



Australian Government

Department of Foreign Affairs and Trade

Aid Investment Plan

Indonesia

2015/16 to 2018/19

Strategic priorities and rationale

Context and rationale

As a close neighbour, Indonesia is a key partner in terms of our bilateral, regional and global interests. A prosperous, stable and growing Indonesia is good for our stability, security, trade and cooperation in our shared region.

Indonesia has reached middle income status and achieved substantial development progress in recent years. But challenges remain such as infrastructure bottlenecks, skills deficits and institutional weaknesses. To address these challenges we will work with Indonesia to target fundamental constraints to Indonesia's growth and poverty reduction, where Australia can add most value.

To address these constraints we will adapt our program to strengthen initiatives that directly support economic diplomacy and aid for trade (contributing to the 20 per cent target under the *Strategy for Australia's Aid for Trade Investments* by 2020). Economic governance programs will double as a proportion of program spending and our support for infrastructure will leverage Indonesia's own infrastructure spending and improve the quality of public and multilateral development bank infrastructure projects. We will ensure a focus on private sector development in all of our investments. Critical also to addressing constraints to growth will be a focus on increasing the capacity of women to participate in the economy and political life. Human development also remains a focus, but we will accelerate our shift away from physical investments towards support for systemic change and Indonesian capacity to deliver better quality services.

Economic growth, poverty reduction and development challenges

Indonesia's recent economic progress has been impressive, having almost doubled its GDP from 2001 to 2012 and reduced poverty levels by roughly half. However, Indonesia's prospects for securing growth at past levels are not certain. Growth has slowed and the risk that it could fall further is real. Slowing growth is a development issue for Indonesia, since it would make it more difficult to meet its goals to graduate from middle income status by 2025. Furthermore, low growth means the poor will find it harder to escape poverty.

Increasing equitable growth and the creation of productive jobs needs a foundation of increased competitiveness for a more attractive investment environment. The major structural constraint for competitiveness includes the quality and quantity of Indonesia's infrastructure and institutional issues such as transparent and effective economic oversight, and regulatory certainty.

Improving the efficiency and competitiveness of Indonesia's labour and product markets are critical challenges. Although on average Indonesia's labour force is becoming better educated and living longer, persistently poor learning and health outcomes mean lower worker productivity and skilled jobs going unfilled, in part through reduced labour mobility. Recent analysis has shown improved health accounted for an estimated 24 per cent of income growth in middle income countries over the past decade. Poor nutrition – most dramatically illustrated by the high prevalence of stunting (37 per cent) among Indonesian children – is also imposing long-term economic costs through impaired cognitive function. And although women constitute an increasingly large share of Indonesia's formal sector workforce, their labour force participation is well below that of men (51 per cent compared with 85 per cent) and wages lag by 25 per cent.

Service delivery aimed at addressing these health and education outcomes is itself complicated by decentralisation. Considerable autonomy has been given to subnational governments but their capacity can be low, and coordination

between different levels of government is sometimes weak. And the regional transfer system that allocates half of the discretionary government resources to local government still has poorly developed performance criteria.

Politically informed and efficient approaches

Australia is the largest bilateral grant partner to Indonesia, but a smaller portfolio of assistance will accelerate our move away from the traditional donor recipient-aid model towards a more mature partnership – an “economic partnership” – that focuses on leveraging Indonesia’s own substantial resources. At around \$320 million per year, Australia’s development assistance will represent less than 0.3 per cent of Indonesian Government revenue. Achieving impact will therefore not be about the volume of resources we bring to the table, but will be about being able to deliver development assistance aimed at catalytic reform.

We will continue to make a contribution in Indonesia by delivering high grade policy knowledge that is responsive to the Indonesian Government’s objectives. Our policy and technical advice will be aimed at improving the quality of Indonesia’s investments in infrastructure, economic governance and social policy. Examples of existing work using this approach include assisting Indonesia manage the risks of the fuel subsidy reduction, improving the efficiency of decentralised funding, and introducing new methods of financing infrastructure. Our new economic partnership will increase this type of assistance in close collaboration with the Indonesian government to maximise results. We will reduce the proportion of spending on actual provision of services themselves, including building schools. These functions can now be absorbed more effectively under Indonesia’s own budget.

The complexities of the Indonesian political economy have been considered in all of our investment choices. Our economic partnership will be targeted at various national, sub-national and local levels, as appropriate. We have worked with the Indonesian government to closely align Australia’s program with Indonesia’s Medium-Term Development Plan (RPJMN 2015-2019) and priorities of the Indonesian President. President Joko Widodo is seeking to accelerate productivity, competitiveness and inclusive development, including through an ambitious development agenda that focuses on building infrastructure, poverty reduction and inclusive growth through education and health improvements, and strengthening Indonesia’s bureaucracy. Regional disparity between the east and west was also identified in the RPJMN as a primary issue for development.

Goal and objectives

The overarching goal of Australia’s development program will be to partner with Indonesia to boost inclusive growth and productive jobs by improving Indonesia’s competitiveness through strengthening the impact of Indonesia’s own resources.

Three objectives will contribute to this goal:

1. Effective economic institutions and infrastructure,
2. Human development for a productive and healthy society, and
3. An inclusive society through effective governance.

Sectoral programs may contribute to more than one objective, and gender equality, inclusion of people with disabilities, and rural development programs will be cross-cutting. Our investments in gender equality and women’s empowerment will continue to focus on women’s political and economic empowerment and social protection, including growth-related issues such as labour migration and mobility. Access to education, government social protection and poverty reduction programs, reducing violence against women, and maternal and reproductive health services will also be important. We will develop a gender action plan to specify how we will reach the strategic target on empowering women and girls. In addition, gender will be mainstreamed across all of our new investments by ensuring that personnel on design, implementation and evaluation teams have an appropriate level of gender expertise and by engaging gender advisers where appropriate.

Objective 1: Effective economic institutions and infrastructure

We will align our economic governance investments with our economic diplomacy strategy by supporting Indonesia to boost inclusive growth and productive jobs by improving its policy and regulatory settings. We will support aid for

trade by providing the foundation for higher economic growth, private sector investment and increased levels of trade. We will promote productivity-enhancing reforms such as financial sector stability, revenue mobilisation, and improved budget execution through our economic governance programs. Technical assistance, including through government-to-government partnerships, will focus on areas such as financial sector supervision and regulation, tax collection, budgeting, macroeconomic management, and providing a supportive trade and investment climate.

We will help Indonesia tackle underlying disincentives to investment in infrastructure, particularly from the private sector, including input on regulations and project planning. Improvement in this area will require higher levels and better quality of spending, strengthened project selection and preparation, partnerships between the public and private sector and streamlining land acquisition processes. Sustainable revenue increases through the tax system will also be essential for meeting infrastructure plans.

Our strengths lie in supporting the roads, water and sanitation investments that Indonesia's rapidly urbanising population need to become more productive. We will shift away from directly building or demonstrating actual infrastructure using grant funding, to partnerships with relevant ministries to provide policy advice and improve the preparation phase of projects funded by the Indonesian government and the development banks. In addition to these investments, our governance programs that support Indonesia's community grants program, will target rural village-level infrastructure such as roads and water connections to essential public services including schools and health clinics.

As nearly two thirds of Indonesia's poor live in rural areas, we will continue to focus on the development of the agricultural sector. We will encourage inclusive economic growth by strengthening the operation of agricultural markets, improving food security, raising agricultural productivity, and helping to boost poor farmer's incomes and employment by addressing constraints such as access to loans. We will also increasingly look to better connect implementation programs with policy dimensions and facilitate private sector-led investment in better agricultural practices and services such as irrigation. The *Investing in Women Initiative* will promote an economic growth agenda that increases employment opportunities for women in the formal sector.

Objective 2: Human development for a productive and healthy society

Human capital is central to improving the productivity and mobility of Indonesia's labour force. We will help catalyse systemic change to provide better quality health and education services to local communities, including in the poorer eastern regions of Indonesia where health and education indicators are low. We will move away from investments that support the delivery of basic services, such as funding training of government staff, and instead focus on the design and testing of flexible programs that address underlying structural weaknesses or problems. Our investments in human development will target both the supply and demand side. We will work at the national level to support policy-makers and at the sub-national level to improve service quality and governance systems. In addition, we will address demand-side factors, including support for communities and civil society to engage in the governance of service delivery and to hold providers accountable.

Despite its middle income status, Indonesia spends the least in the region on health as a percentage of GDP (around 2.4 per cent) and has some of the lowest health indicators. We will retain a focus on HIV in eastern Indonesia, emerging infectious diseases, and consolidate support to maternal health and systems strengthening, the latter addressing regional biosecurity in line with the *Health for Development Strategy 2015-2020*.

Our community-driven programs in the water and sanitation sector, and our community grants programs are focused on human development goals and also contribute to the health and learning goals under this objective.

Without efforts to improve the mobility of the workforce through improving the quality of education and workforce skills, Indonesia will remain poorly positioned to transition towards a globally-competitive economy and the workforce required by the creation of the ASEAN Economic Community in December 2015. We will strengthen our program to focus on education quality – through improving Indonesian-led efforts focussing on teacher quality and learning outcomes in schools. We will complete our schools construction program and move into providing timely policy advice and testing innovation at the school level in emerging areas such as school leadership, assessment and public-private partnerships. Our *Empowering Indonesian Women for Poverty Reduction (MAMPU)* program will contribute to this objective, and we will take opportunities to effectively integrate disability considerations.

We will streamline our scholarships program, while strengthening alumni links and people-to-people connections. We will balance degree awards with short courses, increasingly targeting the private sector. PhD and Masters scholarships will be targeted towards Indonesia's future leaders in economics, engineering, health and education. We will also enhance alumni engagement with privately-funded scholars, including to support the New Colombo Plan.

Objective 3: An inclusive society through effective governance

Besides poor health and education outcomes, the low coverage of social safety nets is a constraint to inclusive growth in Indonesia. Indonesia still has the fifth largest concentration of poor in the world with around 100 million living on \$2 or less a day. This means many are vulnerable to falling back into poverty due to relatively minor shocks (such as food price increases or health problems). Indonesia recognises that it needs programs which address the near poor and vulnerable, including people with disabilities. People with disabilities continue to face exclusion from services, jobs and non-fulfilment of basic human rights. Disability factors are included in most of our human development programs and in addition, DFAT is supporting the Government of Indonesia to implement *Program Peduli*. In line with the Australian Government's *Development for All 2015-2020 Disability Strategy*, this program will increase access for people with disabilities to public services and social assistance, increased fulfilment of human rights and improved government policy on the inclusion of people with disabilities.

By introducing greater flexibility into our governance investments, we will be able to respond to Indonesian priorities, providing world class international and Indonesian expertise to advise on policy and implementation. This will focus on policies to better target poverty programs, reform labour legislation and promote greater labour market flexibility and mobility.

Our law and justice work, important to promoting stability and prosperity in the region, will support our shared interests in counter-terrorism, transnational crime, prison reform and anti-corruption.

New decentralisation laws mean there will be increased authority at the provincial and district level, and new funding managed directly at the village level. Managed carefully, this has potential to produce improvements in services and increase local economic opportunities. We will help strengthen the capacities of villages and community institutions to demand quality services from providers and engage with sub-national governments to underpin efficient, effective and accountable service delivery.

We will continue to pursue programs for women's economic and political empowerment which encourage legislation that helps women gain access to jobs and other sources of financial autonomy, including from migration; increasing support to women's businesses, including through micro-finance; and providing support to new women parliamentarians.

The use of evidence and analysis to inform policy development is a critical aspect to all our engagements. Our investments in the knowledge sector will help Indonesia to develop the government, private sector, and civil society organisations that provide analysis for policy makers. The primary focus will be on issues of social policy such as poverty reduction, health and education service delivery.

Implementation approaches

The Government of Indonesia is our principal delivery partner. An effective program will depend on us prosecuting a genuine partnership with the government, and ensuring that the right relationships are in place with key Ministries. We will continue to engage regularly with the Ministry of National Development Planning/National Development Planning Agency (Bappenas) to confirm that Australia's priorities remain aligned with and contribute to the development agenda of Indonesia.

We will select the most appropriate implementing agencies, rigorously oversee the effectiveness and efficiency of progress and make hard decisions to deal with underperformance. We will continue our trend toward fewer, larger investments and continue compliance with Australian aid visibility guidelines so that our partnership assistance is appropriately recognised.

A successful shift in program focus will require intense negotiations with a large number of stakeholders and significant changes to existing and planned contract arrangements.

The private sector

In line with the Australian Government's development policy *Australian aid: promoting prosperity, reducing poverty, enhancing stability*, we will help create a business enabling environment, deepen engagement with, and aim to leverage support from, the private sector. Initiatives will be required to demonstrate regular engagement with relevant private sector stakeholders and report on this in annual monitoring processes. These issues are a priority across all three objectives.

In support of our aid for trade objectives, we will work extensively on enabling the business and trade and investment environment. We will help Indonesia attract large scale loans for infrastructure from investors such as multilateral development banks by providing high level technical advice to develop quality investment proposals. We will also use our economic governance programs to support private sector investment by assisting with Indonesia's macroeconomic stability, bureaucratic reform and financial sector regulation. We will facilitate private-sector led investment in innovative agricultural practices, such as improvements to the red meat and cattle supply chain through the *Indonesia Australia Partnership on Food Security in the Red Meat and Cattle Sector*, to boost farmer productivity and competitiveness. We will also demonstrate innovative ways to raise the quality of teaching across the many thousands of non-government Indonesian schools.

We will engage with the private sector to help promote growth or solve development problems through working with more private sector partners to deliver short courses, by partnering with innovative public-private partnerships such as Grow Asia, and through programs such as our *Empowering Indonesian women for poverty reduction* which works with retailers to help traditional women's weaving groups develop high quality products and access to distribution channels for domestic and international markets. We will also pilot different financing models such as our contribution, with the backing of the InnovationXchange, to USAID's Development Credit Authority to enable private financing of small-scale clean energy projects throughout Indonesia.

Technical assistance

Technical assistance is a large proportion of our assistance in Indonesia and is critical to helping unlock reforms and engage in policy dialogue. Australia utilises high quality technical assistance and policy advice that is flexible, efficient and demand-driven by the Government of Indonesia. Relevant experience, strong advocacy skills, extensive local networks and an understanding of Indonesia's key reform priorities ensure that Australian-funded advisers and Australian Government officials (through the Government Partnerships Fund) achieve value for money. Using technical assistance to provide targeted advice has proven particularly successful (for example, Australia is now Indonesia's leading development partner in economic governance) and why we are focusing more of our investment in this area.

Where Australia does engage advisers, they will be accountable to both the Australian Government and Indonesia. Australia will engage our partners on adviser recruitment and review processes. All adviser positions will continue to be jointly agreed with the Government of Indonesia, represent value-for money and deliver against terms of reference carefully linked to our objectives.

NGOs

Indonesian NGOs have been a key driver of political, economic and social reform, including on issues such as women's rights, anti-corruption, freedom of information, and religious tolerance. The NGO sector has also made critical contributions at both national and local levels to enhancing inclusive and sustainable development by seeking to ensure that those most in need are able to live healthy and productive lives.

To ensure that Indonesian NGOs continue playing an active and effective role in Indonesian development and democracy, they need to have effective and equitable engagement with government and the private sector; be well governed, independent and accountable; and have access to adequate, diversified funding.

We will work through NGOs on several priority outcome areas including:

- improving the quality of public spending;
- improving governance effectiveness;
- meeting community needs;
- empowering women and people with disabilities;
- improving provision of public services; and
- identifying local solutions to local problems.

Australian and international NGOs will continue to be important partners in program delivery, both through centrally managed programs such as the Australian NGO Cooperation Program and as service providers under the bilaterally managed development cooperation program.

Managing contractors and flexible approaches

A large proportion of program funds are currently delivered through managing contractors, engaged to deliver beneficial outcomes on behalf of the Australian Government. This includes providing strategic and technical advice to DFAT and the Government of Indonesia, managing procurement, facilitating strong local networks and partnerships, and monitoring and evaluating the results of implementation.

We will continue to use managing contractors where they represent the most effective delivery model. DFAT, in partnership with the Government of Indonesia, will closely oversee the selection and performance of managing contractors. We will engage contractors and develop funding facilities in line with plans that are both programmatically coherent and flexible enough to adapt to unforeseen reform opportunities. We will also rigorously assess the performance of our managing contractors through annual partner performance assessments to ensure that they continue to represent the best value for money for Australian taxpayers.

Multilateral organisations and other donors

Australia has a strong partnership with the World Bank and Asian Development Bank in Indonesia which will continue and deepen through the term of this AIP. We will align more squarely with their expanded lending programs and assistance for infrastructure including the World Bank's Global Infrastructure Facility and the Asian Development Bank's Asia Pacific Project Preparation Facility. We will also collaborate more on national-level policy issues including in areas such as social protection, education and health. We will also engage with the new Asian Infrastructure Investment Bank whose presence in Indonesia is likely to expand over the period, and the Global Infrastructure Hub that will commence in 2016. Key other donor partners include the United Nations, GAVI Alliance, and USAID.

Australian academic institutions

We will deepen engagement with Australian universities, including institutions such as the Indonesia Project at the Australian National University funded as part of the development program. Building on further opportunities under the New Colombo Plan in Indonesia will also provide greater opportunity for Australian universities to develop understanding of the tertiary education sector in Indonesia.

Progressively working through government systems

Where appropriate, Australia will use Indonesia's own systems to deliver Australian development assistance. Alignment with Indonesian systems will be selective and we will adopt a phased approach, informed by rigorous assessment of fiduciary and other risks. Our Fraud and Anti-Corruption Strategy along with ongoing risk and performance measurement will ensure that risks are proactively identified and effectively managed.

Performance management

Performance benchmarks

The following performance benchmarks are based on the interim benchmarks published in the 2013-14 APPR. They are representative of the broad range of sectors the program currently operates in, and where we can measure Australia's attribution to development outcomes. A revised set of benchmarks, linked to the PAF and more representative of the future profile of the program, will be developed once budget allocations and programmatic implications have been agreed.

		2015-16
Aid objective	Enhanced economic institutions and infrastructure	
Performance benchmark 1	Km of roads rehabilitated or maintained	1,300
Performance benchmark 2	People living in urban and rural areas with improved access to water and sanitation	1,090,000
Performance benchmark 3	Undertake a review with the Government of Indonesia (GoI) of financial sector needs in order to meet economic growth expectations and finalise development and pilot a risk framework to identify tax payer compliance risk, improving targeting of those audited.	Review completed & risk framework accepted by GoI.
Performance benchmark 4	Number of smallholder farmers with increased incomes through private sector investment	18,000
Aid objective	Human development for a skilled and healthy society	
Performance benchmark 5	Additional births attended by a skilled birth attendant	2,000
Performance benchmark 6	New school places created	23,760
Aid objective	Promote effective governance for an inclusive society	
Performance benchmark 7	Additional local women's groups established to participate in policy influencing activities in areas such as jobs, leadership and reducing violence against women.	180
Aid objective	Advance gender equality and women's empowerment	
Performance benchmark 8	Quality: Percentage of investments assessed as effectively addressing gender equality in implementation	74
Performance benchmark 9	Spend: Percentage of total spend where gender is a significant objective	40

Mutual obligations

Australia's support is provided in alignment with Indonesia's own development agenda and progressive policy commitments. This agenda is set out in Indonesia's five-year development plan (RPJMN 2015-2019), which includes annual performance targets. We will work to closely align with these commitments. Indonesia has committed to

strengthen human development; make improvements to primary sectors, such as infrastructure, agriculture, health, and education; and promote financial stability and equity between income groups and regions in order to grow the economy. Our technical assistance will provide the evidence necessary to encourage reform and adherence to commitments in the RPJMN.

Australia will deliver development assistance in line with the strategic objectives of this Aid Investment Plan, against the performance benchmarks identified. Our activities are designed and managed in collaboration with Indonesian Government counterparts. We have built strong relationships with key economic ministries such as the Indonesian Ministry of Finance, Coordinating Ministry for Economic Affairs, Financial Services Authority, Ministry of Trade, Ministry of Agriculture and Ministry of National Development Planning. We will maintain regular high-level engagement, such as the annual Senior Officials' Meeting, where we can review our individual and collective obligations, discuss emerging issues and target areas of underperformance.

Australia's ODA funding, while substantial, represents a small fraction of Indonesia's budget. Therefore, it will be important that Indonesia continues to provide the political momentum and economic support to implement its own development priorities, and to build on proven approaches supported through the development program. We will ensure the sustainability of our investments through strategies that foster ownership by government, private sector and the community. Sustainability strategies include co-funding arrangements, appropriate use of local systems, broad stakeholder engagement and proactive transition planning. These strategies will be carefully monitored to ensure that positive changes in budget allocations, systems, behaviours and development outcomes endure after program activities have ceased.

Monitoring, review and evaluation

Across all investments, we will continue to take responsibility for generating credible information, and using it for accountability and good program management. Staff will actively monitor programs, communicate robust performance management standards to contractors and partners, and ensure their products (such as investment designs, evaluations, and progress reports) meet these standards. Managers will take responsibility for synthesis and use of credible information in decision making through purposeful scoping of evaluation terms of reference, and proactive management responses to their recommendations.

To date, the Indonesia program's efforts in measuring performance have focussed on the outputs and impacts at investment level. While monitoring these outputs will continue to be important, we will also demonstrate the cumulative effect and broader significance of their achievements.

As part of the AIP, DFAT has selected Indonesia Program Country Goals that will correspond with and be measured against the three objectives and be connected to investment outcomes. These goals represent the program's contribution to both Australia's national interest in the bilateral relationship, and also an alignment with the development priorities of the Indonesian government.

The country Level Goals for the Indonesia aid program are:

- Improved performance of public economic sectors and increased access to infrastructure
- Improved education and health outcomes
- Improved performance of public institutions through participation of civil society and citizens

We will use the monitoring and evaluation information generated for each of the investments in the aid program and assess the cumulative impact and performance of these against the goals. We will also use this cumulative assessment exercise to judge the effectiveness of each initiative and the quality of the performance data each is contributing. In addition, we will test that our interventions represent value for money, and that we are adapting to changes in context and where we are achieving quality outcomes.

We will report progress against country objectives in annual Aid Program Performance Reports (APPRs). APPRs will include recommended actions to the program management team based on progress implemented as a result of previous APPR, as well as new challenges and proposed responses. Consistent with past practice, we will rigorously moderate our aid investment quality reporting. The independent reviews of larger investments will complement our own routine monitoring and assessments. Related performance and financial information will also guide regular discussions with the Indonesian government about our partnership.

Program management

Governance and resource management

Australia's economic partnership with Indonesia will be managed by the Australian Department of Foreign Affairs and Trade (DFAT) in Jakarta and Canberra.

Overall responsibility for aid policy, strategy and the divisional aid budget will lie with DFAT's First Assistant Secretary (Southeast Asia Maritime Division), while the Head of Mission (Jakarta) will have responsibility for the leadership of the development relationship and for the delivery of the bilateral aid program.

We will maximise flexibility in the use of human resources across Canberra and Jakarta so that we can deliver a highly effective and efficient program.

Appropriate levels of funding will be made available to design and evaluate new initiatives, in addition to the direct implementation costs. Developing, implementing and evaluating aid investments requires highly skilled staff. We will maximise our capability through integrated and flexible use of resources and by investing in staff training and development.

Risk management

The highest order risks and mitigation measures are outlined below.

In Indonesia some places where we operate are identified as having high security risks due to potential terrorism, civil unrest and political tension. Aid program activities, including staff travel, are subject to security risk assessment and security risks to aid investments are monitored at the country program level and treated accordingly. External shocks such as natural disasters could also have a large impact. While these events may be beyond our control, we will retain flexibility in our program to help ensure we can provide emergency assistance when needed.

The highest risks of policy non-compliance in Indonesia are in the areas of fraud and child protection. A number of fraud cases have been reported in aid program activities and fraud case management has senior management oversight at post and in Canberra. The strategy to protect Australian Government aid funds in Indonesia sets out sound mitigation and prevention actions to manage fraud risk. The DFAT Child Protection policy is embedded in routine aid investment program management. Training in fraud control and child protection is conducted regularly for DFAT staff and implementing partners.

Reducing the size and focus of the aid program could potentially impact on the Australian Embassy's reputation, influence and access to the Government of Indonesia and relationships with implementing partners. We will maintain close engagement with the Government of Indonesia, particularly with Bappenas, and implementing partners. Senior management will also closely monitor the impact of these changes on staff turnover and morale and take appropriate management actions when necessary.

Risk monitoring and communication

Process	Frequency
Update of country program-level risk register	Quarterly
Update of sector-level risk registers	Monthly
Senior management team discusses progress of risk treatments, escalation of country aid risks and any new risks	Monthly