000 hectares a year (of which agriculture and conversion of land to other activities has contributed as well) (Hill, 1996 pg. 145).

Vegetable production on upland slopes has been responsible for serious erosion problems in ecologically sensitive soils. In some cases, high protection of certain selected crops – notably certain vegetables and sugar – provides an incentive for the abuse of those sensitive lands, but the failure to clearly title land has also produced insecurity for the tenant farmers and acted as a disincentive for careful management as well. Absentee landlords are clearly an exacerbating factor in this process (Hill, 1996 pg. 145-6).

Much of Indonesia's agricultural growth occurred as a result of the so-called Green Revolution that intensified agriculture through chemical inputs. In practice, a policy framework in place since the 1970s has provided high subsidies for pesticide, fertilizer, irrigation, credit, and research and extension services. The Green Revolution has largely concluded however, as scientists predict Indonesia will be unable to repeat the doubling of crop output as it did in the 1970s. Further inhibiting a policy framework like that which sustained the Green Revolution is a fiscal austerity plan in place since the mid-1980s, which has done away with the important fertilizer subsidies. Economic growth in some sectors – primarily light manufacturing, poultry raising, and tourism and recreational services – may take some of the pressure off Indonesia's environment (Hill, 1996 pg. 147).

Malaysia

Malaysia's environment was afforded no higher a priority than was Indonesia's. Vincent and Ali (1997) concluded a study showing that in general the Malaysian government's approach to the use of natural resources with which it had been endowed emphasized maximizing revenue and production in lieu of following principles of strict cost-benefit analysis (quoted in Drabble, 2000 pg. 289) As such, Malaysia's rapid economic growth in both primary and secondary industries in the post-WWII period broadly impacted patterns of land use. Principal among the effects was expansion of cultivated areas and accelerated deforestation via commercial logging and land development, but urbanization, and the development of ports, dams, and highways, also impacted the environment during this period (Drabble, 2000 pg. 287). The Malay government encouraged subsistence farmers to abandon the traditional lifestyle for export agriculture, primarily the cultivation of rubber, and funded large land-use schemes like FELDA (Drabble, 2000 pg. 287), a land-use plan inherited from the colonial government that opened large blocks of virgin land in less-developed areas like the Pahang. Families from overcrowded areas were encouraged to move to these new areas, using enticements of financial assistance, plus housing and planting materials, plus technical advice to promote healthy crops, usually of rubber (Drabble, 2000 pg. 166). The result of such intensified land development was the loss of nearly 15% of primary forest in the Peninsula between 1966 and 1978 (Drabble, 2000 pg. 288).

Land development in East Malaysia followed a similar track but affected both the environment and the living situation of native peoples established there more adversely. Logging and land development schemes in Sarawak caused the loss of nearly 30% of the forest area between 1963 and 1986, and in Sabah commercial forests were reduced by 66% from 1972 to 1985 (Drabble, 2000 pg. 288). Hydroelectric schemes prompted the same: the Batang Ai hydro-electric plan in 1985 flooded 8400 hectares and forced the resettlement of about 3000 Iban; the much larger Bakun dam on the upper Rajang would have flooded 73,000 hectares and displaced over 5000 people had the global economic problems of the mid-1990s not caused the plan to be, for the moment, shelved (Drabble, 2000 pg. 288).

The physical results of opening up so much virgin land for agricultural use were easily apparent on the landscape: deforestation which climbed to the uplands, loss of forest cover, severe losses of topsoil and silting up of rivers, which in turn negatively impacted the flora and fauna. The Malaysian government responded to pressures to think about conservation by creating a number of parks and natural reserves – totaling just over 250,000 hectares in Sarawak by 1985 – and by encouraging eco-tourism to exploit native populations of turtles, orangutans, and so on (Drabble, 2000 pg. 289).

Table 4, following, summarizes the key elements of environmental policy during this time period.

	Indonesia	Malaysia
Land Use	Resource exploitation	Resource exploitation, immediate revenue generation
Environmental Regulations	Few, and rarely enforced	Few
Key Problems Today	deforestation, soil degradation and erosion	deforestation, soil degradation, river siltation

Table4: Environmental Policy Comparison

B. Policies that Link the National and Local Levels

Indonesia

The Indonesian government under Suharto never had a good relationship with NGOs, perceiving them as a threat to the established political elite. James Riker postulated in 1994 that NGOs struggling to increase their voice in the political sphere were being thwarted by a concerted government effort to limit their role (1994). Riker states that NGOs whose primary focus was the environment or development took advantage of their position and voice to gain prominence in the political sphere as well, from where they criticized the Indonesian government for alleged abuses of human rights and calling for political reform. Suharto's administration responded by increasing its efforts to restrict the growing role of NGOs; as a result, tensions rose through the 1990s (Riker, 1994).

While the state-centric patron-client relationship dominated the decision-making process in Indonesia, Andrew Macintyre (1990) points out the relationship is more complicated than that. Rather, business groups with a high stake in the economy were able to challenge the restrictive corporatist state institutions to serve their purposes in lieu of the interests of state strategists and planners (Macintyre, 1990 pg. 246). In several instances, non-state actors – industry groups, specifically – played a part in shaping policy outcomes, and the press played an important role in articulating industry interests. But successful participation in the policy-formation process by industry groups, while notable, represented hard-won gains. In Suharto's Indonesia, the linkages between state and society have taken three principal forms: corporatist institutions, political "osmosis" of a co-optive nature, and patron-client links (Macintyre, 1990 pgs. 246-7).

Declining oil revenues over this time period help explain why Suharto's administration was increasingly inclined to be receptive to the demands of business sectors that provided an increasing share of the nation's revenues. But the government's distrust of the sector as a potential political threat explains why industry groups were forced to step lightly as they presented their demands. Business activists in the late 1980s established an Indonesian Business Council (DPSN) to promote business interests and in response to the co-opting of KADIN, a government institution whose goal was ostensibly the same. DPSN leaders took great pains to make clear the DPSN was not established in opposition to KADIN but rather to complement the agency's capacity, even if it seemed clear at the time the DPSN leaders were hoping the DPSN would gain in prominence and influence quickly (Macintyre, 1990 pg. 255).

Ethnic issues may also have been tenuously responsible for the growing sensitivity to the business class. While in the early years of Suharto's New Order economy, the business sector was overwhelmingly in the hands of the ethnic Chinese, as Indonesians gradually came to take a bigger role in the economy, the Suharto government may have been more willing to pay attention (Macintyre, 1990 pg. 256).

An important feedback mechanism that the Suharto's government provided was the preponderance of local government structures, albeit controlled from the top. But the state-sponsoring of local governments provided linkages both from Jakarta to the local municipalities as well as from the local level to the top, an aspect often overlooked in discussions of the GOLKAR government. Local and provincial governments began to play an increasingly important role in administering national government policy, and in doing so grew more aware of their local resources and needs. Local governments used this platform to press for local attention when necessary, as made clear by the growing stand taken by many of the provinces in discussions, meetings, and even mass media during the '70s, '80s, and beyond. But these powers remained limited in nature as GOLKAR wanted no vociferous opposition to its policies. Many people's assemblies established at local and provincial levels functioned more as a way to comment upon government policy than to actually formulate policy. In this way, the local level was provided a mechanism for voicing its opinion, but ultimately denied the power to participate in any other meaningful way (MacAndrews, 1986 pgs. 1-2, 16).

Malaysia

Malaysia's relationship with NGOs has been antagonistic more often than not over the past 4-5 decades of economic history. NGOs that pressed for meaningful social change first began to appear in the 1960s shortly after independence. The Malaysian government's reaction was initially negative. NGOs passed through four phases as a consequence: establishing their presence, articulating their rights and defending themselves from the state, coming to terms with an overwhelmingly powerful ruling elite, and finally challenging that political power without sacrificing their integrity. At the end of the process, the Malaysian government has come to embrace these NGOs as a valuable contribution to the civil dialogue, realizing there would be no satisfactory manner to crush them, given growing popular support for the NGOs (Muzaffar, 2001 pg. 197). The NGOs primarily focused on peaceful political dissent, heralding the causes of human rights and pro-democratic ideals, which led to growing support for their causes among the international community. This too, led to their growing legitimacy and forced the Malaysian political elite to accept the NGOs against its will (Muzaffar, 2001 pg. 197).

The most vitriolic moment of the relationship between NGOs and the Malaysian government occurred in 1981, when the Malaysian government introduced amendments to the Societies Act, which classified nascent politically-active NGOs as “political societies” and barred civil servants, academics, school teachers, and the like – the very societal class most interested in reforming politics – from participating in them. Writes Chandra Muzaffar, “It was obvious that the real motive behind the classification of cause-oriented NGOs as political societies was not only to emasculate them, but also to tarnish their image” (2001 pg. 190).

Three events significantly strengthened the NGO movement in Malaysia over the second half of the 20th century; formal government policy was not one of them. Rather, the Malaysian government continued to make a concerted effort to prevent NGOs from strengthening their political base and from forming a broad constituency. The first was a mass movement against the amendments to the Societies act that coalesced around ABIM (Angkatan Belia Islam Malaysia – the “Islamic Youth Movement”), at the hands of 34-year old Anwar Ibrahim, who would go on to be deputy Prime Minister (Muzaffar, 2001 pg. 191). Ibrahim ably united 118 NGOs in the concerted campaign to undo what was popularly perceived as an undemocratic law. The movement garnered such widespread support that the Malaysian government was forced to repeal the amendments. The victory for civil society radically increased the exposure of Malaysian society to the NGOs as a viable force for promoting political and social change (Muzaffar, 2001 pg 191).

The second set of events that strengthened the NGO movements was a pair of scandals: the Bank Bumiputera Finance scandal in 1983, which threatened the financial system, and the amendments to the Official Secrets Act of 1986, which exposed the Malaysian government's reluctance to adhere to principles of accountability and transparency. The NGOs failed to promote real change in both cases, but did make clear the ruling elite could not totally ignore the moral position the NGOs were advancing. The third event was an economic recession that lasted from 1985 to 1987 and made clear the importance of grass-roots movements that promoted social justice and human rights. As the middle class felt the growing economic uncertainty as a result of the recession, their support for the NGOs grew in measure. (Muzaffar, 2001 pg. 192).

Nevertheless, the Malaysian ruling elite managed to eviscerate the NGO movements via two strategic blows to their network. In 1982 the Malaysian government co-opted Anwar Ibrahim by taking him into the United Malays National Organization. Anwar's joining the government sharply reduced confidence in the NGO movement as a channel for promoting change, and as a result demoralized many well-educated Malays who would have otherwise joined the NGO movement, looking to change the Malay government. Not coincidentally, Ibrahim's ABIM shrank when Ibrahim left it (Muzaffar, 2001 pg. 192). The 1987 Operasi Lalang had a greater impact still: on the grounds of "threats to national security" the Malaysian government rounded up and detained 118 individuals without trial, many of whom were leaders of local NGOs. The message was clearly that Malaysian NGOs would be targeted for harassment if the causes they championed were a threat to the ruling elite (Muzaffar, 2001 pg. 193).

Post Operasi Lalang, the Malaysian government felt confident enough in its power to accommodate the NGOs in token ways, including funds from the national coffers to support certain limited activities. But the government in no way permitted its grasp on political power to slip. Rather, it revoked the printing licenses of four newspapers that had questioned state policies, and used the already-existing Internal Security and Official Secrets Act, the Sedition Act, the Publications Act, and the Police Act to defend its position. As the economic environment was healthy at the time, the people saw little reason to question the ruling elite (Muzaffar, 2001 pgs. 195-196).

Since the ousting of Anwar Ibrahim from the United Malays National Organization and his subsequent arrest under trumped-up charges of homosexuality, the relationship between NGOs and the government has soured still more, and changed character. As NGOs added their voices to the outcry against Prime Minister Mahathir's administration, their message was taken up by Malays in general, who embraced the NGOs' demands for human rights and social justice in a way they never had before. Mahathir responded harshly, misusing the police, judicial system, media, anti-corruption agency, and other government ministries (Muzaffar, 2001 pg 196). He jailed several dissident leaders, which forced the remaining NGOs to go political. Several heads of NGOs joined opposition parties for the November 1999 election, while other NGOs monitored the elections themselves. Thus has the role between civil society and an autocratic government been mostly antagonistic over the second half of the 20th century (Muzaffar, 2001 pg. 196-197).

It is clear however that, despite the crackdown by Mahathir, Malaysian civil society grew stronger through the 1990s and contributed in no small way to the change of regime. Civil society was responsible for ensuring that voters and parties adopt the same priorities, for vouching for the integrity, credibility, and plausibility of political parties, and for providing discussion forums and media coverage of important issues. While this political pressure was forced to emerge under great duress, and emerged not until the late days of the administration, it's clear the groundswell of support for these movements was a result of years of political repression by the Mahathir regime (Weiss, 2003 pgs. 68-70).

II. Compatibility of policies with each other

A. Import Substitution Industrialization

Both Indonesia and Malaysia pursued policies of import substitution industrialization ("ISI") in an effort to develop their national economies from the role of raw material-exporter to something greater. Import substitution entails erecting a barrier of high tariffs and quotas to retard the importation of certain goods while providing tax incentives for the development of those same industries within national borders. Nations promoting the development of their industries use the "infant industry" argument that posits they have a natural competitive advantage that will become apparent if those industries are protected long enough to ensure their successful entry into the market. But ISI, which formed the backbone of the development strategy of several Latin American nations is now considered to have failed there (Todaro, 1981 pg. 374-5). Argentina, under a program of ISI, saw minimal economic growth until free trade reform opened the economy in the late 1980s. India implemented an ISI policy from the 1950s to the 1970s yet gained only a small gain in per capita income over that period (Krugman and Obstfeld, 2003 pg. 261).

ISI does indeed promote industrialization, but does so at the cost of four undesirable consequences. First, in cases where the industrialization happens at the hands of foreign firms invited to be responsible for the strengthening of national industry, these same firms are the primary beneficiaries of such policy, leaving little benefit to accrue to the nation as a whole. In Indonesia, a corollary to that point was the fact that newly industrialized sectors became largely controlled by the political elite chosen by President Suharto, and in many cases, his own relatives (Todaro, 1981 pg. 375).

Second, because the importation of the heavy capital necessary for the industry is achieved using hefty government subsidies, ISI tends to worsen a developing nation's balance of payments by encouraging high importation of foreign capital goods while allowing international owners to remit profits back overseas (Todaro, 1981 pg. 375). Third, countries intent on importing expensive capital goods from overseas are easily tempted to overvalue their exchange rates to lower the nominal cost of the goods. But the overvalued exchange rate diminishes the nation's ability to export and thus both harms the agricultural export sector and exacerbates the rural-urban income distribution by favoring the urban sector at the expense of self-employed agriculturalists.

Relative to some Latin American nations, Malaysia's currency was only marginally overvalued at 4% in 1965 (Argentina's currency in 1958 was fully 100% overvalued and Chile's in 1960 was 68% overvalued) Finally, Todaro points out that ISI, while intended to promote forward and backward linkages in a developing economy, in reality prevented them, by developing national industries whose products were too expensive to link to or from (Todaro, 1981pg. 375-6).

Krugman and Obstfeld point out that protection of infant industries using high trade barriers and import substitution don't make an industrial sector competitive on their own, particularly if a country lacks a natural comparative advantage in manufacturing. If comparative advantage in manufacturing is the goal then trade policy is not the most appropriate tool to achieve it, and a country should invest in training its workforce and encouraging skill building in areas like management (2003 pg. 263).

Indonesia more than certainly experienced some, if not all of these negative consequences. G.K. Hellener concluded, in sum, that import substitution more often than not leads to an inefficient industrial sector that operates at a capacity lower than would be possible if managed more efficiently, while failing to provide extensive employment opportunities or generate foreign exchange (quoted in Todaro, 1981 pg. 377). Radius Prawiro, reflecting on Indonesia's economic development in the context of ISI concluded, "According to some theorists, in the early stages of development, it may appropriate for countries to embrace inward-looking policies … Through inward-looking policies, Indonesia gained a false sense of security. In the process, economic growth was sacrificed" (Prawiro, 1998 pg. 336).

ISI as a development strategy doesn't lend itself well then to Malaysia's stated development goal of reducing inequality, and may only have avoided aggravated skewing of income distribution because of specific policies that targeted the bumiputera societal class at the expense of the more wealthy ethnic Chinese and other races. At the same time ISI works against both Indonesia's and Malaysia's likely competitive advantage in agriculture, given both nations' relative abundance in land and natural resources. On the other hand, promoting industrialization did successfully lift both countries out of raw-material exporter status, at least until the crash of 1997.

B. Agricultural Expansion and Income Redistribution

The agricultural expansion that occurred during the so-called "Green Revolution" helped alleviate the Ricardian trap of stagnation and inequality caused by food production that lags behind population growth and the subsequent increase in food demand (Hayami, 1997 pgs. 199-202). And population growth in Southeast Asia was high for most of the latter 20th century, putting pressure on more densely settled islands like Java. But the Green Revolution may have exacerbated income inequality by concentrating the capital inputs to technological growth in the hands of relatively few farmers, which gives the advantage to the larger land-holders and causes an overall decrease in welfare for farmers with relatively small holdings and thus little access to the higher technology inputs. A better way to prevent greater inequality is to promote increased demand for labor at a higher rate than the growth of population. In this regard, Indonesia's effort to retard population growth was appropriate because it took the pressure off the land, particularly in Java (Hayami, 1997 pgs. 199-202).

However, intense agricultural production does not coincide well with environmental goals, and less so when a government attempts to open up new lands for production, as did both Indonesia and Malaysia. Yujiro Hayami defines environmental ills as a problem of natural resource exploitation which occurs at a faster rate than the resource can feasibly sustain (Hayami, 1997 pg. 203). Private ownership of natural resources is one factor that can retard resource exploitation, but the lands opened to development in both Indonesia and Malaysia in this time period were either considered vacant, or its current inhabitants were not regarded as legitimate stewards of the land, as also happened in Malaysia (Hayami, 1997 pg. 204-5).

That is not to suggest that development's effects on the environment warrant continued poverty to abate the damage. In fact, environmental destruction is just as frequently the result of poverty itself, which obliges the rural poor to cut forests for timber, farm marginal soils, and rely on resource extraction in lieu of wage work. As such, development is necessary to alleviate environmental pressure on fragile resources. But to the extent that development comes at the cost of polluting industries, the net effect on the environment may be zero or even negative (Hayami, 1997 pg. 207).

The population control program was more amenable to the environment than the government's other initiative, *transmigrasi*, in which the rural poor were transported to homestead virgin lands found on outlying islands. The transmigrasi program erred in fundamental assumptions about the land which was given to the rural poor on these outer islands. In general the soils were poor quality and quickly degraded once denuded by the farmers. These soils were also acid and suffered from aluminum toxicity, which reduced their overall soil fertility after just a few years (Thorbecke and van der Pluijm, 1993 pg. 259).

C. Crony Capitalism

Suharto announced in 1970 that although the market forces would guide Indonesia's economic growth, the captain would keep his hand on the tiller, with these words:

> "The government emphasizes market forces, but will not surrender to the free play of such forces. The government feels that it is responsible for constantly supervising and controlling the factors and circumstances which influence market forces. Whenever distortions within the market harm the general interest, the government feels that, in order to eliminate these imperfections, it is obliged to take direct action to influence the factors that lie behind these forces." (Chalmers and Hadiz, 1997 pg. 55).

The resulting autocratic state led to an economy dominated by client-patron relations, excessive state control of the means of production through political leverage and patronage, and ultimately, economic weakness. Excessive strength of either the government or the business sector infallibly leads to an excess of rent-seeking, which is economically inefficient. Driven by oil revenues, the Suharto government was able to provide economic growth, but restricted political participation and maintained a select group of elites in control of the means of production. The business sector never had the political or economic power to challenge that relationship. Economic growth in this context is unsustainable, as the crisis of 1997 proved. Faced with extreme economic duress, political pressure heightened and Suharto and his regime were overthrown (Kang, 2002 pgs. 187-190).

Crony capitalism is economically inefficient for several reasons. It diminishes the flow of foreign direct investment of course, because with national wealth so tightly controlled by such few actors, few are willing to assume the political risk of competing at such a disadvantage. But the Suharto case provides several excellent examples of why crony capitalism leads to economic inefficiency: Of Suharto's children, none is free from scandal resulting from economic mismanagement of key Indonesian industries. Suharto's son Bambang mismanaged the petroleum industry into an inefficient monster protected only by the expensive tariffs that cost the government millions in the 1990s; Suhartos' other son Tommy won the concession to build a national car, the Timor, in 1996. The Timor was built entirely in South Korea, however, and imported to Indonesia free of the taxes and duties that international firms like Ford were forced to pay. Tommy also mismanaged the lucrative clove industry for years, costing the government $350 million in lost subsidies to the industry when angry farmers burned their harvests in opposition to the clove surplus caused by Tommy's having set the official price too high (Meyer and Moreau, 1998). Fiascoes like the previous only scratch the surface of what happens when industries are awarded on the basis of loyalty rather than merit.

D. Investment in Education and Social Programs

Few points in development economics are as widely accepted as the premise that investment in education leads to high returns and an overall improvement in welfare, particularly when education programs target women. Education plays a key role in reducing long term poverty by increasing the productivity of the work force while enabling workers to therefore raise their incomes. The World Bank writes "…education is both a cause and a consequence of higher income" (The World Bank, 1990 pg. 77). Capital improvements in post-WWII Europe led to dynamic growth because the populace was already educated and trained and was able to make good use of the new equipment. But development in Asia post-independence was not as successful because the populace lacked the necessary human skills to make productive use of the gains in capital. Analysis of this difference led to wide-scale support for education reform (quoted in Sundrum, 1983 pg. 91).

Indonesia, faced with rampant poverty at the beginning of the New Order Economy, believed that investing in social welfare as a whole – health services, education, family planning – was the best way to attack poverty at its roots, and committed its meager resources to that goal. Successive budgets saw expenditures on social infrastructure rise from 10.9% of development resources in 1969/70 to 19.1% in 1983/84 (Prawiro, 1998 pg. 174-175). Suharto even initiated the "Inpres" ("Instruksi Presiden") program to allocate additional government resources to lower levels of rural and local government, specifically to address social infrastructure projects (schools, health clinics). Inpres funds not only encouraged the strengthening of local government and community involvement but often were used to fund labor-intensive programs that helped stabilize rural incomes (Prawiro, 1998 pg. 174-175).

Education is desirable for many reasons, but in essence, investing in human capital is beneficial to the development of a nation's economy because it allows people to be more productive, make use of existing capital, and because education changes people's attitudes and allows them to absorb new technology as it comes along (Sundrum, 1983 pg. 97). Educational policy needs to target goals in the long-run to be effective though, which means the economic return from education isn't immediately apparent. It also means the production of educated humans must occur at a rate parallel to the rate of capital accumulation in the economy as well, to avoid an educated-but-unemployed structural inefficiency. Education poses real fiscal demands on an economy however and may come at the expense of other programs (Sundrum, 1983 pg. 97).

Because investing in social infrastructure may come at the price of investment in industry, it's important to look at why it was so successful in Indonesia. Radius Prawiro draws the following conclusions from Indonesia's social development strategy (1998 pg. 204-211):

- No private sector companies will have interest in social infrastructure; this must be a primarily government intervention.
- It's important to invest in programs with small unit costs and draw on the support of volunteers. This strategy not only saves money but helps the community take ownership in the project.
- The change is often cultural. Sensitivity to culture is necessary, but so is a gentle push to change habits and expectations of the people. In Indonesia, the New Order government successfully changed people's expectations of having 6 children, making the norm now 2 (Prawiro, 1998 pg. 204-211).

E. Foreign Direct Investment

Foreign Direct Investment (FDI) has played a major role in more than one developing country, and in the majority of developed economies as well. Several reasons exist for why a developing nation prefers to invite foreign-owned companies to do business within their territorial borders than simply borrowing the money and building industries themselves. One is human capital, knowledge, and production ability that foreign firms bring with them when they enter a country, all of which the developing nation would have to develop slowly on their own otherwise. The company may be interested in developing its business overseas to take advantage of locally-owned resources or even the local markets, to avoid tariffs, or for similar reasons. The net economic effect is increased welfare for both countries involved, because the investment increases the efficiency in the allocation of resources internationally (Salvatore, 1998 pgs. 372-374).

FDI, while a valuable opportunity in many cases, is not without deleterious side effects, and multinational corporations that engage in cross-border activities are often among the first to be blamed on both sides of the border when things go wrong. Host countries often complain that multinational countries tend to dominate their economies and affect the local society's taste for consumer goods. This is an especially sharp criticism against some high profile Western goods like blue jeans, Coca-Cola, and the like. FDI is criticized equally for permitting multinational corporations to siphon off their savings into research and development facilities back home, maintaining the host nation's dependency and retarding its ability to take advantage of new technologies available to it. Lastly, in nations where the principal engine for economic growth is an extracted resource like wood products or petroleum, multinational corporations are frequently criticized for expatriating profits, employing capital-intensive instead of labor-intensive practices that would have otherwise benefited the host country, and overexploiting the natural resource on which the host nation is dependent (Salvatore, 1998 pgs. 381-2).

As such, while FDI can provide a big impetus for growth, particularly in developing nations lacking good sources of credit or a high rate of savings, but FDI alone can not be relied upon to safely and fairly develop the host-country's economy. Rather, sound policy and good economic planning are necessary to ensure FDI doesn't clash with other policy goals, like employment or natural resource conservation.

F. Population Control Through Family Planning

While it is not easy to attribute specific economic gains to the implementation of population-limiting programs like the one Suharto's New Order government ran in Indonesia, economists believe that by limiting rampant population growth, Indonesia did indeed improve the likelihood that even small economic gains due to improved infrastructure or expansion in the manufacturing sector would translate into real gains for the populace (Jones, 2003 pg. 158). Economists agree, overall, that countries which have been unable to address a high rate of population growth experience slower economic growth, although this relationship depends on several other factors, including the economic policy regime in place at the time and economic distortions due to nepotism and corruption. Gavin Jones (2003 pg. 158) lists the following mechanisms through which controlling fertility and population growth leads to faster economic development:

- reduces the proportion of dependents to producers, leading to greater per capita production, holding productivity constant. This increases individual welfare, which increases productivity.
- Lower dependency *may* lead to greater savings rates.
- The number of school-age children rises more slowly, permitting a better enrollment ratio and better rates of investment in human capital.

- If the labor force grows more slowly the economy can shift to an employment structure in which more people are engaged in the higher-productivity sectors of the economy (Jones, 2003 pg. 158).

The relationship between population and environmental stress is well-known: denser populations lead to increased stress on the natural environment and hastened degradation of resources. While other variables can ameliorate or exacerbate this relationship, including labor productivity and technology, it is likely that population-planning policies have a positive relationship with environmental policy, particularly when it is the goal of the state to reduce dependence on natural resources (Jones, 2003 pg. 158-159).

Indonesia's family-planning program had other effects as well: the program was an important part of Suharto's New Order government and its autocratic attempt to control activity at the village level. By affecting the role of women, the popular perception of what a "normal" family should look like, and similar, the New Order regime contributed to its own entrenchment and solidified its mechanisms of community control in the context of a broader bureaucratic-military regime (Jones, 2003 pgs. 160-161).

III. To what degree did the policies fit known development models?

Neither Indonesia nor Malaysia followed a consistent set of policies during the time studied; nor do their overall programs lend themselves easily to a simple title that would capture the complexity of their political, economic, and social context. Both countries experimented with both import substitution industrialization and export-led development. Both encouraged foreign direct investment when it suited them. Malaysia, in the aftermath of the 1997 financial meltdown, instituted capital controls to limit the outflow of short-term (speculative) capital, with very few consequences. Both countries, while developing essentially open economies dependent on trade and investment, began from a position of relatively high trade barriers, which they dropped over time to take advantage of their strengthening position in international markets.

Both Indonesia and Malaysia tended towards autocracy to channel development into state-chosen enterprises, and used tax incentives and other economic incentives to encourage both national- and foreign investment in those sectors. Indonesia erred on the side of nepotism and crony capitalism, while Malaysia channeled its development efforts toward the bumiputera class, missing out on some of the efficiencies of the open market economy but avoiding a far more damaging socio-economic split between its two principal societal groups, the bumiputeras and the ethnic Chinese. Notably, neither Indonesia nor Malaysia suffered markedly in the international sphere as a result of their governments' respective autocratic tendencies.

Neither Indonesia nor Malaysia can therefore be easily classified. Both nations developed policies that could now be called neo-liberal, but they developed policies that were statist as well. Both were repressive socially when necessary, but both truly sought to better the welfare of their people and provide for economic growth.

It's clear that no nation selects an economic model and decides to implement it (with the possible exception of Josef Stalin, 1917), but rather muddles through the policy implementation policy, developing the rules that guide the energies of its citizens and international partners as the need arises, until the policy environment as a whole has taken shape as a sum of all its parts. Neither Indonesia nor Malaysia set out with a specific policy environment in mind, but rather, made choices as each decision became necessary. Only afterwards do economists and social scientists study and classify nations' economies, providing labels for the characteristics observed in the field.

IV. Which model offers the most hope for development?

Were the world as easy as a specific model we'd have improved the living standards of earth's poorest members long ago. The reality is that each nation's particular resource base, ethnic mix, capital level, context of social tension, geographical constraints, principal trading partners, colonial legacy, and human capital determine how best to manage that particular economy. What works for El Salvador might not work for Bolivia; what leads to growth in Botswana might lead to ruin in Cambodia.

There are however some elements that stand out as lessons learned – and relearned – in the wake of 40+ years struggling to improve the lives of the world's least advantaged. It's clear that good governance is a crucial factor in the development of a nation's economy and human resources. Individuals will respond to clear and fair rules by investing in their own futures; provided the opportunity to educate their children they will do so; provided the right to own their land and the security that land won't be taken from them, individuals will be careful stewards of the natural resources alloted to them and invest carefully in their future. Clearly stated policies help to encourage foreign investment as well.

Development needs strong institutions as much as it needs clear rules. That means a government with the strength and the resources, not to mention the clarity of mind and honesty, to enforce its own policies, a judicial system capable of rendering unbiased opinions, and in which the people both have faith and accept as legitimate. It's clear that incentives are the key driver for individuals and institutions alike to make the 'right' decisions. Profit is one of these incentives, though profit can also be a disincentive – to report your taxes, for example. No human on earth was born without the desire to improve his or her lot in life, though, and this alone is a powerful incentive that promotes growth, provided other economic obstacles don't prohibit it.

Natural resources are a crucial element in the development strategies of most developing nations, but abundant natural resources alone aren't enough to foment economic development – witness Bolivia, rife with minerals and timber but desperately poor. Peace and its ensuing peace dividend are just as important, however. No nation will have the strength, the time, or the will to develop when warfare or civil strife prevent it from investing more in butter than in guns. Nicaragua stagnated during the civil war decade of the 1980s, and much of the Horn of Africa remains underdeveloped as a result of civil strife.

Both a sense of social cohesion and a sense of ownership play important roles in economic development. Nations that suffer from deep internal divides develop more slowly, as do mountainous nations where from one deep valley to the next one's sense of identity remains centered locally and not on the nation as a whole. That concept lends itself to a bigger idea, that the sense of ownership an individual takes in his nation and his future will lead toward development. The government that wants to encourage a sense of ownership among the populace needs to enter in a sort of social compact, in which the people feel represented by their government. This is easiest when strong linkages between the government level and the people are present, which means that governments ought to listen to their people. That means democratic regimes are, on the whole, more apt to foment a good economic climate for development, though not always: some nations are so torn by rival local needs and desires that no government can successfully represent them all. That means a government must find a way to keep the peace and be as representative to all groups as possible.

Strictly economically, there's little doubt that the import substitution model has been tried, and it has failed. Both Indonesia and Malaysia flirted briefly with ISI before dropping it in lieu of export-led growth. Latin America, particularly Argentina under Perón, were no more successful under this model. Exporting, particularly when led by the private sector, leads to the development of human capital and as a consequence, the growing ability of the poor to take advantage of economic opportunities as they come along. This is more true when educational opportunities are provided along with economic ones.

That said, the failure of the statist model in all its attempted forms is not necessarily a win for the free market capitalists. Neo-liberalism has led to astonishing growth in some circumstances, but the the invisible hand of market forces, if left totally unchecked, will fail to provide for minimum human needs, even those many would consider 'fundamental,' like access to health care, or a clean environment. It is ultimately the role of the government to ensure that externalities are dealt with, as marke forces alone won't do so.

Neither neo-liberalism nor communism nor any other named economic model can therefore safely be declared *the* model that will be the most successful. It is ultimately up to each developing nation to determine how to best deal encourage growth, see to the needs of the people – particularly the least advantaged people – and protect natural resources. It is the right and the responsibility of every citizen to hold their government responsible for the role assigned to it. Likewise, it is the right and the responsibility of every citizen to take advantage of the opportunities at their disposal. No government can successfully provide a better lifestyle for people that expect to be handed the means to a higher quality of life; some entrepreneurship is essential. In sum, economic development is a communal effort, as both the Indonesian and Malaysian cases show. No multilateral agency can 'develop' a nation: development comes from within. The creative, thoughtful, and responsible government that establishes a framework in which the creative can prosper will set the stage for growth. From there, it's up to the creative and entrepreneurial spirits that seek to better their condition to take advantage of the opportunity. Development, if there is to be any, will be a joint effort.

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