Striking the Right Balance:

Economic Concentration and Local Government Performance in Indonesia and the Philippines

Christian von Luebke*

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Abstract

The relationship between economic concentration and governance remains controversial. While some studies find that high economic concentration strengthens collective action and reform cooperation, others stress dangers of rent-seeking and state capture. In this paper I argue that effects are neither strictly positive nor negative: they are best described as an inverted-u-shaped relationship, where better governance performance emerges with moderate economic concentration. Decentralization reforms in Indonesia and the Philippines – unprecedented in scope and scale – provide a unique opportunity to test this hypothesis. Subnational case studies and cross-sections, from both countries, indicate that moderately concentrated polities are accompanied by better service and lower corruption. The presence of 'contested oligarchies' – small circles of multi-sectoral interest groups– creates a situation where economic elites are strong enough to influence policymakers and, at the same time, diverse enough to keep each other in check. The results of this paper suggest that contested oligarchies compensate for weakly-developed societal and juridical forces and can become a stepping stone to good governance.

* Shorenstein/DFG Fellow, Asia-Pacific Research Center, Stanford University, email: cvluebke@stanford.edu
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1. Economic Concentration and Governance

The link between economic concentration and governance has long been a subject of interest to social scientists. To what extent does the distribution of economic power affect the quality of government services and practices? The debate remains controversial. While some scholars contend that high economic concentration strengthens collective action and reform cooperation, others see it at the root of state capture and corruption.

The proposition that higher concentration induces better governance features strongly in recent policy reform literatures. Focusing on Russia's political transition in the early 1990s, Kathryn Stoner-Weiss (1997) identifies the distribution of economic assets as a key factor for explaining subnational government outcomes. In essence, she argues that regions with high economic concentration –in terms of labor, assets and productive outcomes– were better able to overcome collective action dilemmas than their counterparts with highly fragmented economies. In regional 'company towns' a handful of enterprises were able to form economic interest groups and engage in a mutually advantageous exchange with the government. Due to close and interdependent relationships between business and government leaders, these concentrated regions provided a favorable environment for reform initiatives and government improvements.

Jeffrey Frieden, in his study on regime transitions in Latin America, reaches a similar conclusion. His basic proposition is that the more actors are clustered around specific sectors, the higher are their incentives for political mobilization (1991:7). In a concentrated economy, Frieden argues, firms are more successful in identifying common interests and lobbying for policy changes. In a fully diversified economy, on the other hand, political mobilization remains compromised by coordination and free-rider problems. A parallel argument is advanced in Robert Bates (1981) study on agricultural policy in Africa. Building on Olson's group theory (1965), Bates highlights that economic concentration – in terms of firm numbers and location – is a key element to understand the political economy of policy making:

> One major factor that influences the ability of groups to organize is the size distribution of their industry. The fewer number of firms and the larger their individual output, then the smaller the incentives to engage in free-riding … The costs of lobbying also vary with the [structure] of the industry. When there are a few centrally located producers, the costs of communicating, negotiating, and coordinating strategies are comparatively low. But when producers are numerous and widely scattered, the costs of organizing are higher (Bates 1981:88).

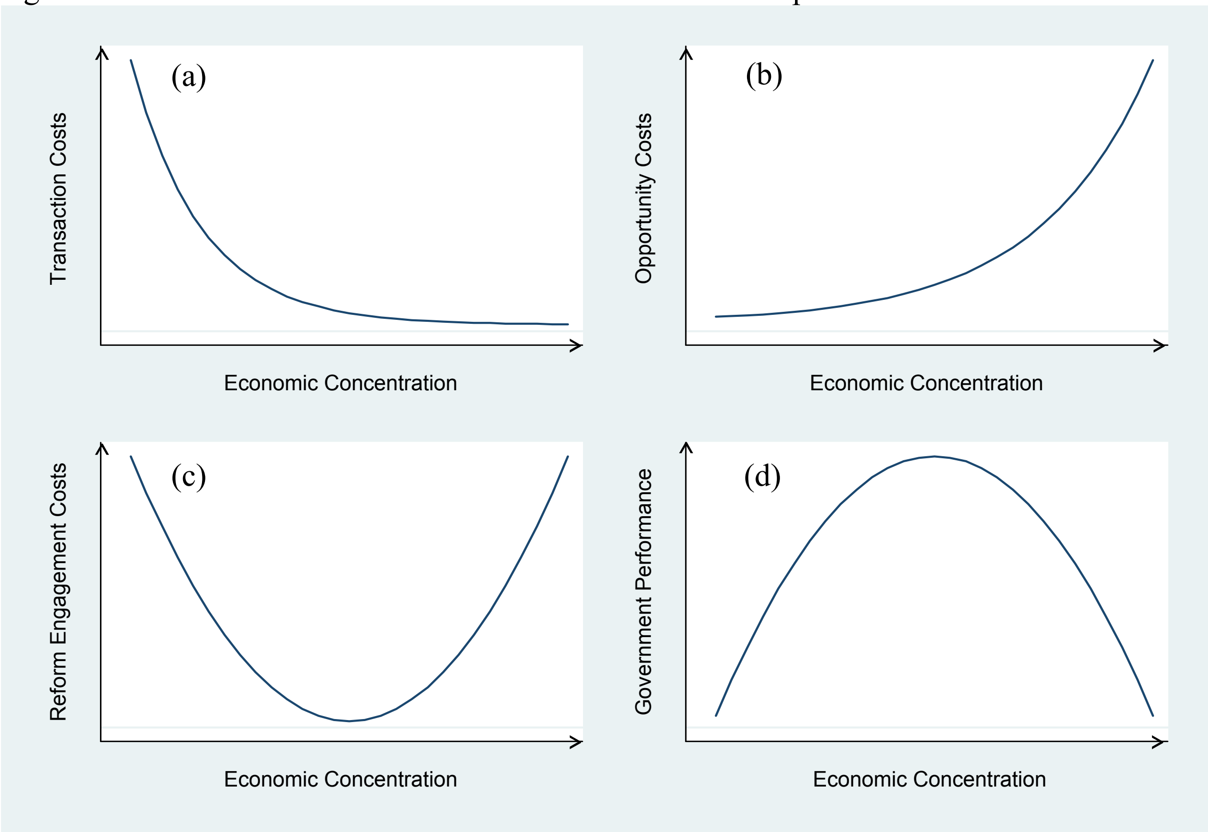
The presence of more concentrated and well-organized groups, however, does not always translate into better governance. Sectoral imbalances, reflected in the emergence of powerful special interest groups, give rise to preferential policies and welfare distortions (Eucken 1950). 'Often a relatively small group of industry will win a tariff, or a tax loophole', Mancur Olson notes, 'at the expense of millions of consumers or taxpayer in spite of the ostensible rule of the majority' (1965:144). The notion that excessive concentrations lead to misallocations of public resources is widely shared in public choice (Bardhan and Mookherjee 2000; Grossman and Helpman 1994) rent-seeking (Krueger 1974; 1990; Srinivasan 1985) and iron-triangle literatures (Huntington 1952; Lowi 1979; McConnell 1966).

Another drawback is that protectionist policies tend to be more persistent in highly concentrated economies. Reform resistance, emerging from disproportionate benefits of protected industries (Haggard and Kaufman 1995; Olson 1982), is likely to rise in regions where 'reform losers' are clustered around specific sectors. Joel Hellman's (1998) account of post-communist transitions serves as an illustrative example in this context. Hellman posits that reform efforts in countries with unbalanced, highly concentrated economies were often undermined by elite opposition. In many cases, powerful groups of firms –which benefited from economic liberalization in the 1990s – were able to capture state resources and resist institutional changes:

> Rising financial-industrial conglomerates … have used their power to block new market entry. New entrepreneurs-cum-mafiosi … have undermined the formation of a viable legal system to support the market economy. In each case the winners from an earlier stage of reform have incentives to block further advances in reform that would correct the very distortions on which their initial gains were based. In effect, they [preserve the] initial flow of rents, [at] a considerable social cost. (Hellman 1998:233)

In combination, existing studies suggest that both extremes – high fragmentation and high concentration – entail considerable governance risks. While the former tends to be compromised by weak business coordination and arbitrary government policies, the latter runs the risk of state capture and exclusive policies. Since problems are more pronounced the closer we move to each extreme, it becomes plausible that better government performance is most likely to arise with moderate levels of economic concentration.

Figure 1: Cost and Incentive Functions of Private Sector Groups



The moderate-concentration argument can be best illustrated by taking a closer look at private-sector incentives (Figure 1). Motivations for engaging in constructive dialogues with the government are primarily shaped by two counterbalancing 'cost functions'. On the one hand, economic actors are inclined to cooperate if they face fewer communication and coordination problems ('transaction costs'). As illustrated in Figure 1a, these transaction costs decline exponentially with rising economic concentration (i.e. decreasing number of actors). [1] On the other hand, economic concentration also affects the susceptibility to rent-seeking and corruption: as firms become more concentrated, they rapidly gain policy influence.[2] As outlined in Figure 1b, rising policy influence, combined with weak law enforcement, translates into rapidly growing 'opportunity costs' for productive reform efforts (and a rising attractiveness of consumptive rent-seeking). If we aggregate these two cost functions, the resulting 'disincentives' for reform cooperation take the shape of a U-shaped curve (Figure

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[1] The implicit assumption that a growing number of actors entail exponential transaction costs can be supported in stochastic terms. In accordance with the binomial coefficient $\binom{n}{k}$, an economy with n actors, which interact bilaterally (k = 2), has $\frac{n!}{2\cdot(n-2)!}$ communication links. If unit costs are constant for each interaction (c > 0), overall transaction costs are given as $t(n) = c \cdot \frac{n!}{2\cdot(n-2)!}$; a function that grows exponentially with n.

[2] If the total amount of 'policy influence' (PI) is equally distributed among n firms, the relative share of influence ($S_{PI} = \frac{PI}{n}$) grows exponentially with economic concentration (i.e. with declining numbers of firms).

1c).[3] According, moderately concentrated settings provide the strongest incentives for economic actors to join reform efforts and scrutinize public officials; which suggests an inverted-u-shaped relationship between economic concentration and government performance (Figure 1d).

From an agency point of view, moderately concentrated economies strike a balance of coherence and control. They create a situation where local interest groups are concentrated enough to be well-coordinated and, at the same time, diverse enough to keep each other in check. Moderate economic concentration is likely to give rise to 'contested oligarchies', a circle of multi-sectoral elites that have strong access to government and, at the same time, stand in competition to each other. The argument bears resemblance with existing 'elite pact' debates (Higley and Gunther 1992; O'Donnell and Schmitter 1986; Weingast 1997), which have provided important insights into the process of democratic transition. By adding a greater emphasis on the composition of relative economic powers, the notion of contested oligarchies offers a new perspective on why elite groups in some regions cooperate more than in others.

2. Research Focus and Methodology

To test the moderate-concentration hypothesis, this study focuses on two transitional democracies in Southeast Asia: Indonesia and the Philippines. After the Asian financial crisis and General Suharto's resignation in 1998, Indonesia put an end to thirty years of authoritarian rule and implemented far-reaching political reforms. Over the last decade, Indonesian citizens were allowed to choose roughly 1,600 national representatives, 30,000 local council members, and 800 governors, mayors, and regents in free and fair elections. In addition, since the implementation of administrative decentralization in 2001, local tax and service responsibilities have been fully devolved to more than 450 city and district governments.[4] These reforms have rapidly transformed Indonesia into one of the most decentralized democracies in the world.

[3] The proposition of non-linear governance effects is inspired by fieldwork observations in Indonesia (von Luebke *et al.* 2009) as well has related political economy studies. MacIntyre (2001), for example, identifies a U-shaped relationship between the number of political veto players and governance risks; Acemoglu and Robinson (2006) propose a non-linear relationship between economic inequality and the likelihood of democratic transition.

[4] The basic stipulations of decentralization are outlined in the Laws UU 22/1999 and 25/1999 and refined (with some revisions) in Laws UU 32/2004 and UU33/2004.

The Philippines is characterized by an equally pronounced regime shift. Under the authoritarian regime of Ferdinand Marcos the country reached its highpoint of centralization in the 1970s and early 1980s; only to swing back to its highpoint of decentralization following the 'people power' revolution in 1986. Since 1991, the Local Government Code has increasingly shifted tax and service delivery to subnational governments and introduced new mechanisms for citizens to participate in local decision making (Capuno 2007). Apart from devolving administrative powers across hundreds of provinces, cities and municipalities, decentralization reforms have widened the political space and enabled local citizens to choose executive officials and councilors in free and competitive elections (Etemadi 2000).

Unsurprisingly, these far-reaching decentralization measures in both countries have been accompanied by a large variation in local policy outcomes. In Indonesia, recent empirical studies show that some local governments have substantively improved public services and administrative practices, whereas others continue to exhibit poor service provision, sustained administrative inefficiencies, and high levels of public corruption (KPPOD 2005; von Luebke 2009; World Bank 2006). Evaluations of the Philippine decentralization program reveal similarly strong differences. In a countrywide assessment of regional economies, Balisacan and Hill (2007) conclude that 'governance quality varies considerably across local governments'. Indeed, while some empirical studies find enhanced citizen participation and government performance (Angeles and Magno 2004; Domingo 2005), others point to the continuation of elitism, bossism and cronyism (Hutchcroft 1994; 2000; Sidel 1999; 2005).

The regime shifts in both countries provide an excellent opportunity to analyze whether moderate concentration coincides with better government performance. By making use of local policy variations in Indonesia and the Philippines, this paper will explore the following hypothesis:

> *Local governments in Indonesia and the Philippines are more service-oriented and less corrupt when they are moderately concentrated across economic sectors and groups. The presence of a small circle of multi-sectoral economic elites paves the way for constructive public-private cooperation and governance improvements.*

Methodologically, this paper applies a nested research design (Lieberman 2005), which combines case study observations with statistical analyses. The case studies focus on two municipal governments: 'Surakarta City' in Indonesia (Section 3) and 'Marikina City' in the

Philippines (Section 4). Apart from similar population and GDP levels[5], both of these cities are characterized by a moderate level of economic concentration (the emergence of multi-sectoral, yet elite-centered, interest groups) and provide important insights into the mechanisms of business-government reforms. In a subsequent step, Section 5 tests the moderate-concentration hypothesis by drawing on income and governance data from 200 Indonesian districts and 15 Philippine regions. Section 6 draws conclusions and discusses implications for policymakers.

3. Case Findings from Surakarta City

The city of Surakarta is the second largest municipality in Central Java. Located in the eastern lowlands of the province, the city extends over an area of 44 square kilometers and hosts 530.000 people. Similar to its neighbor city Yogyakarta, Surakarta has developed around an ancient Javanese sultanate (*keraton kasunanan*), whose historical heritage continues to be a main tourist attraction. While agricultural production is virtually absent, the economy of Surakarta primarily rests on secondary and tertiary sectors.[6] Indeed, in the course of the 20th century, the city has experienced a considerable transformation from traditional to industrial and service-oriented sectors. Although the traditional batik industry continues to define Surakarta's cultural image, well-reflected in colorful batik home-industries that cluster around the sultanate palace, other manufacturing sectors (in particular furniture and garment industries) have become equally or more significant.[7] In 2007, Surakarta's gross domestic product accrued mostly from manufacturing (24.1 percent), retail and tourism services (24.2 percent) and physical construction (13.4 percent).

These statistical figures, however, provide limited information on the composition of economic interests. Field observations yield additional insights. Interviews with local firms and government officials confirm that a small number of business groups are in the position to

[5] According to regional statistics, Surakarta and Marikina are largely comparable in terms of population size (in 2006, 530.000 and 470.000, respectively) and economic development (annual per-capita incomes of 903 and 1072 USD, respectively). Annual per-capita estimates are provided by the Philippine National Statistics Office (2000, current market prices) and the Indonesian Central Statistics Bureau (2003, current market prices).

[6] In 2005, for example, secondary and tertiary sectors contributed 42 and 57 percent to Surakarta's annual GDP, respectively. Further information is accessible at Central Java's statistic bureau: see http://jateng.bps.go.id.

[7] Sectoral GDP figures (BPS 2002) indicate that traditional batik industries contribute roughly 1 percent (300 billion Rupiah) to the local economy in 2002.

influence local policy-making. A survey conducted with 64 local firms[8] identifies eight key associations (see Table 1). Key groups include Surakarta's furniture (*ASMINDO*), tourism (*PHRI*), real estate (*REI*), young entrepreneurs' (*HIPMI),* Chinese-Indonesian entrepreneurs' (*PMS*) and handicraft (*ASEPHI*) associations. They also include umbrella organizations, such as the local chamber of commerce and industry (*KADINDA*) and the public contractors' association (*GAPENSI*), which receive high recall-rates but have lost much of the influence they exerted during the Suharto period.[9]

Table 1: Key Business Associations

Business Organization	*Focus/Membership*	*Recall Rate (percent)*
GAPENSI	Public Construction	64.1
KADINDA	Industry and Commerce	59.4
ASMINDO	Furniture Export	54.7
REI	Real Estate	40.6
PHRI	Tourism, Hotels, Restaurants	34.4
HIPMI	Young Entrepreneurs	32.8
ASEPHI	Handicraft	26.6
PMS	Chinese Entrepreneurs	26.6

Source: Author's business survey with 64 randomly selected small- and medium-sized firms in Surakarta.
Note: Based on the survey question 'please identity key business associations in the economy of Surakarta'. 'Recall Rate' reflects the share of respondents explicitly mentioning a specific business association.

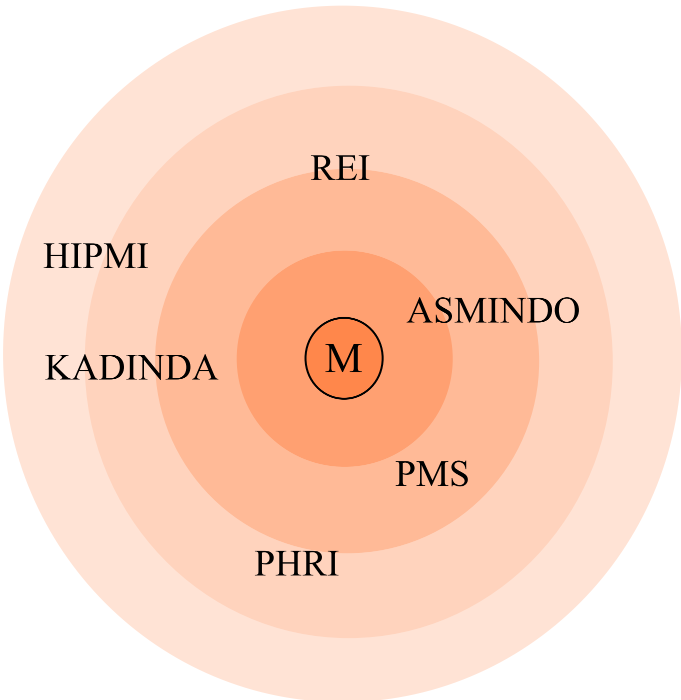
It is important to note that these eight associations represent a diverse set of sectoral and ethnic interests. They represent both capital- and labor-intensive industries and draw members from different manufacturing, trade and service segments. What is more, Surakarta's business groups exhibits a fairly balanced composition of ethnic affiliations. According to our observations, *ASMINDO* and *ASEPHI* consist mainly of Javanese firms, whereas *REI, PHRI* and *PMS* are strongly influenced by Chinese business interests.

The balanced setting of these interest groups, however, should not be mistaken as a high level of fragmentation. There are two clear indications for moderate concentration. First, policy advocacy is limited to small number of economic groups. Numerous other private-sector associations, which fail to reach a critical mass of membership, remain invisible in the local policy arena. Second, the eight key associations represent a smaller clientele than their names suggest. The 'furniture association' *ASMINDO*, for instance, does not operate as a broad-based advocacy forum, but rather as a policy platform for a handful of large furniture

[8] The business survey was conducted in February-March 2008, in the context of a DFID-funded research project on 'Public Action and Private Investment', together with Neil McCulloch and Arianto Patunru.
[9] For a discussion on KADINDA's diminishing membership and policy influence see von Luebke (2009) and von Luebke *et al.* (2009).

exporters. Equally concentrated leadership structures are observable across the other seven associations. In general, associational structures seem to reflect the social norms that underpin them. In this early stage of democratization, Surakarta's society continues to be guided by elite-centric principles. Our interviews highlight two important aspects: First, the access to leading positions in private and government organizations is largely defined by social status, such as a person's individual wealth, family linage, and education. Second, management structures in many business associations continue to be hierarchical and exclusionary. As a result, many of the key economic groups can be characterized as organizational vehicles for elite interests. The persistence of elite-centric norms, combined with a sectorally-balanced distribution of elite powers, paves the ground for what I referred to above as a 'contested oligarchy'.

Figure 2: Constellation of Surakarta's Business Associations



Source: Focus group discussion with 20 business representatives in Surakarta, February 2008.
Note: 'M' signifies the position of the mayor. Focus group participants were asked to position six familiar associations (see Table 1) in the policy arena, according to their relations towards the mayor (visualized by concentric circles) and towards each other (visualized by respective group distances).

The competitive, balanced setting of Surakarta's economic groups is best visualized in a public-private relationship chart (see Figure 2). Based on focus group discussions with local firms – where participants were asked to position familiar business associations in relation (a) to the mayor and (b) to each other – it became obvious that Surakarta's policy arena is overall well-balanced in terms of sectoral and ethnic intersts. Although some groups are slightly closer to the mayor (e.g. *ASMINDO* and *PMS*) than others (e.g. *KADINDA* and *HIPMI*), respondents confirmed that, by and large, sectoral associations face a level playing field on which they compete for policy influence. The diversity of policy interests renders exclusionary policies and state capture less probable. As soon as one group receives illegitimate benefits from the government another equally influential group is likely to intervene.

Our observations and interviews suggest that interactions between business and government are mostly informal. Many of the key associations maintain close, personal ties with senior officials. Instead of attending official forums – such as monthly gatherings at the chamber of commerce – economic elites discuss pressing policy issues in private meetings with Surakarta's mayor. According to one senior businessman, Mayor Jokowi, as he is commonly referred to, 'schedules informal meetings with private-sector representatives every evening … He does not discriminate against groups. He has an open ear for everyone.' This informal exchange mechanism provides business groups with a platform to lobby for government improvements and support.

Many respondents emphasize that this informal, multi-sectoral exchange has notably benefited Surakarta's economic policies. Recent government initiatives have entailed well-balanced stimulation packages for small and large firms. The support measures for two distinctly different sectors – informal street vendors and real estate developers – provide an illustrative example. The 'street vendor relocation program', which the government introduced in 2007, has providing sheltered market spaces and micro credits to over 5000 informal sector businesses.[10] Over a period of two years, the mayor negotiated continuously with Surakarta's street vendors. As one businessman recalls, "Jokowi attended over 70 discussion rounds, seeking consensus for compensation and relocation modalities." Most interviewees concur that the street vendor relocation policy has brought considerable benefits for Surakarta's economy. First, most of the relocated street vendors enjoy more economic security, as they now have access to credit and all-weather facilities. Second, the formalization of thousands of new businesses has generated additional revenues for

[10] Surakarta's informal sector program has been widely covered by the national press (Kompas 2006; Sinombor 2008). Due to his tireless efforts to relocate Surakarta's informal businesses by persuasion rather than force, Mayor Jokowi was selected as one of the top-ten subnational leaders in 2008 (Tempo 2008).

Surakarta's budget.[11] And third, the relocation has made the inner city more accessible for urban restoration and other business sectors.

The street vendor relocation program also paved the ground for real estate developments. As one entrepreneur summarizes it, "the policy sequencing was smart. The government deliberately dealt with the informal and traditional sectors first. Later, when it gave out permissions for real estate developments, resistance in the local community was low … mostly because the support for small firms was widely recognized." This sequential and balanced strategy is reiterated in the development vision of the mayor: "My objective is to develop a modern metropolitan economy that maintains its heritage … it is important to strengthen traditional businesses and markets … At the same time, Surakarta needs to accommodate new investments and urban development." The balanced policies of the government seem to bear fruit: after the successful reallocation of informal firms to traditional markets, three large real estate projects sprang up in the city center in 2008.[12]

The good performance of Surakarta's government is readily observable in recent business surveys. A nationwide assessment, conducted by the Regional Autonomy Watch in 2007 (KPPOD 2008:87), finds that local regulations in Surakarta are more business-friendly (score of 92 out of 100) than other cities in the region, including Yogyakarta (score of 78) and Surabaya (score of 57). This positive evaluation is confirmed in our interview data. There is wide agreement among local firms that Surakarta's government has reduced regulatory burdens over the last five years. A good example is the 2007 revision of the 'urban construction' bill. Based on traditional custom, former regulations (*Perda* 06/1991) stipulated that construction projects were not to exceed the height of the sultanate palace. Since these traditional norms rendered several tourism and property investments unfeasible, the hotel and real estate associations (*PHRI* and *REI*) called upon the government to revise the bill. As one real estate developer recalls , "owing to the mayor's support in revising the outdated bill …and the collaborative efforts of real estate and tourism associations … three property developments are now underway which, eventually, will be higher that the sultanate palace".

[11] The national newspaper Kompas (Sinombor 2008) reports that the *PKL* formalization has raised the official income from traditional markets from 5 to 12 billion Rupiah (700,000 to 1,200,000 US).

[12] The first property is the 'Surakarta Paragon' developed by the Gapura Prima Group and Sunindo Prima; the second is the 'Surakarta Center Point' constructed by PT Duta Mitra Propertindo; and the third is the 'Kusuma Tower' built by PT Kusuma Mulia.

Table 2: Access to License Information and Administrative Ease (in Percent)

	Access to Information	*Administrative Ease*
Very Good	15.6	10.9
Good	43.8	50.0
Poor	26.6	25.0
Very Poor	14.0	14.1

Source: Authors' business survey with 64 randomly selected small- and medium-sized firms in Surakarta.
Note: Based on the survey questions 'please evaluate the access to licensing information' and 'please evaluate the administrative ease to obtain business licenses'.

Another indicator of Surakarta's government performance is given by the rising efficiency of its administrative practices. Responding to repeated business complaints about bureaucratic red tape, the city government streamlined existing licensing procedures into a 'one-stop-shop' (OSS). This reform initiative was animated by common interests: Mayor Jokowi, due to his own business background, understood the problems of the business community well. "After discussing with several business associations", the OSS director noted, "the mayor first sought support in Surakarta's city council and then approached technical departments." A set of penalties and inducements (demotion, promotion) weakened bureaucratic resistance and opened the way for the new OSS service unit. In our interview, the mayor stressed administrative streamlining as a key challenge for economic development: "prior to the establishment of the OSS, business people had to wait several weeks for their permits, which provided ample leeway for corruption … Now citizens can obtain most licenses within a few days". Overall, the introduction of licensing reforms were well-received by the business community. According to the results of our survey (see Table 2) roughly 6 in 10 firms are satisfied with the access to licensing information (59.4 percent) and the ease of administrative licensing procedures (60.9 percent).

In order to put Surakarta's performance into perspective, it is helpful to juxtapose it with other regional yardsticks. In a 10-city comparison (KPPOD 2008), Surakarta exhibits the second best score in 'overall business-friendliness'[13] (Table 3, column 3), the third best result in licensing efficiency (column 1), the the forth best evaluation in administrative corruption (column 2). Apart from these above-average performance scores, Surakarta also stands out for its active private-sector. More than one in three respondents (one of the highest shares across the ten cities) confirmed their membership in a local business association and the existence of an active public-private policy forum (column 4 and 5). Another noteworthy result is

[13] Surakarta's good performance is also confirmed in a recent governance survey, funded by the German Development Agency GTZ. It shows that Surakarta markedly improved its administrative policies and practices between 2005 and 2007 and receives the highest score (8 out of 10) within a 7-district comparison (average score of 5.8). According to the report, the City of Surakarta 'seems to offer the most conducive business climate in the region. Enterprises [perceive] today's and tomorrow's business conditions as excellent, are less bothered by [labor] problems . . . and like to join together in associations'.(GTZ, 2008, p. 94).

Surakarta's good government leadership. Over 70 percent of the respondents recognize the anti-corruption efforts of Mayor Jokowi (column 6), the highest approval within the group.

Table 3: The City of Surakarta in Comparison

City	(1) Processing Days for Trade Licenses	(2) Indication of Illegal Admin. Fees	(3) Business-Friendliness of Government Policies
Surakarta	13	47.1	70.6
Denpasar	26	28.0	40.0
Depok, Jakarta	19	46.0	58.0
Malang	27	58.8	60.8
Kupang	14	44.0	70.0
Makasar	18	50.0	64.0
Manado	11	56.9	82.4
Medan	12	86.0	58.0
Surabaya	34	64.8	59.3
Yogyakarta	15	26.0	68.0
Average	*18.9*	*50.8*	*63.1*

City	(4) Presence of Business Associations	(5) Presence of a Public-Private Forum	(6) Strong Anti-Corruption Efforts of the Mayor
Surakarta	35.3	35.2	72.6
Denpasar	28.0	10.0	66.0
Depok, Jakarta	20.0	24.0	26.0
Malang	21.6	5.9	37.3
Kupang	18.0	14.0	54.0
Makasar	20.0	36.0	62.0
Manado	11.8	29.4	37.3
Medan	10.0	16.0	30.0
Surabaya	31.5	16.7	22.2
Yogyakarta	38.0	40.0	64.0
Average	*23.5*	*22.7*	*47.1*

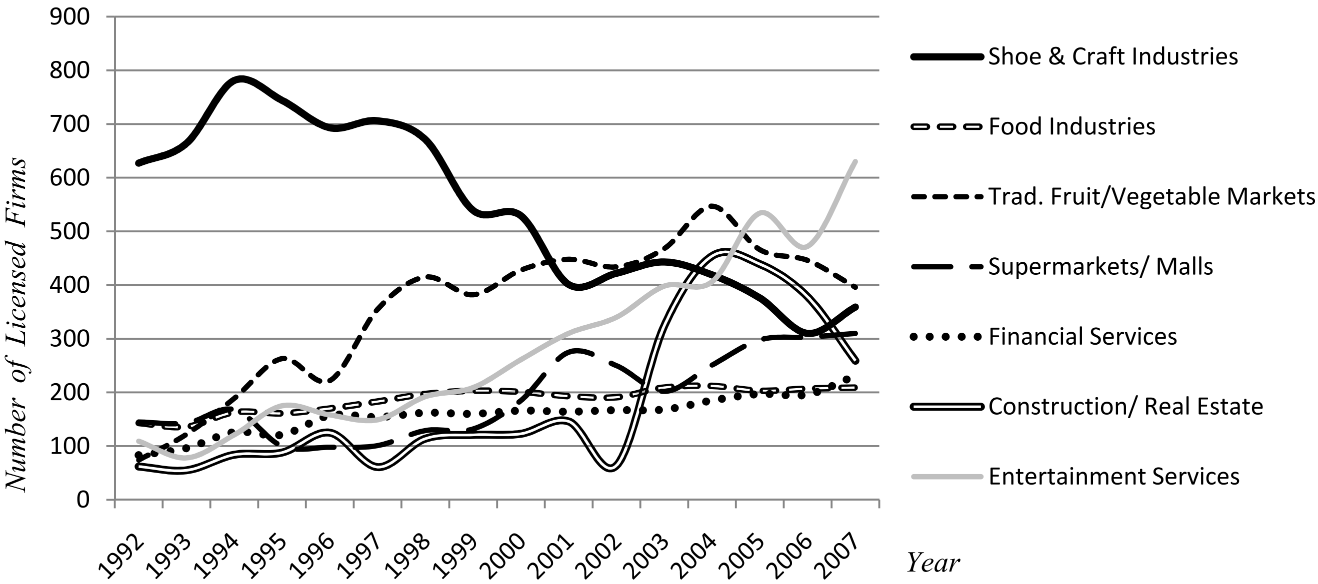
Source: Author's estimates based on raw survey data from the Regional Autonomy Watch (KPPOD 2008).
Note: Column 1 summarizes reported waiting times to obtain standard trade licenses (mean values, in working days); remaining columns denote the share of 50 business respondents in each of the ten cities that confirm the presence of illegal licensing fees (column 2); perceive government policies to have positive business effects (column 3); belong to a business association (column 4); confirm the existence of an active public-private forum (column 5); and report strong anticorruption efforts of the mayor (column 6);

In view of these field observations, Surakarta's case provides tentative support for the moderate-concentration hypothesis. The empirical results confirm that the city's moderately concentrated economy coincides with a high level of government performance. The presence of contending business elites, which have equal access to the government, has provided a platform for constructive policy reforms. On the one hand, the city mayor, a former businessman himself, could gain private-sector support for administrative reforms without running the risk of being captured by one dominant interest group. On the other hand, Surakarta's 'contested oligarchy' kept the mayor on his toes. As a political entrepreneur, Jokowi knew that he needed to strike compromises and implement well-balanced policies, in order to secure funding and support for his re-election. He also knew that favoritism and back-door deals involved great risks, since they could be made public by excluded groups and thereby threaten political career prospects.

4. Case Findings from Marikina City

The city of Marikina is one of seventeen municipalities constituting the national capital region ('Metro Manila'). Located to the northeast of the Philippine capital, the city covers an area of 21 square kilometers and hosts 470.000 people. Similar to Surakarta, Marikina's economy historically developed around traditional handicraft sectors. As indicated by its nickname, "Shoe Capital of the Philippines," the city's shoe industry was, for many years, the backbone of the local economy.

Figure 3: Significance of Selected Economic Sectors in Marikina City, 1992-2007



Source: Author's estimates based on 2009 licensing data from Marikina's Business Permits and Licensing Office.

But with rising trade liberalization and foreign competition, domestic market shares of Marikina's shoe industry have continuously declined since the 1990s. While shoe producers were thriving in the 1970s and 80s, protected by high import tariffs, sales plummeted as the

Philippines opened its market to foreign imports. Nominal tariffs for manufactured goods dropped from 34 percent in 1981 to 5 percent in 2003 (Scott 2005:83). With the abandonment of protectionist measures, cheap imports from other Asian countries (in particular China) penetrated the domestic economy and forced many of Marikina's shoe firms out of business. While the city hosted almost 800 shoe producers in 1994, registration numbers were down to 300 establishments in 2006 (see Figure 3). Within ten years (1993-2003) employment numbers dropped from 105.000 to 42.000 jobs and annual production volumes plummeted from 15 million to 6 million pairs of shoes (Bacalla 2004).

Yet despite its diminishing shoe industry, Marikina's economy has been expanding. The steady decline of traditional handicraft firms has been offset by a substantial rise in other retail and service sectors. Defying its image of a "murky, low-profile town", marginalized by globalization, Marikina developed into one of the most attractive business regions in the Philippines (Ishii *et al.* 2007:336).. According to official business registration statistics[14], Marikina has – over the last fifteen years (1992-2007) – witnessed a two-fold increase in the number of supermarkets; a three-fold rise in the amount of financial services, construction companies and traditional market vendors; and a six-fold increase in entertainment businesses (see Figure 3).

Changes in Marikina's economy are also reflected in associational dynamics. While the footwear association (PFFI) dominated much of the public-private policy dialogue until the mid 1990s, it now competes with other sectoral groups. Among these groups, three stand out in particular: the Public Constructors' Association (PCA), which has gained weight with the development of public and private properties;[15] the local chapter of the Philippine Retailers' association (PRA), which has sprung up in the 1990s with the rehabilitation of public markets;

[14] Unfortunately, the Philippine National Statistics Office does not provide data on provincial or city-level GDP. Income analyses, including sectoral GDP distributions, are only available on the level of 'government regions'. In the absence of GDP figures, we focus on city-level business registration data, which provides a reasonable proxy of the distribution of economic activity.

[15] The rising influence of PCA is well exemplified in the upsurge of construction and realtor firms, particularly between 2003 and 2005 (see Figure 3). Growing firm registration numbers are partly explained by the rapid extension of Marikina's commercial centers; including the construction of 'SM Marikina', one of the largest shopping malls in the Philippines, the enlargement of the Riverside Center, and the construction of the Marikina Convention Center.

and the Marikina Filipino Chinese Chamber (MFCC), which has increasingly shifted its focus from shoe to retail and entertainment industries.

Similar to the Surakarta case, the composition of economic groups is well-balanced in terms of sectoral interests, firm size, and ethnic affiliation. Key economic groups represent small retailers (PRA), medium industries (PFFI), and large enterprises (PCA, MFCC) and comprise interests of the Filipino (PRA, PFFI) as well as the Chinese-Filipino (MFCC) business community. Moreover, our interviews with city officials clearly indicate that each of these key groups has equal access to the city hall. As the head of Marikina's business licensing office explains, 'each Thursday, the mayor invites a wide range of business representatives and listens to complaints and suggestions for improvement … None of the groups has a higher standing in the city hall … the mayor maintains close relations with each of them.'

This sectoral balance notwithstanding, Marikina's policy sphere continues to be characterized by elite-centrism. For one thing, Marikina mayors – Bayani Fernando (1992-2001) and his wife Marides Fernando (2002-2011) – are widely perceived as strong and reform-minded leaders who, especially in Bayani's case, have managed city affairs in a 'top-down' rather than a participatory manner.[16] For another, our interviews show that most private-sector associations continue to be dominated by a relatively small group of key actors.[17] Thus, akin to the Indonesian case, Marikina can be best described as a moderately concentrated economy: a city where a handful of sectorally-diverse economic elites are closely linked to a reform-oriented mayor.

While city policies were initially criticized for being 'corporatist' and 'anti-poor',[18] public opinion turned as Marikina became one of the best performing cities in the country. Since the

[16] According to Philippine Law, mayors can only remain in office for 9 years. After two re-elections in 1995 and 1998, Bayani Fernando was succeeded by his wife Maria Lourdes ('Marides') Carlos-Fernando. Both mayors have received a large number of awards for their leadership in revitalizing Marikina's slum areas, public markets, and health facilities (see www.marikina.gov.ph). Nation-wide recognition notwithstanding, some observers have criticized Bayani's leadership style as authoritarian and non-participatory (Brillantes 2003).

[17] Scott (2005) provides support for the elite-centric character of economic groups by highlighting the steep hierarchies that prevail in Marikina's footwear association (PFFI).

[18] Criticism was further fueled by a national audit report (COA 2002), which indicated that Marikina's government accounting was far from spotless. The report revealed imprecise property declarations and irregularities in the assignment of public contracts for school buildings.

mid 1990s, Bayani and Marides Fernando have launched a wide range of city development programs that helped to boost the city's investment attractiveness. Key reforms included the restoration of public markets, the construction of roads, sidewalks, and bridges, and the establishment of a functional waste management system. Moreover, similar to its counterpart in Surakarta, the city government initiated an extensive resettlement program, which provided informal vendors with sheltered market stalls and squatter families with subsidized public housing. Over time, these reforms attracted increasing media and donor attention. Marikina became a showcase for good government performance: over the last ten years the city has received national governance awards for its 'Squatter Resettlement' (1998), 'Save the Marikina River' (2003), 'Public Discipline' (2003), 'Bicycle Paths' (2005), and 'Central Warehouse Management' (2008) programs.

While in the early 1990s many citizens had 'resigned to a tediously slow and often incompetent bureaucracy' (Del Rosario 1998:2), today's administration is hailed for its responsive and efficient administration. Our interview data suggests that reform initiatives have greatly benefited from a close and continuous exchange between government and business leaders. The public-private dialogue was enhanced by joint study tours to Singapore, Shanghai, and Taiwan, which gradually introduced 'new public management' principles to Marikina's city hall. As one senior official puts it, "discipline, professionalism, and customer-orientation have become the mantra of this administration … we are increasingly run like a private firm … we spoil our citizens by reminding them of deadlines, reducing their paperwork, and delivering their permits."

High standards of administrative efficiency and responsiveness are well-exemplified in recent survey data. The latest subnational 'Doing Business in the Philippines' report of the World Bank (2008) finds that starting a limited liability company in Marikina is less complicated and less time-intensive than in other Philippine cities (see Table 4). While firms in Marikina are required to complete four administrative steps and wait for one week (column 1 and 2), firms in other parts of the country encounter on average seven steps and two weeks of waiting time. In terms of licensing costs, Marikina lies within the average range: roughly 28 percent of national per-capita income (column 3). Similarly good results emerge from the 'Philippine

Cities Competitiveness Ranking Project' (AIM 2005). According to survey results (columns 4 to 6), Marikina exhibits the highest level of service responsiveness (score of 7.2), a moderately good human resource training (score of 6.16), and the best quality of local infrastructure (score of 7.6).

Table 4: The City of Marikina in Comparison

City	(1) License Procedures (administrative steps)	(2) Licensing Time (in days)	(3) Licensing Cost (in percent of PCI)
Marikina	4	7	27.5
Cebu	5	11	23.9
Davao	12	21	20.7
Lapu-Lapu	5	12	17.0
Las Piñas	8	12	44.6
Makati	7	11	37.2
Mandaluyong	7	8	22.8
Mandaue	6	13	21.3
Manila	4	31	32.6
Muntinlupa	7	19	25.4
Pasay	6	14	35.2
Pasig	11	14	27.7
Quezon City	6	16	21.6
Average	6.8	14.5	27.5

City	(4) Service Responsiveness	(5) Human Resource Training	(6) Infrastructure Quality
Marikina	7.15	6.16	7.62
Cebu	5.69	6.41	6.13
Davao	6.02	5.85	7.10
Lapu-Lapu	5.50	6.14	5.23
Las Piñas	6.74	6.43	6.90
Makati	6.03	6.65	7.25
Mandaluyong	6.06	5.53	6.65
Mandaue	5.71	6.58	6.21
Manila	5.59	6.22	6.61
Muntinlupa	6.35	6.32	6.25
Pasay	5.66	5.98	6.40
Pasig	5.78	5.74	6.68
Quezon City	5.65	5.95	6.82
Average	5.99	6.15	6.60

Source: columns (1) to (3): 'Doing Business in the Philippines', World Bank (2008); columns (4) to (6): Philippine Cities Competitiveness Ranking Project, Asian Institute of Management (AIM 2005).
Note: World Bank indicators refer to the procedures for starting a limited liability company; figures are drawn from analyses of official regulations and interviews with lawyers and public officials, for more details see www.doingbusiness.org/MethodologySurveys; licensing procedures and times are *exclusive* of the 11 national procedures (which are assumed to require 21 days on average); AIM figures are based on survey data from 60 randomly selected business respondents in each city; perception values range from 1 (very poor) to 10 (very good).

In view of these governance indicators, Marikina's case provides additional support for the hypothesis that moderately concentrated economies coincide with better government performance. The emergence of a balanced policy arena, in which economic elites from various sectors have equal access to the city hall, has paved the ground for constructive business-government cooperation. In the absence of a dominant group, the mayors of Marikina were able to forge stable reform coalitions. Arguably, the sectoral diversity of business elites also put a check on government behavior. In order to secure sufficient resources for political mobilization, both mayors were required to reach out to a range of business elites by focusing on cross-sectoral programs – such as broad administrative and infrastructural measures. The interdependency between government and private-sector leaders created a conducive environment for reform and enhanced government performance.

5. Cross-Sectional Analysis

After contextualizing the political economy in two city-level cases, this section moves on to a cross-sectional analysis of local government performance. Based on the data of 200 Indonesian districts and 15 Philippine regions, I employ a series of bivariate and multivariate regression analyses to test the moderate-concentration hypothesis. The objective is to triangulate case findings and explore whether statistical estimates substantiate the messages emerging from the field surveys in Surakarta and Marikina.

5.1 Variables and Model

The phenomenon to be explained, the dependent variable, is the quality of subnational governments. For each country, local government performance is approximated by four indictors. In Indonesia, performance measures draw on nation-wide business (KPPOD 2005) and household surveys (PODES 2005); indicators include (1) qualities of district roads, (2) corruption during license procedures; (3) anti-corruption efforts of local mayors[19], (4) and inclusion of private-sector actors in public policy making.[20] In the Philippines, local government quality is captured by making use of four indices reported by the 'Local Government Performance Management Survey' (LGPMS): the qualities of (1) economic development services, (2) administrative procedures, (3) governance transparency, (4) and social services.[21]

The independent variable, the level of economic concentration, is constructed as an index that measures the distribution of local industry-specific incomes. Building on the propositions of

[19] Our sample includes both city (*kota*) and district (*kabupaten*) governments, which are treated as equal units in Indonesia's Decentralization Laws (UU 22/1999 and 25/1999). While the former are governed by city mayors (*walikota*) and the latter by district heads (*bupati*), I continue to use the generic term 'mayor' in this section.

[20] As outlined in Table 6, Indicator (1) is compiled from the 2005 *PODES* Dataset (Indonesian Central Bureau of Statistics), which annually surveys approximately 65.000 villagers in respect to their living conditions (including road conditions). The remaining three indicators (2 to 4) are drawn from the 2005 Business Survey of the Regional Autonomy Watch (KPPOD 2005), which annually surveys 8900 private-sector respondents in more than 200 districts. The survey includes questions on how much 'additional unofficial fees' firms pay for general business permits (*TDP*); how they perceive the efforts of their mayor in curbing local corruption; and how much the local government reaches out to the private sector in its policy making.

[21] LGPMS was initiated by the Department of the Interior and Local Government (DILG). It is based on online surveys of public servants in 107 Philippine cities. Results were submitted by interdepartmental evaluation teams that provided scores for 111 governance indicators, based on secondary data analysis and stakeholder discussions.

Herfindahl (1950) and Hirschman (1945), economic concentration is specified as the sum of squared income shares of local industry sectors:

$$Economic\ Concentration\ Index\ = \sum_{i=1}^{N} s_i^2$$

Where s_i is the GDP share of individual sectors and N is the total number of economic sectors in a jurisdiction.[22] The economic concentration index (EC) ranges from $\frac{1}{N}$ to 1: low values indicating a dispersed, high values a concentrated setting.

Table 5: Descriptive Statistics

Variables	Mean	Stand. Dev	Median	Min	Max	Unit	Source
Indonesian Districts							
Local Road Quality 05†	1.41	0.37	1.33	1	2.59	perception [1-5]	PODES
License Corruption 05†	71,212	150,617	9,875	0	829,250	Rps	KPPOD
Anti-Corruption Efforts 05†	5.26	1.03	5.29	1.87	8.15	perception [1-9]	KPPOD
Private-Sector Inclusion 05†	5.20	1.03	5.18	1.71	8.25	perception [1-9]	KPPOD
Econ. Concentration 04 (EC)*	0.29	0.12	0.25	0.15	0.85	percent	BPS
Population Density 01 (POP)	1.29	2.15	0.60	0.01	12.74	persons/km^2	BPS
Regional Income 01 (GDP)	4,589,598	6,430,979	2,433,818	116,226	53,715,710	million Rupiah	BPS
Poverty Level 01 (POV)	21.44	10.11	20.20	2.26	50.63	percent	BPS
Adult Literacy 02 (LIT)	88.36	8.29	89.12	56.32	99.02	percent	BPS
Philippine Regions							
Econ. Develop. Services 06†	4.08727	0.6363015	4.200893	2.835	5	perception [1-5]	LGPMS
Administrative Quality 06†	3.62	0.50	3.72	2.27	4.44	perception [1-5]	LGPMS
Gov. Transparency 06†	3.65	0.57	3.78	2.20	4.59	perception [1-5]	LGPMS
Social Services 06†	3.78	0.67	3.88	1.72	4.54	perception [1-5]	LGPMS
Econ. Concentration 05 (EC)*	0.39	0.06	0.37	0.34	0.57	percent	NSCB
Population Density 00 (POP)	1,198	3,973	177	70	16,091	persons/km^2	NSCB
Regional Income 05 (GDP)	75,592,089	93,499,449	39,027,332	10,885,684	385,563,464	thousand Pesos	NSCB
Poverty Level 01 (POV)	6.26	3.32	6.45	1.01	13.02	percent	NSCB
Adult Literacy 03 (LIT)	81.69	6.77	81.55	65.90	94.60	percent	NSCB

Note: Dependent variables are marked with a cross (†), independent variables with an asterisk (*); remaining indicators are socio-economic control variables; Indonesian data draw on the 2005 Business Survey of the Regional Autonomy Watch (KPPOD 2005) and various statistical sources of the Indonesia's Central Bureau of Statistics, including PODES (2005) and BPS (2004; 2005); the Philippine variables are compiled from data of the National Statistical Coordination Board (NSCB) and the Local Governance Performance Management System (LGPMS).

[22] The Indonesian Central Bureau of Statistics, for example, distinguishes 9 sectors in its regional GDP figures: agriculture, mining, manufacturing, electricity and natural resources, construction, trade and tourism, transportation, financial services, and other services (BPS 2005).

Since local government performance is unlikely the result from economic concentration alone, regression analyses control for a set of jurisdiction-specific characteristics. To account for differences in economic development, the analysis includes regional income (GDP) and poverty levels (POV).[23] To reflect socio-demographic variations, we add indicators on adult literacy (LIT) and population density (POP). Statistical characteristics and data sources are summarized in Table 5.

To test the u-shaped relationship between government performance and economic concentration (see Figure 1d) in an ordinary least squares (OLS) framework, the independent variable EC appears both in its normal and quadratic form in the equation.[24] The regression model is specified as

$$G = a_1 + b_1 EC + b_2 EC^2 + c_i CV_i + \epsilon ;$$

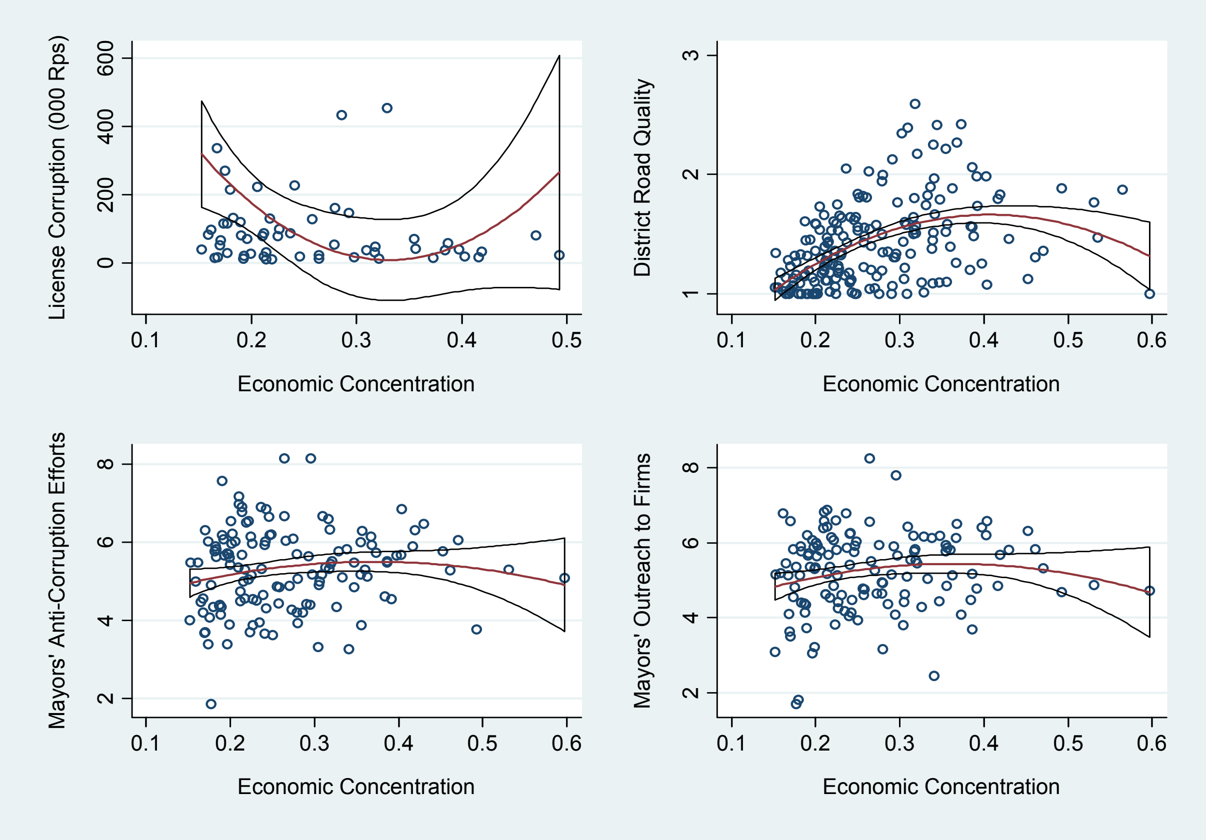
where G denotes government performance, EC economic concentration, CV_i a set of control variables, and ϵ the error term.

5.2 Results

Bivariate scatterplots provide an indication for the non-linear relationship between economic concentration and government performance. As depicted in Figure 4, the performance levels of Indonesian districts describe a curvilinear pattern. As expected, the curves are bent upward (inverted u-shape) for positive governance indicators – such as road quality, anti-corruption efforts, and private-sector inclusion – and bent downward (non-inverted u-shape) for measures on licensing corruption. The most marked convex pattern is observable for district road qualities (top-right graph), which strongly rise and fall with increasing EC-levels. Overall, fitted curves and confidence intervals[25] suggest that moderately-concentrated districts exhibit better services, more private-sector participation, and less corruption.

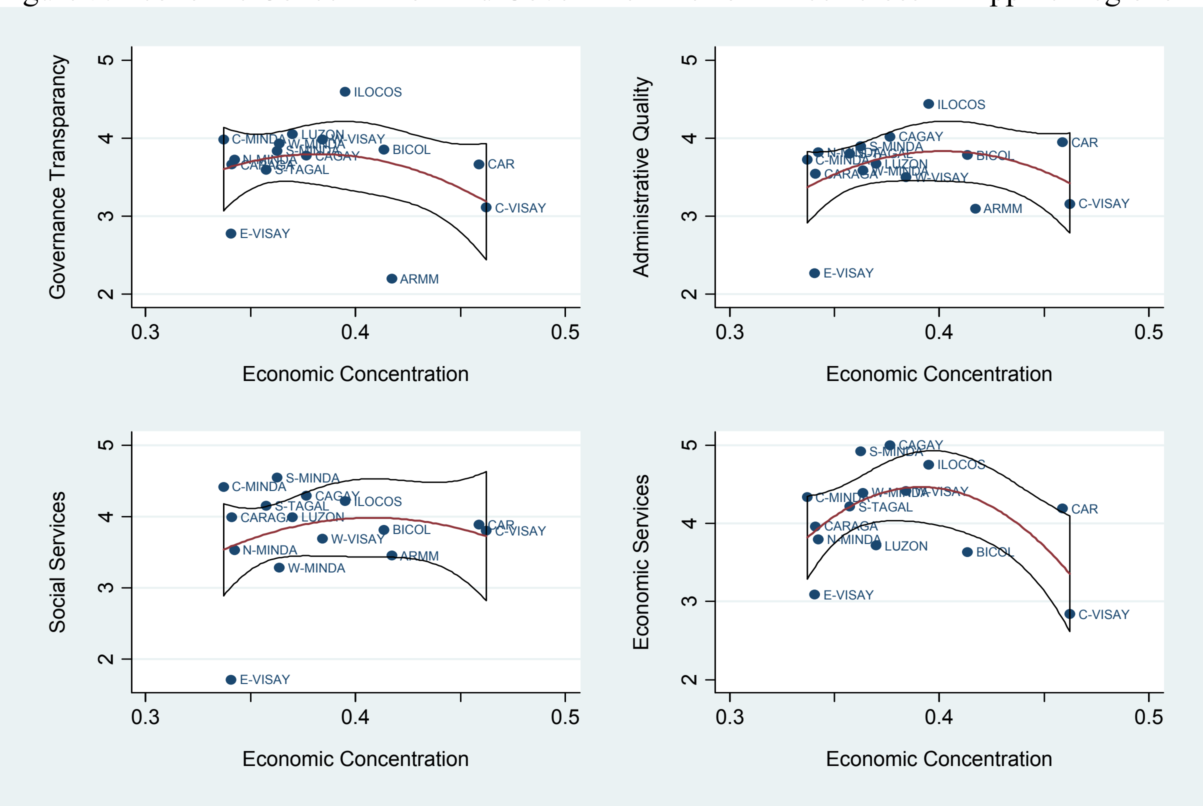
[23] Regional GDP data reflect constant prices (of the year 19985 in the Philippines; of the year 2000 in Indonesia); poverty lines are based on headcounts in Indonesian/Philippine census data.
[24] See Wooldridge (2006:200).
[25] Consistent with the regression equation, prediction curves and 90-percent confidence intervals are calculated in STATA (twoway qfitci) by applying linear regressions of G on EC and EC^2.

Figure 4: Economic Concentration and Government Performance across Indonesian Districts



Source: Variables are explained in Table 5; quadratic prediction curves and 90-percent confidence intervals are fitted to the data in accordance with the regression model.

Figure 5: Economic Concentration and Government Performance across Philippine Regions



Source: Variables are explained in Table 5; quadratic prediction curves and 90-percent confidence intervals are fitted to the data in accordance with the regression model.

A similar picture emerges in the Philippine scatterplots. Plotting the fifteen major Philippine regions with respect to economic concentration and government performance suggests, once again, convex relationships (Figure 5). Given the limited sample size[26], dependent and independent variables exhibit relatively small variations and larger confidence intervals. These limitations notwithstanding, fitted prediction curves continue to rise in the expected hyperbolic pattern: scatterplots across all four governance measures – governance transparency, administrative procedures, social services, and economic services – exhibit inverted U-shapes. The most pronounced of these negative quadratic relationships is observable for the economic service indicator (lower right graph): the convexly upward-bent prediction curve underlines that moderate EC-levels are associated with more effective support measures for small- and large-scale firms.

Table 6: OLS Regression on Indonesian District Data

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
	Road Quality		License Corruption		Anti-Corruption Efforts (of Mayor)		Private-Sector Inclusion	
EC	4.92 (6.12)***	3.57 (4.84)***	-747,59 (3.34)***	-761,08 (3.15)***	7.10 (2.46)**	6.45 (2.10)**	6.10 (2.09)**	4.92 (1.57)
EC^2	-4.59 (4.79)***	-3.04 (3.41)***	1,063,19 (4.02)***	1,108,35 (3.87)***	-9.08 (2.65)***	-7.55 (2.08)**	-7.28 (2.11)**	-5.53 (1.50)
POP		-0.05 (4.01)***		-185.56 (0.04)		-0.01 (0.17)		-0.01 (0.16)
RGDP		-0.00 (1.39)		-0.00 (0.81)		-0.00 (1.74)*		-0.00 (0.81)
POV		0.01 (5.53)***		-210.52 (0.24)		-0.00 (0.29)		0.00 (0.32)
LIT		0.01 (5.00)***		51.13 (0.05)		-0.00 (0.12)		-0.01 (0.57)
Constant	0.46 (3.18)***	-0.78 (2.44)**	157,214.46 (3.90)***	161,813.22 (1.51)	4.12 (7.92)***	4.50 (3.28)***	4.16 (7.93)***	4.98 (3.58)***
Obs.	196	193	132	132	138	138	138	138
R-squared	0.24	0.45	0.14	0.14	0.05	0.08	0.03	0.05

Note: Variables explained in Table 5; t statistics in parentheses, *significant at 10%, **significant at 5%, ***significant at 1%. As the Indonesian cross-section combines three data sources (see Table 5), whose sampling frames differ, observation numbers vary across models: ranging from 132 to 196 districts.

[26] Sectoral GDP data is only available for the 15 major regions in the Philippines. The National Statistics Office does not publish provincial or city-level income data by industrial origin (see footnote 14). The economic concentration index can thus be only constructed on the regional level. For future research it is desirable to calculate an alternative concentration measure by using firm registration data (as in Marikina).

The quadratic relationships are confirmed in simple OLS models that regress EC and EC^2 (without control variables) against government performance indicators. For the Indonesian dataset, the results are summarized in the odd-numbered columns in Table 6. It is noteworthy that all EC^2 coefficients are significant at the 0.01 or 0.05 levels and have the expected signs: indicating negative quadratic relationships (inverse U-shapes) with district road qualities (-4.59), anti-corruption measures (-9.08), and the inclusion of private firms in policy making (-7.28); and a positive quadratic relationship (U-shape) with license corruption (1,063.19). These associations remain largely unchanged, once they are controlled for different levels of population density (POP), regional income (RGDP), poverty (POV) and adult literacy (LIT). Recalculated EC^2 coefficients (even-numbered columns) point in the same direction and remain significant (with the exception of private-sector inclusion, column 8), at the five percent level or more.

Table 7: OLS Regression on Philippine Regional Data

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
	Economic Services		Governance Transparency		Administrative Quality		Social Services	
EC	172.34 (2.09)*	285.08 (4.46)***	139.02 (2.68)**	147.30 (2.68)**	89.42 (1.28)	130.47 (2.19)*	72.18 (0.73)	112.72 (1.05)
EC^2	-220.23 (2.14)*	-356.34 (4.51)***	-174.96 (2.69)**	-185.21 (2.73)**	-111.31 (1.27)	-161.88 (2.18)*	-88.42 (0.71)	-137.60 (1.02)
POP		-0.00 (2.72)**		0.00 (0.61)		-0.00 (0.82)		-0.00 (0.40)
RGDP		0.00 (2.06)*		0.00 (0.64)		0.00 (0.46)		0.00 (0.91)
POV		-0.15 (2.42)**		-0.09 (1.80)		-0.06 (1.06)		-0.10 (0.95)
LIT		-0.04 (1.03)		-0.01 (0.26)		0.04 (1.46)		0.02 (0.32)
Constant	-29.25 (1.80)*	-47.61 (3.98)***	-23.53 (2.29)**	-24.11 (2.35)*	-14.13 (1.02)	-25.34 (2.10)*	-10.75 (0.55)	-19.96 (0.91)
Obs	14	14	14	14	15	15	15	15
R-square	0.33	0.81	0.40	0.69	0.12	0.63	0.05	0.34

Note: Variables explained in Table 5; t statistics in parentheses, *significant at 10%, **significant at 5%, ***significant at 1%.

The OLS estimates in the Philippine dataset exhibit similar results (Table 7). Despite the smaller sample size, three out of four controlled models (columns 2, 4, and 6) confirm a quadratic relationship between economic concentration and government performance. EC^2-coefficients are significant at the 6-percent level or more[27] and, consistent with the moderate-concentration hypothesis, remain negative. As foreshadowed in the scatterplots, this quadratic relationship is particularly strong (t-values of 4.5 and R^2 values of 0.81) in case of economic development services, whereas the association with social services is statistically insignificant.

In sum, the results from the Indonesian and Philippine datasets provide considerable support for the moderate-concentration hypothesis. Most subnational governance indicators have a significant relationship with squared concentration levels. Although the limited time frames and sample sizes of the data do not allow for definitive causal statements, the association of moderate concentration and government performance is nonetheless revealing. This is particularly true for infrastructure qualities, anti-corruption efforts, and economic development measures; and less so for social services. One interpretation, consistent with case findings in Surakarta and Marikina, is that business-government cooperation tends to be more directed towards policies with immediate economic effects (such as road construction and SME promotion) than towards welfare issues (such as health and education). Thus, the data suggest that while elite competition fosters government performance, it also introduces a 'technocratic' development focus.

6. Conclusion

Does the distribution of economic power affect government performance? The answer, emerging from the Indonesian and Philippine decentralization experience, is affirmative. Case studies and cross-sectional regressions indicate a strong link between the concentration of industry-specific groups and the quality of local governance. But in contrast to existing policy reform studies, the present study demonstrates that this link is neither strictly positive nor negative: instead it is best described as an inverted-u-shaped relationship that implies favorable government outcomes in settings with moderate economic concentration.

The presence of a small number of sectorally-balanced interest groups is likely to strike a balance between elite cooperation and competition: creating a situation where key economic

[27] The EC^2 coefficient for administrative quality (t-value of 2.18 , column 6) is significant at the 6 percent level

actors are strong enough to influence policy and, at the same time, diverse enough to keep each other in check. The empirical findings from Surakarta and Marikina suggest that governance outcomes have benefited from the emergences of these contested oligarchies. Many local governments in Indonesia and the Philippines continue to be characterized by low juridical and societal enforcement. In these second best environments, contested oligarchies can serve as a surrogate for weakly-defined legal norms and act as a stepping stone for government improvements.

The notions of ‘moderate concentration’ and ‘contested oligarchies’ have several implications for policy. Today most good governance programs prioritize bottom-up empowerment, assuming that a strengthening of civil society is a sufficient means to improve government performance. The findings from Indonesia and the Philippines, however, suggest a nuanced approach: one that takes account of existing elite groups, without labeling them a-priori as a detriment to good governance. An important message emerging from this study is that less weight should be put on elite disempowerment, and more on elite balance and competition. As exemplified in the cases of Surakarta and Marikina, a balanced distribution of elite powers – which cuts across sectoral and ethnic divides – can facilitate collaborate reform efforts. Thus, in addition to support measures for civil society, good governance programs would benefit from putting more emphasis on elite dialogues, public-private cooperation and economic diversification.

Appendix

Map of Philippine Regions

Map of Indonesian Regions

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