

11th Consultative Group Meeting on Indonesia
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Concluding statement of Mr. Jemal-ud-din Kassum
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Coordinating Ministers, Ministers, Excellencies, Distinguished Representatives, Ladies and Gentlemen,

We have come to the end of a day and a half of very fruitful discussions and it is now my difficult task to sum up the key ideas, decisions, and agreements that have emerged. But before I do so, may I, on behalf of all of you, thank the Government of Indonesia for their very gracious hospitality and Bank Indonesia for their excellent premises and the outstanding arrangements – and particularly to Pak Komara Djaja and his team, without whom this CGI would not have been so smooth and productive. I also want to express my appreciation to all the ministers who so generously gave of their time to attend these meetings and to share with us their thoughts and ideas. To all the CGI member representatives– especially those who came from far away – thank you for participating and for pledging so generously. Our special thanks are due to your staff and the government representatives who participated in the preparatory working groups. And finally, thanks go to the civil society representatives who added valuable perspectives to our discussions.

With each CGI, the discussions have improved in quality and focus. This time, the painstaking preparation of the working groups comprising donor and government representatives – and in some cases, civil society representatives as well – has paid big dividends. The presentations made by the coordinators of the working groups were quite excellent and enriched our discussions greatly. I hope that we can evaluate the work of these groups and assess how best they can contribute between CGI meetings and to the poverty reduction agenda.

The need for urgent action

If there was one theme that emerged from this CGI meeting, it was – to echo the words of the United States delegate – the need for action, action, action. The delegates recognized the many constraints facing Indonesia – weak institutions, an ongoing ambitious decentralization process, a turbulent transition to democracy, lack of coordination among different branches of government – but urged that inaction carried with it its own severe costs. Where there are policy reforms within the control of government to implement – it should do so immediately. Successful reforms would create their own virtuous circle, allowing Indonesia time to address its more fundamental problems.

Recovery, fiscal sustainability, and SMEs

We started our substantive discussions with a review of Indonesia's economic stability and recovery – and were reminded by Minister Boediono of the two important pillars of **fiscal sustainability** and monetary prudence. The size of Indonesia's debt burden was an important theme both yesterday and this morning. We learnt that the Government intended to reach a balanced budget by 2004 while lowering the debt-GDP ratio to 60 percent. As Mr. Boediono said this morning, the

government is moving on two tracks. The first is on the budgetary side through significant improvements in tax administration, aggressive asset sales, privatization of state enterprises, and phased increases in fuel and electricity prices. These are all the more important given the need for expenditure increases in selected, high priority areas – such as health, education, and the maintenance of public infrastructure. A second track was to seek better terms from the Paris Club, and indeed from all of us (through access to our soft loan arms) and to explore debt-swaps, a suggestion that also came from the NGOs. Ibu Binny from INFID, reviewing the views of other civil society groups was impatient that we were not seeking more aggressive solutions. Australia reminded us of the importance of improving debt management. As you may know the Bank is working with Australia on this issue.

On monetary prudence, the Governor reassured the meeting of Bank Indonesia's strong commitment to price stability through a firm monetary stance, adjusted in light of international conditions – and noted the work ahead on restoring bank intermediation as critical to sustaining the economic recovery.

The IMF noted that a robust recovery would also need a healthy and functioning banking system and a conducive investment climate supported by good governance and an effective legal system – a theme that was picked up in later discussions. The investment climate received a lot of attention yesterday. Tomorrow's government consultations with the private sector, to which you have been invited, will provide an opportunity to learn more about this issue. But many of you raised key issues: Japan cited the need to improve labor management relations. The ADB cited potential power constraints from the slow progress on power sector restructuring. Members generally welcomed the new investment policy and urged early enactment of a unified national law on investment. Members stressed the need to ensure that regions also are aware of the importance of establishing an enabling environment for investment. Australia pointed out that investments in mining had ground to a halt because of large uncertainties following decentralization.

SME development was recognized as important for exports, employment, foreign direct investment, and poverty reduction. The meeting called upon government to exercise a leadership role in this important area, build a more conducive and predictable policy environment, streamline rules and regulations, encourage best practice among SMEs, and design differentiated approaches to SME groups of different size and capability. The international community is prepared to support this effort – and looks to the ADB and Japan for leadership in this important area.

Governance and Corruption

We had an extremely frank session on **justice sector** reform yesterday. I very much appreciated the candor of all those who spoke – as well as the willingness of our Indonesian colleagues to listen to, and answer, some tough messages from members of the donor and creditor community. I was also very gratified at the fact that the top leadership of the justice sector institutions – the Ministry of Justice, the Attorney General's Office, the National Police, and the Supreme Court -- as well as of course Coordinating Minister Yudhoyono were present at that session.

The four messages delivered by the donor community were:

- First, that the justice sector matters enormously for Indonesia's future, both because economic recovery in good part depends on it and because it is a key factor in retaining

social cohesion and stability. It was important, therefore to consider its reform a national policy priority with a commensurate allocation of political attention and commitment

- Second that the complexities and inter-relationships of the different parts of the sector are such that a comprehensive time-bound program of reform, including demonstrable milestones, needs to be urgently adopted and pursued;
- Third, the process of reform, precisely because of its complexity, needs strong management, including effective coordination, by government.
- Fourth, the sector needs to be properly funded and resourced. Donors were willing to support such an effort, but government needed to find resources from its budget.

Government speakers described the sector not so differently from the way donors did. There was a frank acknowledgement of the weaknesses of the sector and of the difficulties Indonesia faces in overcoming these weaknesses. The Government noted that reform of this sector was a top priority for the country, as is shown by the prominence the matter is given both in the State Policy Guidelines and in the National Development Program 2000 – 2004 (PROPENAS). A number of measures have been taken to address some of the more manifest problems, including the passing of new anti-corruption legislation and a law establishing an anti corruption commission. In addition ad hoc judges are now being trained to carry out the mandate of the new human rights court. Other legislative initiatives were noted, including a proposed anti-money laundering law. The Coordinating Minister did caution us not to overestimate the formal capacity of his Office to coordinate reform in this sector. However, he did tell us that he intended to make sure that the President was fully informed about the messages given at this CGI and that he was confident the Government would respond appropriately to the challenges of justice sector reform. Indeed he suggested the first step was some form of national consultation, and in this context, he agreed to consult Indonesia's international partners on the process going forward.

In this context, given that Pak Yudhoyono has agreed to join the Board of the Governance Partnership, a very significant development, and given that the Partnership has already begun a dialogue with him on such a consultation, perhaps the Partnership could be an appropriate forum in which all the key stakeholders are brought together. In this context, I was pleased with the strong support offered to the Partnership, including Japan and EU's significant contributions to the Governance Fund of the Partnership. Most of us were there on Tuesday at the Partnership's dialogue with the CGI and I am glad to note the progress that it has made since we last met in Tokyo.

Our discussion on **forest management** risked being overcrowded by the justice sector. Nevertheless it yielded some very useful conclusions. As with the justice sector, the Government agreed with the donors and NGOs that progress in tackling the sector's many complex problems has been inadequate. The main obstacle, setting up and maintaining an effective inter-departmental mechanism to coordinate sectoral policy and process, has been recognized since the February 2000 CGI meeting but has yet to be overcome. The Government, I am pleased to note, will prioritize revitalizing the Interdepartmental Committee on Forestry (IDCF) and providing it with a means to receive input from all stakeholders. This should facilitate sustained, effective approaches to most of the forestry problems - including the two that were generally accepted as the most urgent – control of illegal logging, and restructuring the forest-based industries to improve their efficiency and balance their raw material requirements with sustainable timber supply. Indonesia's development partners and NGOs also observed that there have been "more than enough workshops and meetings" but not nearly enough concrete and sustained action. The message to Government was clear. Begin at a more modest scale and use success to develop

momentum and demonstrate successful interagency cooperation. It was interesting to note that the successes reported by the Ministry of Forestry in controlling illegal logging involved direct inter-agency action at the level of individual national parks and kabupatens. Small beginnings with potentially large ripple effects. We also welcome Min. Yudhoyono's endorsement of the principles of transparency and civil society in participation in forestry management.

Empowering and Investing in the Poor

The key message from the **decentralization** discussion, which was a remarkably interesting session, was that decentralization could make or break Indonesia's effort towards poverty reduction through changes in accountability relations, fiscal transfers from the central government, tax and regional regulations, and the ability to enforce national standards. The Central government needs to strengthen its ability to facilitate and promote effective pro-poor decentralization. Apart from capacity strengthening, the main messages from a poverty reduction perspective were:

- Improve the DAU general grant allocation formula further in 2003. The reversal in parliament of efforts to improve it in 2002 was a setback that needs to be taken up with parliament by the government. In this regard CGI members welcome the government's commitment to make progress on pro poor outcomes in decentralization, including mechanisms of targeted DAK grants as a mechanism for equalization and transparency.
- Effective supervision of regions to ensure that regulations and tax policies protect the poor.
- Clarifying what are indispensable functions of different levels of government and minimum standard targets for health and education and other poverty related activities. These standards must address inequity and disparities within and between regions, which implies developing adequate monitoring systems for social indicators.

While conveying this advice, donors were anxious to ensure that this was done in a way that it did not recentralize activities. I believe that Government is open to these ideas and that they must be high on the list of things for the new poverty secretariat to focus on. I was also pleased to hear the government's commitment to revitalize the intergovernmental coordination team chaired by the Ministry of Home Affairs so that it plays a more effective role in coordination.

I found it fascinating, as you must have done, to see the discussion on education picking up on many of these themes. What was encouraging here was the considerable convergence in thinking between government and its international development partners. Clarification of the distinctive, efficiency-driven relative roles of different levels of government, delineating a role for communities, capacity building, concerns about inequality, the need for minimum service standards, and the key but changed role of central ministries, were themes that reverberated between the general discussion on decentralization and that on education. The working group would like to see a clear education sector reform strategy to address issues of quality (high drop out rates and low attainment levels, and low labor market results) which perpetuate poverty. With the ministry of education clearly on board on all these issues, we need to now encourage the working group to continue its work and to help government set for itself some clear benchmarks for progress.

Implications for A Poverty Reduction Agenda

For me one of the high points of yesterday's discussions was Pak Dorodjatun's remarks at the beginning of our last session relating the various discussions to our theme of poverty reduction. I was delighted to see that we have now crossed the hurdle of establishing a sensible institutional underpinning for the development of a poverty reduction strategy, a process which is strongly supported by members. The Coordinating Ministers for the Economy and People's Welfare will jointly be responsible for developing and implementing a poverty reduction strategy. They will head a ministerial committee which will be supported by a secretariat to be established in Bappenas. In this context, I would stress the point made by the UK that the Coordinating Ministers review the suggested tasks and mandates in the CGI working group paper. A Presidential decree is expected by the end of this month. We were all, I am sure, particularly pleased to see how the Minister saw the process for preparing a poverty reduction strategy, and his strong commitment to a thoroughly participatory process with broad consultations to take place over the next six months. To quote the Minister, "the aim of this process is not planning documents, but a locally owned process of strategic change that will improve the enabling environment for the poor and lead to proposals that can be integrated into all aspects of the country's program." We could not have said it better. The minister's statement then went on to articulate what might be covered under such a strategy. We are off to a strong start here. In this context, members would urge the Government to review jointly with the various working groups for the CGI the actionable short term items on poverty reduction identified in the poverty reduction working paper with a view to possible joint implementation with donors.

Aid Effectiveness

Let me now turn to this morning's discussion. As I said this morning, it is remarkable how far we have come in our ability to confront difficult issues. I believe it is a true compliment to the vibrancy of Indonesia's democracy and to the respect that the Government of Indonesia has for the right of free speech that a senior minister of the government can speak as freely on issues of corruption as Pak Kwik did this morning. It was an important reminder of our roles and obligations as donors. Most of us, as the German and ADB interventions have clarified, are now spending a lot of resources to prevent corruption and collusion in our projects. There are limits to what we can achieve by ourselves. It is, therefore, important that government now move decisively on the reform of public procurement and financial management, with initial steps, as noted in Pak Kwik's statement, including the establishment of an NPPO and the revision of the flawed current drafts on state finance, treasury, and audit taking into account international best practice.

Pak Kwik's statement also including a number of other commitments to address aid effectiveness issues including rationalization of ongoing development activities in light of current budget constraints, and the extension of transition arrangement for onlending through fiscal 2002.

CGI members also recognize that we are part of the solution on aid effectiveness. Ensuring aid effectiveness will require greater emphasis on government ownership of the development process, and strengthened participation of beneficiaries and civil society in the design and implementation of projects. The Netherlands also favors a DAC review of aid effectiveness in Indonesia and how it can be improved.

Pledges

The Government requested a disbursement amount from the CGI of between US\$3.0 to 3.5 billion to meet the external financing gap in the budget. The total pledge from the CGI in support of the 2002 budget amounted to US\$3.14 billion, of which over \$1.3 billion will be dependent on policy performance and the remainder will be disbursed in support of development projects. These pledges indicate, perhaps more clearly than words, that the international community would like to see Indonesia succeed and is prepared to support its recovery efforts with substantial amounts of financial assistance. But much of this support will be contingent upon improved policy performance – which, in the eyes of the international community, is critical for sustainable, rapid growth. The large differences between pledges and actual disbursements in the past suggest that, while such resources are available, their disbursement in 2002 will depend on a significantly higher level of reform effort than has been seen in the past few years.

In closing, let me once again thank you for participating in this productive day and a half of meetings and for your generous pledges in support of Indonesia. The next CGI meeting will be held a year from now. We will get back to you on location, but I look forward to seeing you all there in 2002. In addition Pak Dorodjatun has suggested in the interim that we hold periodic stock taking reviews and chart next steps. I welcome this suggestion and will ask Mark Baird to work toward this objective, and think through the role of the working groups to facilitate this process.

Thank you very much and – to many of you – have a safe journey home.