

Promoting Peaceful Development in Aceh

An Informal background paper prepared for the
Preparatory Conference on Peace and Reconstruction in Aceh

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Overview

The prospect of peace provides a unique opportunity for improving life for the people of Aceh. The peace agreement needs to be complemented by a phased development strategy that will allow Aceh to recover from its decades of conflict and to provide its people with broad-based benefits from its many resources. This paper is meant to serve as an input into a more sustained discussion over Aceh's development once the peace agreement has been signed. The analysis is based on a very preliminary analysis of existing economic data supplemented by some recent field reports.

Income poverty in Aceh is severe among those who are directly affected by the conflict, such as widows and internally displaced people. But it is in non-income dimensions of poverty that the largest numbers of the population are affected. For example, because of the conflict there is a large gap between how social services are delivered in urban in comparison with remote areas, where public health and education services are of lower quality due to poor infrastructure and the difficulty of attracting staff. The result is low school attendance and low coverage of public health programs. This is just one of the many ways in which conflict lowers the quality of life and the prospects for development – and which now hopefully can be reversed.

The investment climate in Aceh has greatly deteriorated as a result of the conflict. Transportation costs are high because of illegal fees that need to be paid en route, making it difficult to get goods to the market at a competitive price. Credit is available only for large, established businesses or those with regular incomes. As a result, non-farm (and non-oil) economic activity is concentrated in urban areas. Attention should focus on reducing the cost of trade, improving safety and revamping of the legal system.

The analysis of public finances indicates that government resources will not be the main constraint in Aceh. However, these high endowments, resulting from the share in oil and gas revenues that Aceh receives, are expected to deplete within a decade. Strategic planning on how to use these windfall gains in a way so that they line up with the long-term development goals of Aceh is warranted.

The international community can play a helpful role in supporting peaceful development in Aceh, with support for the peace monitoring mechanism the most immediate priority. In the short run, support can be provided to targeted humanitarian aid and recovery, quick impact programs that show tangible results of peace to the people of Aceh, and establishing monitoring systems to track economic and social developments. In the medium term, donors can help by providing support to the design of a comprehensive development strategy that has broad support from all major stakeholders in Aceh. A credible commitment to such a plan should form the basis of long term donor assistance to Aceh. Donor coordination can then be folded back into the established mechanisms of the CGI.

Recommendations for donor assistance to Aceh

The paper divides the recovery and development process into three main stages. In the short term, development aid should complement the humanitarian program with quick impact programs that provide visible returns on peace. Such programs would include the resumption of basic services through community-based planning and work through non-governmental organizations.

Medium term projects with longer planning horizons should be based on an examination of the quality of service delivery in Aceh as a whole, not just in the conflict areas. Restoring Aceh's formerly vibrant private sector will be a key element of the medium term strategy. This review also suggests that to strengthen and deepen the roots of peace, Aceh can and should pursue the more participatory and inclusive planning models taking root elsewhere in Indonesia. Support could be given to provincial and kabupaten/kota budget expenditure preparation, beginning with a public expenditure review for the 2003 budget.

For the longer term, the critical question is how to place Aceh's public financing onto a sustainable basis. Current projections estimate that Aceh's main natural resources – oil, gas, and forest products – will be seriously depleted within a decade. Consideration should be given to options for investing this current resource windfall so that the province can enjoy a

long-term benefit stream. The province would also benefit from a strengthening of the local tax base.

The volume of donor financing is less important than its quality. Government finances are not the main problems in Aceh. The inability to deliver government services – especially in remote areas – and the absence of a favorable environment for private sector development are. The peace agreement needs to be accompanied by improvements to safety, better governance, and improvements to the quality and coverage of public services in the field to have a lasting effect on development.

It is suggested that in deciding upon support programs, government and donors should focus on the following eight recommendations:

1. Support humanitarian and development programs, giving quick demonstrated returns to peace.

While a review of the details of the humanitarian program is outside the scope of this report, a successful humanitarian and peace monitoring program are essential pre-conditions for follow-on development. An effective humanitarian program will require outside support. To the extent possible, humanitarian aid should build in bridges to the development strategy by promoting public transparency and involvement, by careful targeting, and by building in clear exit strategies or transfers to longer term, sustainable programs. Humanitarian programs also need to be screened for their development impacts; improperly targeted food aid, for example, can have adverse impacts on local farmers. Demobilization programs can help to create new livelihoods to those who have turned to peaceful means of making a living, but care needs to be given to their design so as to avoid perverse incentives. Mechanisms should be introduced to ensure that programming information is shared between the humanitarian and development programs.

2. Unblock existing projects

A number of donor-funded projects – especially in rural areas – are currently stalled or disbursing only slowly, due to the difficulties of supervision. Such investments in health, education, roads, irrigation etc, offer perhaps the best opportunity to get tangible benefits on the ground quickly. The government and

donors should make the unblocking of such projects an immediate priority. In several cases, Ministry of Finance will need to revise annual budget plans quickly so that activities can begin.

3. Expand delivery mechanisms which have proven to be successful in reaching the poor (and phase out those that are not successful)

For the peace process to succeed, it is important that the population living in those areas that were mostly affected by the conflict see tangible benefits of the new situation soon. Getting resources on the ground quickly is therefore an appropriate goal. However the evidence from many post conflict situations is that hastily designed delivery mechanisms often have disappointing, and sometimes negative outcomes. Fortunately there are a number of proven mechanisms already in operation in Aceh to channel resources to communities. For example, this year the Kecamatan Development Program (KDP) will be providing resources to 2700 villages in Aceh to be allocated, implemented and monitored by the communities themselves. It would be wise to use these existing mechanisms rather than create new ones. Relatedly, funding should be increased to NGOs which have a track record of being able to deliver services in an effective manner. Programs which are unsuccessful, or only benefit a small elite, should be phased out.

4. Support the establishment of independent monitoring of social-economic indicators

Independent monitoring of social and economic outcomes in parallel with the monitoring of the peace agreement can play a very valuable role. Credible information of the success of policies and programs will help set development targets, design the appropriate interventions and evaluate success. One element of the system could be a resumption of the national social economic household survey in Aceh. The system should be supplemented by independent monitoring of the investment climate. Costs of business are high in Aceh. Travelers, farmers and businessmen alike often have to pay illegal fees, ranging from ‘protection fees’ to a broad range of permits, licenses, and fines. Civil society monitoring will also contribute to independent information on performance.

5. Use available resources more effectively

There is already good scope for improving the efficiency of resource use in Aceh. Nominal resource allocations to Aceh from the national budget and the subnational autonomy program are the fourth highest in Indonesia, yet individual sectors such as education, health, and others appear to lack adequate resources. Losses come from many sources – late release of funds, non-competitive procurement practices, weak absorptive capacities within agencies, and so on. A credible program solving bottlenecks to the effective use of Aceh existing development resources should be an essential complement to an expanded assistance package.

6. Increase public transparency and accountability

Related to the above, increasing the accountability of public expenditures and aligning them better with the needs of the Acehnese people will improve the quality and effectiveness of public investment. Budgets should be published and accessible at all levels of government – from central, provincial, local government allocations to the resources that are eventually received by those delivering the services in the villages. Greater use of participatory planning, implementation and monitoring mechanisms in government programming can help to increase the ownership and effectiveness of government sponsored programs. Experience shows that in post-conflict situations such measures can play a vital role in building trust and sustaining the peace.

7. Assess the investment climate, and improve it.

Essential to peaceful development will be a strong, efficient private sector. But, at present costs of doing business in Aceh are very high. Conflict has resulted in rent extraction on a large scale. Businessmen have to pay “protection fees” for their business to survive. Travelers have to pay at numerous roadblocks. GAM has no monopoly on these practices. The lack of accountability that the low intensity conflict provided allowed such practices to flourish. Implementing existing laws and beginning to demonstrate that the legal system can work in a professional unbiased manner, will be essential if Aceh is to succeed. An assessment of the investment climate could begin right away, and should involve a careful listening to the concerns of local entrepreneurs as well as large businesses.

8. Save resources for later.

Expanding public spending is only effective to the extent that there is an absorption capacity. Absorption capacity here means that the money is spent effectively, reaches the poor and improves their livelihoods. Our assessment is that the absorption capacity is relatively low at present. It will improve as a result of the peace agreement, but not dramatically. At the same time, Aceh province will retain its high revenue inflows from natural gas, oil, and forest products for less than a decade. Consideration should be given to placing excess government resources into a trust fund. The advantages are twofold. On the one hand it will make government resources available in the future years when oil and gas revenues will not be available; it will also shift spending towards a period when the absorption capacity is likely to have increased. Government and donor support could then concentrate on strengthening the local government’s planning and management capacities.

1. Introduction and Summary

This paper provides an initial assessment of the socio-economic situation in the province of Aceh and its development needs. It compiles survey data from the national bureau of statistics (BPS), administrative data, socio economic surveys undertaken in the past year in Aceh with World Bank, WHO, and Asian Development Bank assistance, and the conclusions of a World Bank mission that visited Banda Aceh in November 2002. It also draws on summaries of development activities supported by the international donor community in Aceh provided as contributions to the Tokyo workshop. It is important to underscore that this is a highly preliminary analysis developed in an environment where information is often scarce and difficult to verify.

The remainder of the paper is divided into four

Section 4 is a preliminary attempt to identify the overall budgetary resource package that is available to restart development in Aceh. The discussion combines an evaluation of available regional and central budgets with on-site interviews with key officials.

Section 5 draws together summary information on current donor aid to Aceh and some possible entry points for future donor support.

2. Poverty, Health, and Education Profile

According to the 1999 Susenas data,¹ and using an aggregated, consumption-based definition of poverty, Aceh is not a poor province. 15 percent of the rural population was categorized as poor, while this was

Table 1 Key poverty indicators

	Poor			Middle			Rich		
	Indonesia	Aceh		Indonesia	Aceh		Indonesia	Aceh	
	Susenas 1999	Susenas 1999	Poverty survey 2002	Susenas 1999	Susenas 1999	Poverty survey 2002	Susenas 1999	Susenas 1999	Poverty survey 2002
years of education [aged 18-65 in 1999, 68-2002 in 2002]	5.1	6.2	7.2	6.6	7.2	9.4	9.9	9.9	10.3
fraction of female headed households (%)	8.3	12.3	12	8.2	9.5	1	11.0	11.7	3
house has earth, wood or bamboo floor (%)	54	52	56	34	35	3	14	22	3
Has access to safe (pipe, pump, bottled, covered well) drinking water	65	50	52	76	66	84	90	79	92
Has electricity (%)	69	53	50	84	70	86	96	88	94

sections. Section 2 provides a poverty, health and profile of the province. Not unexpectedly, poverty studies show that despite the overall wealth of the province, conflict has produced substantial direct and indirect poverty impacts. Impacts on public services in the province also vary substantially.

Section 3 provides a brief assessment of the investment climate in Aceh. The preliminary assessment is based on interviews with business people, including small entrepreneurs and bankers.

the case for 5 percent of the urban population. Aceh is ranked as Indonesia's fourth or fifth richest province, depending on whether one focuses on rural or urban poverty.

Current wage data for unskilled labor indicate that wages are not below the national average. According to data collected by the bureau of statistics, agricultural wages in Aceh increased since 1996,

¹ This was the last year that Susenas was carried out in Aceh.

while they fell nationally. The KDP survey asked for daily wages of ojek (motorcycle taxi) drivers and found that they earn on average 27,000 Rupiah per day in Aceh compared to a national average of 20,000 Rupiah.

However, poverty comprises many other aspects than just consumption, and it is in these areas where Aceh faces the greatest challenges. Table 1 provides descriptive statistics for the poor, middle and rich households. Education strongly correlates with poverty. The poor in the Susenas and Poverty survey have similar housing conditions. About half have earth or wooden floors, access to safe drinking water and access to electricity. Access to safe drinking water and electricity compare unfavorably with the rest of the Indonesian poor.²

Aggregate poverty figures can conceal high poverty incidence both in relatively small geographical areas and in particular socio-cultural groups. Female headed households are significantly poorer than male headed households. Of the 75 female headed households included in the Poverty Survey, 64 were categorized as poor. The incidence of poverty among female-headed households is much higher in Aceh than in Indonesia as a whole. Internally displaced people (IDPs) are another vulnerable group that do not show up in large aggregates. Their poverty status is well documented in three studies.³ IDPs often lack basic services in health and education.

Health

Health services seem to have been spared by the conflicting parties. Both sides have an immediate interest in functioning health services in case of casualties. The main problem in the delivery of health services comes from the inability to serve remote areas. Aceh has no lack of health personnel, but health personnel often refuse to work in rural areas. At the same time, urban areas have an excess of health personnel that are poorly utilized and which

presses on the city budget. The government works with incentive mechanisms, such as high salary offers from the districts, and the policy that specialists who agree to work in NAD will only have to do half of the required service time for newly graduated specialists. This has not been enough to attract staff to serve in high-risk rural areas.

The Poverty Survey shows that 41 percent of the Puskesmas have sufficient staff to provide service, and 44 percent indicate that they have sufficient medicines. The figures drop sharply for auxiliary health centers to 17 percent. Stocks of essential medicines are usually sufficient for about 12 days. Around 25 percent of the Puskesmas indicate that their infrastructure is damaged, 34 percent of the auxiliary health centers indicate that they operate from a damaged building. The KDP survey found low budgets for the Puskesmas compared to the rest of the country. The average budget, including financing from Dinas, JPS-BK and patient fees, equaled 35 million for the 15 Puskesmas which provided complete data. The national average was 76 million.

Morbidity and utilization

Contrary to the rest of the country, the poor in Aceh report being sick more frequently than do the rich (see Table 2 below). It is a common finding that self-reported illness increases as one gets richer. (The poor often can't afford treatment or time off work, and thus tend not to report). The fact that in Aceh the pattern is reversed indicates that the poor may face significantly worse health.

The utilization rates in the poverty survey are higher for all groups, indicating that utilization increased since 1999, as it did elsewhere in Indonesia. Both surveys show that the poor in Aceh more often rely on self-treatment than the rich. The costs of treatment are a major obstacle for the poor. When asked why they did not seek modern treatment, the most common (34 percent) response was that it was too expensive.

² The housing conditions of the middle and rich in the Poverty Survey are substantially better than in the Susenas which probably more reflects the sampling methodology than any changes in the housing conditions.

³ World Food Programme: Report on Livelihood of IDPs in Indonesia. Drafts for Aceh Utara, Aceh Tengah, and Aceh Barat.

	Poor			Middle			Rich		
	Indonesia	Aceh		Indonesia	Aceh		Indonesia	Aceh	
	Susenas 1999	Susenas 1999	Poverty survey 2002	Susenas 1999	Susenas 1999	Poverty survey 2002	Susenas 1999	Susenas 1999	Poverty survey 2002
Percent ill in past month	21.5	22.4	29.2	23.5	21.2	19.9	25.0	19.3	19.2
Percent ill and sought care in past month	8.4	7.2	16.7	10.4	11.2	16.1	12.3	10.9	16.7
Percent ill and that used modern care	8.5	7.6	15.5	10.6	11.4	15.5	12.6	11.0	16.5
Percent ill and that used traditional care	0.4	0.6	1.2	0.4	0.3	0.6	0.4	0.2	0.2
Percent ill and that self-treated	12.8	14.0	5.1	14.5	12.1	1.1	15.3	9.9	0.4

Maternal health care and early childhood development

Village midwives play an important role in providing maternal care. However, the village midwife program is at risk because many will complete their final national contract in January and the local government has not made the resources available to continue this program. In Aceh, the village midwife attends most of the births. The Poverty Survey indicates 51 percent of births are attended by a village midwife. Vaccination rates are low in Aceh compared to the national figures. According to the Poverty Survey, 72 percent of the children under 5 received vaccinations

Table 3 Coverage of selected health services in 2001 in Aceh

Selected Health Services	Coverage
Vaccinations	
Difteri, Pertusis, Tetanus 1	84.2%
Polio 4	68.9%
Measles	71.2%
Hepatitis B 1	66.1%
Difteri tetanus 1 (school children)	36.3%
Tetanus toxoid 2 (school children)	37.1%
1 st ante natal care visit	86.8% (see above)
4 th ante natal care visit	74.2%
Tetanus Toxoid 2 (pregnant women)	61.3%
Other	
Iron tablet distribution	3.1% (very low)
Birth delivery assisted by health personnel	65.5% (see above text)

Source: Provincial health ministry Aceh.

in Aceh in 1999, compared to 83 percent nationally. But the last PIN (National Immunization Day) was considered successful. Coverage was reported to be 102%, owing mostly to a major socialization effort to support PIN, including approaching the GAM.

Administrative data collected by provincial staff show a similar picture. Table 3 shows program coverage for year 2001, based on district reports. Birth delivery assisted by health personnel for example was only 55%. Severe malnutrition among children is 4%, which is higher than average. Prevalent communicable diseases are tuberculosis, malaria, diarrhea, and dengue. Disease control programs are reportedly not running smoothly. Health promotion work is very limited: only Rp. 200 million is available to support this program in 2002. The main health information system, SP2TP, no longer functions, but individual programs still submit their reports to the province.

Education

Enrollment rates in Aceh are not very different from the rest of Indonesia (see Table 4). In 1999, the pattern was virtually identical for primary education, and or junior secondary Aceh scores even higher in terms of net enrollment rates. None of the surveys shows sex biases in education enrollment. The Poverty Survey shows lower enrollment rates for primary, and higher for junior secondary. Junior secondary enrollment increases with wealth according to both surveys.

School attendance is a problem in Aceh. The KDP survey covered 13 primary schools in Aceh and found that 73 percent of the boys registered were actually attending class, the same holds for 71 percent of the girls. The national averages in the school facilities survey were 86 percent for both sexes. The Poverty Survey recorded an attendance rate of 85 percent at the primary level, 86 percent at the junior secondary level and 82 percent at the senior secondary level. This is well below the national average, for comparison, the 2002 national household survey

Table 4: Enrollment in Basic Education

	Poor			Middle			Rich		
	Indonesia	Aceh	Poverty	Indonesia	Aceh	Poverty	Indonesia	Aceh	Poverty
	Susenas 1999	Susenas 1999	survey 2002	Susenas 1999	Susenas 1999	survey 2002	Susenas 1999	Susenas 1999	survey 2002
Boys									
net primary	90	91	87	94	96	79	94	97	67
Gross primary	105	106	110	110	113	92	109	111	79
Net junior secondary	40	46	56	62	62	74	77	82	67
Gross junior secondary	54	59	87	80	74	104	98	94	131
Girls									
net primary	90	94	87	94	93	86	93	97	73
Gross primary	106	105	109	109	111	93	108	108	89
Net junior secondary	42	46	65	63	56	72	76	84	63
Gross junior	54	56	97	80	77	114	97	91	83

shows an attendance rate of 95 to 96 percent at all levels.⁴ Teacher attendance is also lower than the national average. The KDP survey found 78 percent of the permanent teachers present at school at the time of the interview, compared to a national average of 89 percent.

Many schools are damaged but most of them are still functioning. The Poverty Survey found that 46 percent of the primary schools are damaged, but still functioning. 51 percent reported no damages. 64 percent of schools report damaged desks and chairs. On the other hand, all schools reported having a blackboard and 78 percent reported sufficient light in the classroom for reading.

No information is provided here on school budgets as school administrators were highly reluctant to provide financial information. This is consistent with the reality that in conflict situations, financial information can be politically sensitive and thus is difficult to collect, and is also generally reflective of the low level of public transparency in the province. The KDP survey was able to collect budget information only from 21 out of 49 schools, the Poverty Survey only from 75 out of 260 schools.

⁴ Household surveys tend to report higher school attendance rates than facility based surveys.

By way of summary, the main conclusions of this poverty overview are that:

- On average poverty rates in Aceh are below the national average;
- For the groups most directly affected by the conflict, however, poverty rates can be high;
- The quality and coverage of public services in Aceh has been disrupted by the conflict and will require corrective actions to restore it.

3. Improving the Investment Climate

In the long run, private sector growth will be the foundation for Aceh's development and success in meaningful poverty reduction. The oil and gas sector, which is accounted to the mining and manufacturing sector, accounted for 48 percent of Aceh's regional income in 2000. However, this sector is largely of an enclave type, and impacts the economy primarily through channels such as fiscal revenues (see next section). At about Rp.3.7 million per capita in 2000, Aceh's .

Most Acehneese continue to depend on the agricultural sector, especially the poor (see Table 5).

The sector includes plantation crops, estate crops, and forestry, many of which are traded beyond the provinces boundaries.

Businessmen, bankers, and government officials are unanimous in their opinion that the number one requirement for restoring growth in the private sector is peace and security. Without security in the rural areas, farmers in this largely agricultural province

can't work their fields or plantations, and can't get their produce to market. Poor security on the main highways means goods traveling between Medan and Aceh arrive irregularly and at higher cost. When the transportation system can't operate, neither people nor goods can move efficiently, markets don't work, and the economy is paralyzed. Thus the agreement between GAM and the Government must come with improved security in all areas, from the most remote village to the main highways, if the economy is to restart and people are to re-build their livelihoods.

Table 5: Aceh's Economic Structure

Sector	Non poor	Poor	Aceh RGDP (Non-Oil and Gas), 2000
Agriculture	60.28	75.59	57.1
Mining	0.12	0.25	1.1
Industry	5.08	5.92	10.9
Electricity	0.09	0.09	0.3
Building	2.89	2.00	4.3
Trade	15.20	8.12	11.1
Transportation	2.99	2.52	8.8
Finance and Other Services	0.35	0.13	1.2
Community Service	12.99	5.38	5.1
Total	100.00	100.00	100.0

Source: SUSENAS 1999, BPS

Credit is also a key issue in Aceh. While bankers report that conditions have improved somewhat this past year and credit has grown, this appears to be very selective growth. In contrast, the provincial and kabupaten Chambers of Commerce in Aceh describe an environment of stuck credit. Small businessmen who have been burned out can't pay outstanding credit and can't borrow to rebuild. New or revolving credit lines are reportedly impossible to obtain except for the very best, most secure businesses, and as a result many borrowers are not repaying even when they are able since this will represent a loss of working capital.

Box 1: The Impact of Conflict on Transportation in Aceh

Medan is the central point for trade in Aceh, as consumer goods are distributed from there, most commodities are processed there, and all exports transit through Belawan port. Transportation is thus key to all aspects of consumption and production in Aceh, and has been greatly affected by the general conflict and state of insecurity.

- Trucking firms spend an average of 60% of total cargo revenues on formal and informal check posts.
- From Aceh to Medan (608 km), there are 60 official check posts along the East Coast road, and 87 check posts along the West Coast road.
- Passage through each check post involves payments ranging from Rp 50,000 to Rp 2 million, depending on the value of the cargo. Failure to pre-negotiate these amounts means higher fees and added time to negotiate at each check post. Buses and bemos also pay at the check points, but a lower amount.
- Cargo transport costs for the 608 km trip Aceh-Medan are Rp 250/kg, reportedly the highest land transport costs in Indonesia.
- NAD has a public rolling stock estimated at roughly 70,000 vehicles (including trucks, buses, bemos, etc.) although only an estimated 15% of those vehicles are on the road. Many have been burned, but a large number are warehoused both in Aceh province and in North Sumatra, waiting for safer times.
- Many interior areas suffering more persistent conflict are thought not to have any public transportation service available.

Sources: Organda and private sector interviews, February and November, 2002

Traders who continue to operate in the rural areas are almost always self-financed. Businessmen complain that loans are available mainly to civil servants, and are used primarily for consumption. This picture is generally confirmed by banks in the province. One public bank with the largest rural coverage reports 21% growth in credit this year (to date), but the number of borrowers has shrunk by 2%. Similarly, an important commercial bank in the province stated that they are very selective in their lending and tend to focus on recruiting the best of existing businesses.

When the private sector was asked during recent interviews what kind of assistance would be most effective for Aceh, their were remarkably thoughtful and generally consistent in their answers:

- Provide infrastructure and security so the private sector can operate efficiently
- Re-establish a functioning legal system
- Monitor illegal rent-extractions that may not immediately disappear with the ceasefire
- De-politicize aid, and deliver it directly to the people
- Focus on technical assistance.

Box 2: Farmers Need Markets

The departure during recent years of firms processing Aceh's agricultural produce have taken a heavy toll on farm incomes. In one area of Aceh Utara, palm oil smallholders have only one firm (a state-owned PTP) to sell to, and receive Rp 100/kg. In another area of Aceh Timor, farmers have four processing firms to choose from and receive Rp 400/kg.

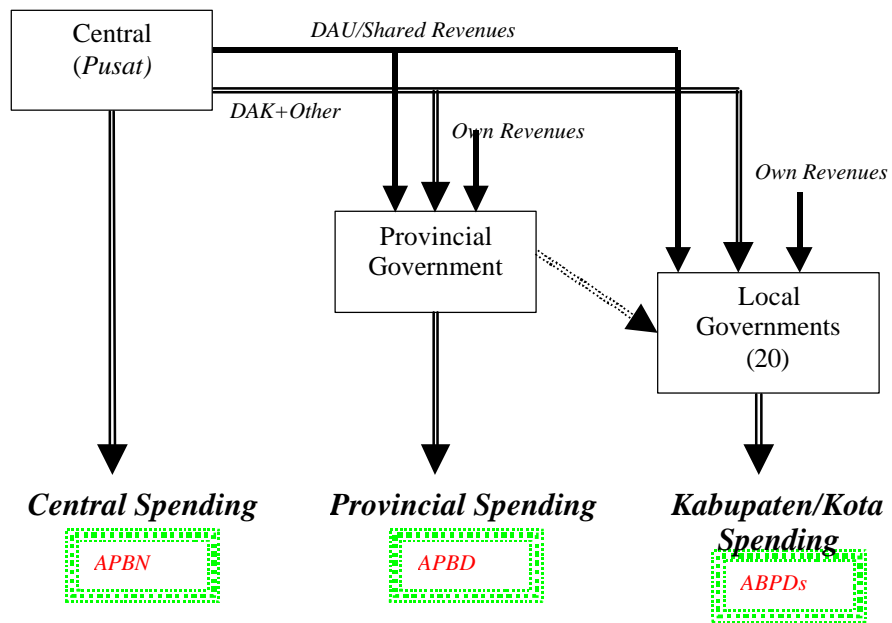
4. Public Resources and Spending in Aceh

To better appreciate current public spending patterns and possible resource needs in Aceh, one needs to focus on the central government, the provincial government, and the province's now 20 local governments – *kabupaten and kota* – jointly, including resources provided by donors/multilaterals.

Such a consolidated picture incorporates three major public spending – as associated resource -- flows to Aceh: (a) expenditures by the provincial and local governments through the regional budgets (the APBDs), (b) expenditures by the national government (the APBN, and its routine “DIKs” and development “DIPs”, donor projects often playing an important part in the latter), and (c) donor/multilateral funding that does not flow through enter into the government budget.

Figure 1, shown on the next page, illustrates the major revenue flows and ultimate spending by center and regional governments. Regional governments in Indonesia rely primarily on central transfers (World Bank 2002a;b). These include the general block grant (DAU), shared taxes (STX), and natural resource revenues (SDA). Other transfers such as the earmarked grant (DAK) for reforestation, infrastructure, education and health remain small. Own revenues (PAD), for example taxes of restaurants and hotels, tend to be quite limited.

Figure 1: Principal Fiscal Flows in Aceh (Center, Provinces, and Local Governments)



Legend:
 General Flows: Block Grant (DAU), Shared Revenues (SDA/STX)

**Figure 2: Consolidated Public Resources at Provincial Level
(Province, LG, Central Development)**

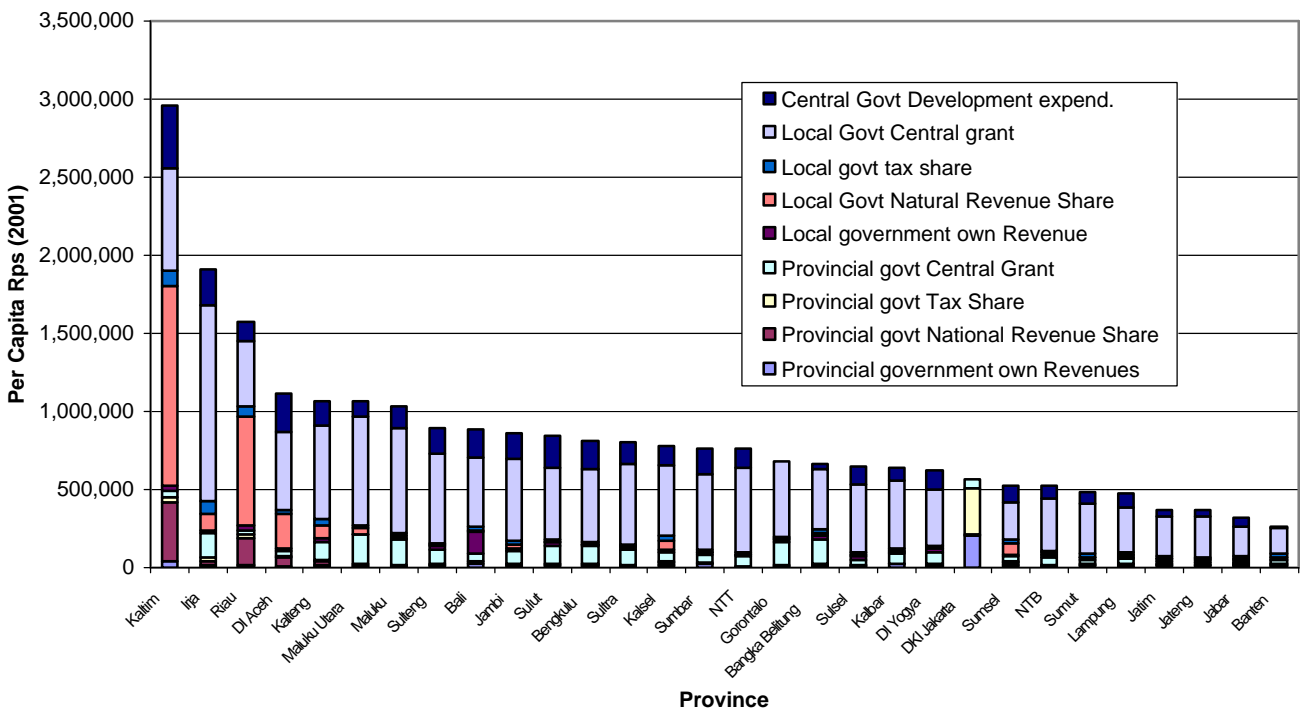


Figure 2 adds up these various revenue components for Aceh, and compares that sum to Indonesia’s 29 other provinces. In 2001, at least Rps 4.4 trillion (USD 490 million), or Rp. 1.1 million per capita (USD 123), appears to have been available in Aceh for the provision of public services and investments through the regional budgets and that part of the central development budget we can attribute directly to the province.⁵

According to this consolidated picture, Aceh trailed only East Kalimantan, Papua, and Riau, three other natural resource rich provinces, in terms of available funding per capita. This would suggest that public spending was already 2-3 times higher on a per capita basis than in many other provinces, although this higher figure clearly does not say much about the actual spending needs or efficiency. Special autonomy approved in 2001 has brought Aceh

additional resources, especially at the provincial level.⁶

⁶ Starting in 2002, Law 18/2001 (9th August) provides for Aceh’s Special Autonomy and higher revenue sharing. Aceh’s Special Autonomy Law gives it 55% of petroleum and 40% gas natural-resource taxes (rather than the standard Government Regulation 104/2000 (Article 12) of 15 % petroleum and 30% of gas). Law 18/2001 (Article 4.5) states that that this arrangement will be re-evaluated after eight years, i.e., in 2009. In addition, the Special Autonomy law stipulates that 30% of the transfers from the central government must be set aside for development expenditures in education.

⁵ These estimates do not reflect any possible withholding.

Table 6: Provincial (APBD) Budgets for FY 2002

(Rupiah, and percent where indicated)

	Per Capita Revenue	Share Own Revs %	Share SDA %
Nanggroe Aceh Darussalam Province	716,651	4.4	81
National Average	189,122	28.8	10.3

Regional Budgets (APBD)

Aceh is a strong beneficiary of natural resource revenue sharing (SDA), which accounted for 81 percent of its revenues. This means that on a per capita level, Aceh planned to spend far more than most other provinces in Indonesia in 2002 (see Table 6).

The local (district) governments on average spent per capita levels that were more comparable to that of local governments in the rest of Indonesia, and combined spent about as much as the province (see Table 7). However, the data suggests big differences across the 15 local governments in existence in 2002. While many greatly exceeded the national per capita average, others were quite close to this average.

The province, moreover, enjoys more discretion in its budgets due to a lower share of wages to total revenues (38 versus 72 percent for the average local government). The province is allocated its extra resources across local government jurisdictions according to the implementation regulation (Kanun) passed by the Aceh DPR.

Comprehensive central, provincial, and local government budgets for 2003 are not yet available. The finalized 2003 central allocation figures suggest that Aceh will receive Rp 2.3 trillion (est. USD 260.3 million) in block grants transfers (DAU) in 2003, plus USD 33 million in other transfers.⁷ With 7 percent of the national allocation of Rp 2.269 trillion, Aceh

⁷ These include USD 18 million in the newly introduced DAK for infrastructure, health, and education, largely for facilities rehabilitation.

Table 7: Local Government (APBD) Budgets for FY 2002

	Per Capita Revenue	Share PAD %	Share SDA %
Kab. Aceh Barat	638,997	1.74	22.41
Kab. Aceh Besar	777,360	1.78	19.89
Kab. Aceh Selatan	792,648	1.73	27.79
Kab. Aceh Singkil	-	-	-
Kab. Aceh Tengah	820,891	2.33	11.38
Kab. Aceh Tenggara	-	-	-
Kab. Aceh Timur	-	-	-
Kab. Aceh Utara	1,292,791	0.71	33.23
Kab. Bireuen	-	-	-
Kab. Pidie	628,663	1.25	16.57
Kab. Simeuleu	-	-	-
Kota Banda Aceh	884,974	2.87	18.78
Kota Sabang (2001 data)	4,876,106	1.34	22.85
Kota Langsa	609,855	2.32	13.10
Kota Loksumawe	-	-	-
National LG Average	657,285	5.98	5.07

has already received relatively generous DAK allocations from the national government's budget program. The additional funds mandated in the 30% education set aside under Special Autonomy means that ample funds will be available to rehabilitate schools damaged through conflict or general depreciation.⁸

Actual data for the natural resource transfers for 2003 are not yet available, but revenue transfers – mostly from gas – amounted to an estimated 2.2 trillion (USD 241 million) in 2002. Assuming that natural resource revenues will stay at least the same next year, this suggests that at least 535.5 million USD (about 133 USD per capita will be available through the regional budgets in Aceh next year, not including other own source revenues (see Table 8).

New to 2003 is also the creation of five new local governments, increasing the number from 15 to 20 (see Annex 2: nationally the total number of local governments went from 348 to 370). This expansion will also require resources to establish the new local governments that have been split from existing units. Further work will also be needed to determine the capacity and operating cost of this increased number of local governments.

⁸ Much of Aceh's basic school infrastructure was built in the 1970s under the Inpres, has reached the end of its lifespan and needs to be replaced.

Table 6. Projected Regional Government Revenues

	Local Governments	Provincial Government	Total
	(millions USD)	(millions USD)	(millions USD)
DAU 2003	241.1	19.2	260.3
DAK/Other Special Transfers 2003	32.6	1.4	33.9
Revenue Sharing (SDA/STX 2002)	134.8	106.3	241.1
TOTAL TRANSFERS	408.5	126.8	535.3

Source: Ministry of Finance, see also Annex 2

Natural resource transfers (SDA) are potential a much needed boon for Aceh's development prospects. But these flows will likely not last forever. Taking the provinces – which draws heavily on natural revenue sharing – and local governments together in Aceh, about one third of overall revenues were derived from natural resource transfers (SDA) in 2001. Aceh's natural resource sharing revenues are anticipated to decline markedly in five years as oil and gas production declines. Although SDA revenue streams are anticipated to decline, these will not completely disappear in the next ten years. By volume, production levels may drop by more than half in the next decade (Mann, Arthur J. 2001b).⁹ This would impact primarily the province. Assuming that Aceh did lose this one third of decentralization/special autonomy SDA revenues, this would at present still place Aceh's overall per capita provincial resource availability in 12th place nationally (see Figure 2).

Central Expenditures (APBN)

Nationally, the central government continues to spend more than the regions for development, even in such areas such as education, health, and infrastructure. The 2002 development budget projected spending 53.3 trillion on development across the whole country. The central government's development budget distinguishes between own source (*rupiah murni*) and donor funded expenditures. Just under half has historically been donor funded.

⁹ Until April 2000, six LNG trains operated in Aceh. From the four remaining trains, two are anticipated to close between 2005-2007, with only one train remaining in operation from 2008-2014.

In 2001, we could attribute about Rp 0.97 trillion (est. USD 107 million) of direct central government expenditure realization to Aceh (WBOJ 2002). If we assume that the center spent its development expenditures proportional to population (i.e., for Aceh's 4 million relative to the national population), we would expect Aceh to have received 1.03 trillion in 2002. Given the priority that is often given to Aceh in government documents, we would have expected the proportional allocations to be higher (Government of Indonesia 2002) rather than lower. Further work will be needed to highlight the actual levels of resources the center is allocating to Aceh.

While allocations for Aceh may be high, realized expenditures have typically lagged behind planned allocations in past years, and tend to be highly compressed in the latter part of the year -- even in comparison with other areas of the country. By October 15, 2002, only 46 percent of overall national central development allocations had been realized. The government was still projecting realizing Rp. 47.5 trillion (90.1 %). Local government expenditures have been even more problematic, with reportedly less than 30% of the APBD having been disbursed by the fourth week of November 2002. Anecdotal evidence suggests that the problem of realized expenditures may be especially chronic in Aceh, especially for donor funded activities (Mann, Arthur J. 2001a). Whereas this is an overall problem for development spending in Aceh, in the current circumstance it may also be an opportunity. The emphasis in 2003 – where initial budget plans are for Rp 54.5 trillion -- may therefore not have to be in increasing budgetary allocations for Aceh, but ensuring that those allocations are actually implemented effectively.

In sum, two key points can be drawn from this picture.

- Overall resource availability is not a key constraint to Aceh's development.
- Efforts to improve the effectiveness of resource use can have high returns.

5. Ways in which donors can help

The most direct and immediate need for support is for the peace monitoring mechanism, under the

management of the HDC. Existing support from Norway, the US and Sweden will need to be supplemented by additional grant funding from donors and government.

In the short run, development aid should also focus on humanitarian relief, quick impact programs which provide tangible benefits, and assistance with monitoring. In order to move quickly, wherever possible assistance should be through existing projects which have a proven track record to deliver, either by scaling up activities already taking place in Aceh or else adapting similar programs in neighboring provinces to encompass Aceh. Implementation can be through by government, NGOs and/or donor organizations. A number of such programs are already underway. For example, UNDP's Community Recovery Program (CRP) has disbursed 4.2 million since 1998. USAID's Office of Transition Initiatives has spent 3.5 million in Aceh since October 2000.

Humanitarian relief efforts should first target the most vulnerable. These include internally displaced people (IDP), widows, and communities who were in the immediate conflict zones. Several donors are already working with NGOs that are active in this field. For instance, Norway provides support to an international NGO, CARDI (Consortium for Assistance to Refugees and the Displaced in Indonesia), for activities, which seek to improve the capacity of vulnerable households to generate income, which in turn will ensure their future livelihood. In 2001 this contribution amounted to USD 270,000. The PEKKA program for female-headed households in conflict areas is funded primarily through the Japanese Social Development Fund but also with support from DFID and the World Bank. PEKKA works primarily with widows. The program uses a facilitated planning process to help widows invest micro-finance in productive activities and to address basic needs such as food and schooling.

Community development programs are an appropriate tool for delivering tangible peace benefits to a large number of communities in the short run. Two programs are operating successfully in Aceh. In addition to the Community Recovery Program (see above), the government's Kecamatan Development Project, financed out of a World Bank and the

ABPD, has the potential to be scaled up quickly (see box 3).

Socioeconomic monitoring should also be supported. Important here will be restarting the national household survey. In the short run some donor support may be required to cover startup costs. There is little experience with monitoring the business climate but it is also of immediate need.

Donors can also assist by restarting sectoral projects with a longer planning horizons aimed at improving the quality of service delivery in Aceh as a whole. Several large investment projects have been negotiated and could be restarted or implemented more rapidly once the peace agreement takes effect. The Asian Development Bank, the Japan Bank for International Cooperation, and the World Bank already have large projects (in health, education, infrastructure and communications) that can be expected to be accelerated. Nearly all have been delayed or suspended because of security and related administrative problems.

Box 3: The Kecamatan Development Project in Aceh

Kecamatan Development Project is a national program to provide direct financing in support of community generated development plans. Funds can be used as grants for village infrastructure, or as loans for income generating ventures. Trained technical and social facilitators support the community planning process. NGOs and journalists provide independent monitoring. Villages compete with one another for project funds in kecamatan (subdistrict) forums, but there is no further review or top down guidance once villagers agree on which proposals get supported. The program includes a matching grant mechanism that allows kabupaten (districts) to increase their KDP allocation if they provide the village block grant (80% of the costs) in exchange for the KDP facilitators, external monitors, and rule book (20%).

KDP already exists in 8 of Aceh's 15 (now 20) kabupaten, including most of the conflict areas. For 2003, KDP will provide almost \$10 million to cover 2,000 Acehese villages through the main grant and 700 villages through the local government matching grant mechanism. Adapting KDP to the post-conflict environment in Aceh could take place by expanding the number of villages covered, or by increasing the size of the grants given to each subdistrict for allocation.

In the medium term, donors can assist in developing a comprehensive development strategy for Aceh. One element of this could be support for the provincial and kabupaten budget expenditure preparation, beginning with a public expenditure review for the 2003 budget. Also ways in which accountability, participation and transparency in government spending decisions can be increased should be considered. A review of public service delivery and a strategy of how they can be improved, especially in remote areas, is highly needed. So is a strategy for improvements in the legal system. Another critical question is how to place Aceh's public financing onto

a sustainable basis.

In the long run, this new strategy should form the basis for any for new donor assistance. Future assistance to Aceh can be coordinated through the regular donor coordination mechanisms established as part of the CGI meetings.

Box 4: The Sumatra Urban Development Project

Supported through an ADB loan for \$122 million, the project is a good example of a currently suspended project that can quickly start up again once the peace agreement takes effect. Covering seven kabupaten in Aceh with a value of \$8-10 million, the project provides infrastructure such as water supply, road improvements, and drainage for urban centers and simple sanity infrastructure such as wells, pipelines, and latrines for poor villages. The project has been suspended since early 2001 because of the difficulty of carrying out on-site technical supervision and monitoring (cf Mann 2001b).

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Annex I: Data sources

The analysis of the social sectors below of the health and education sectors draws on various data sources. The most recent of the Susenas household survey was conducted in 1999 by the bureau of statistics (BPS). For more recent data we rely on a poverty survey conducted by the University of Siah Kuala¹⁰ (Poverty Survey) and a facility survey conducted by KDP facilitators (KDP survey).

The 1999 Susenas provides statistically sound estimates of poverty, and other social welfare indicators. The data also allow for a comparison between Aceh and the rest of the country. BPS ceased

the household survey after 1999 because of safety concerns. When presenting tabulations by welfare status we distinguish between poor, middle, and rich households. For the analysis based on the Susenas 1999 this classification is based on the per capita household consumption of the household. The first quintile is categorized as poor, the third as middle and the fifth as rich.

The Poverty Survey was conducted by students of the university during their summer break in August 2002. Basic socio-economic information was collected from households, health and education facilities and a community questionnaire for 2 villages in almost all kecamatans in Aceh. Students were asked to collect information from 2 poor households, 1 middle, and 1 rich households. Because the classification is subjective, and probably depends on how wealthy the area is, the categorization of households in poor, middle and rich it is based on an indicator based on household assets and consumption. The sampling however, remains non-random. If we compare characteristics of time-invariant variables across the three groups we find that the poor generally have rather similar characteristics. The housing characteristics indicate that the rich in the Poverty Survey represent a higher income bracket than the rich in the Susenas household survey.

The KDP survey was fielded in September 2002 and collected information on prices, wages, and health and education service delivery from 900 kecamatans in which KDP was operating throughout the country. The choice of the village where the facilitator collected the data was not specified. The purpose of the survey was to establish a mechanism that could deliver up to date information on the situation in the social sectors by using existing project reporting mechanisms.

¹⁰ Financial assistance was provided by the Office of Transition Initiatives and technical assistance by the World Bank.

Annex II: Fiscal Flows to the Aceh's Regional Governments (2002/2003)

	<u>Central Transfers</u>				<u>Other Allocations</u>			<u>FY 2002 Revenue Sharing</u>				
	DAU 2002 Final (billions Rp)	DAU TA 2003 (billions Rp)	DAU 2003 Adjustment (billions Rp)	DAU 2003 Final (billions Rp)	DAK 2003 (billions Rp)	Wage Hike Compensation 2003 (billions Rp)	Teacher Top Up 2003 (billions Rp)	STX (billions Rp)	SDA (Oil) (billions Rp)	SDA (Gas) (billions Rp)	SDA (Other) (billions Rp)	
1 Kab. Aceh Barat	174.8	76.3	0.0	76.3	9.2	4.7	2.1	6.6	7.7	1.2	0.	
2 Kab. Aceh Besar	167.0	192.2	0.0	192.2	7.0	12.7	3.3	5.0	7.7	1.2	0.	
3 Kab. Aceh Selatan	137.5	114.3	0.0	114.3	10.9	6.7	1.5	4.2	7.7	1.2	0.	
4 Kab. Aceh Singkil	101.5	93.3	8.3	101.5	3.6	1.6	0.6	4.8	7.7	1.2	0.	
5 Kab. Aceh Tengah	146.1	149.7	0.0	149.7	12.5	7.4	2.5	4.9	7.7	1.2	0.	
5 Kab. Aceh Tenggara	130.6	89.1	0.0	89.1	10.2	4.0	1.2	5.4	7.7	1.2	0.	
7 Kab. Aceh Timur	180.1	139.0	0.0	139.0	8.4	8.2	2.5	15.0	21.2	1.6	0.	
3 Kab. Aceh Utara	199.9	149.1	50.8	199.9	4.4	9.4	2.9	24.4	94.8	15.7	0.	
9 Kab. Bireuen	138.9	154.0	0.0	154.0	4.8	8.5	3.2	7.7	7.7	1.2	0.	
9 Kab. Pidie	233.0	221.8	11.2	233.0	8.7	12.4	3.9	5.5	7.7	1.2	0.	
1 Kab. Simeuleu	87.3	79.7	7.6	87.3	10.2	1.4	0.6	4.7	7.7	1.2	0.	
2 Kota Banda Aceh	138.0	134.5	3.5	138.0	8.4	7.8	2.7	7.7	7.7	1.2	0.	
3 Kota Sabang	79.9	77.8	2.1	79.9	9.6	1.8	0.3	4.6	7.7	1.2	0.	
4 Kota Langsa	57.5	62.6	0.0	62.6	3.4	1.0	0.4	0.0	7.7	1.2	0.	
5 Kota Loksumawe	62.7	87.3	0.0	87.3	3.7	2.8	1.0	0.0	7.7	1.2	0.	
5 Kab. Aceh Jaya	0.0	41.9	0.0	41.9	8.6	2.8	0.8	0.0	631.4	228.8	1.	
7 Kab. Nagan Raya	0.0	64.9	0.0	64.9	8.8	1.5	0.4	-	-	-	-	
3 Kab. Aceh Barat Daya	0.0	47.6	0.0	47.6	8.7	2.3	0.5	-	-	-	-	
9 Kab. Gayo Lues	0.0	58.9	0.0	58.9	8.2	1.9	0.6	-	-	-	-	
9 Kab. Aceh Tamiang	0.0	52.5	0.0	52.5	9.1	2.9	0.9	-	-	-	-	
Local Governments (Total)	2,034.7	2,086.3	83.5	2,169.8	158.5	101.9	32.1	100.3	847.9	261.1	4.	
Province Aceh	172.4	76.1	96.3	172.4	2.5	9.7	0.0	32.0	54.1	8.1	1.	
Province Aceh (Special SDA)								0.0	631.4	228.8	1.	
Total (Province + LGs)	2,207.1	2,162.5	179.8	2,342.3	161.0	111.6	32.1	132.3	1,533.4	497.9	6.	
Local Governments (est. million USD)	226.1	231.8	9.3	241.1	17.7	11.3	3.6	11.1	94.2	29.0	0.	
Province (est. million USD)	19.2	8.5	10.7	19.2	0.3	1.1	0.0	3.6	76.2	26.3	0.	
Total Aceh (Province + LGs est. million USD)	245.2	240.3	20.0	260.3	18.0	12.4	3.6	14.7	170.4	55.3	0.	