Proposal for Scale Up and Extension

National Program for Community Empowerment (PNPM)

March 2013

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I. Introduction & Overview

Indonesia's strategy for poverty reduction has evolved considerably since the fall of the New Order. Prior to 1998, Indonesia's basic strategy could be summarised as macroeconomic stability for growth, support for food price stability and the mass construction of basic infrastructure and service facilities. This strategy produced spectacular results for 30 years, although by the tail end of that period there were already clear signs of diminishing returns.

Since the end of the New Order there have been three factors that provide the landmarks for the next generation of thinking about poverty. First, the East Asia crisis and the various global and national events that followed it drove home the importance of a strategy that focused on helping the poor handle shocks rather than just increase their incomes. Second, Indonesia is richer. Most of Indonesia's 'low hanging fruit' on the poverty front have already been picked. The country can now afford to think about institutionalising poverty programs built around predictable transfers rather than mass building campaigns. And third, senior decision-makers as much as international analysts have come to recognise the political and institutional challenges that accompanied the fall of the highly centralised New Order. Democracy, decentralisation and the breakup of Indonesia's command and control-based bureaucracy poses both opportunities and constraints. The past ten years have forced close scrutiny of how poverty programs can work effectively within an entirely new institutional order.

Starting in 2007, the Susilo Bambang Yudhoyono government charged its newly formed National Team for Accelerating Poverty Reduction ('TNP2K') with designing a budget and policy-based strategy for reducing poverty that could be presented to parliament by 2014 and would form the poverty pillar of the government's long term development plan. The government was committed in principle to providing as much as 5% of GDP to supporting these programs – a sum that is potentially as large as AUD$15 billion per year, nearly a 300% increase over its 1997 levels. TNP2K was to not only provide a strategic vision for the strategy. For the first time, a high level poverty commission was tasked with carrying out evidence-based analysis and empirical reviews of what would be needed to improve the efficiency and coherence of the existing poverty programs and where whole new types of programs would need to be designed, trialled and introduced at scale.

In order to make this complex assignment manageable, the government's conceptual framework for managing the targeted poverty programs grouped them into three categories, or Clusters. Cluster 1 programs conform more or less closely to global definitions of social protection – the household transfer programs that help poor families stabilise expenditure, resist shocks, and guarantee that they can meet minimum household needs. Cluster 2 is the programs under discussion in this paper. They are Indonesia's programs for creating community assets through block grant transfers to subdistrict and village planning councils, to be invested in small-scale economic and social infrastructure. While community programs are not normally considered to be part of social protection, Indonesia already had a long experience of using these programs successfully to cope with the East Asia financial crisis, the Aceh tsunami, and other such shocks. Cluster 3 consists of programs that provide

microcredit and support to small and medium enterprises. Programs such as these are also not normally considered to be social protection under global definitions, but they again reflect the government's view that their policy interest is to identify a diverse set of mechanisms that will help them deal with shocks and vulnerability across a still largely rural, diverse, and poorly connected population, not solely with the establishment of labour-market inspired social safety nets.

This project paper is concerned with the middle group of poverty programs, the community based block grant transfers. Indonesia's National Program for Community Empowerment ('PNPM') is the single largest poverty program operating in Indonesia. Built out of some thirty years of experience designing community-driven infrastructure programs[1], PNPM was formed when Indonesia's president announced in late 2007 that PNPM would become the backbone for the government's approach to community development. PNPM's scale-up was to be backed by the PNPM Support Facility (PSF), a multi-donor trust fund managed by the World Bank and co-chaired by the Coordinating Ministry for People's Welfare and by Bappenas, Indonesia's national planning board. Since 2009, AusAID has been a leading supporter of PNPM, providing AUD$215 million to support the program's national scale-up. That goal has been achieved: PNPM now reaches around 76,000 villages, including rural and urban sites.

This proposal addresses the Government of Indonesia's (GoI) formal request for additional support to PNPM. GoI is now producing a road map that will embed PNPM in the long-term budget. AusAID's review of PNPM's performance to date confirms the success of the national scale-up, but it also identified several areas where GoI management systems continue to struggle and where adjustments to the PNPM main program could yield significant increases in the program's effectiveness. AusAID's support to that road map will strengthen the program's management and improve its effectiveness at reaching the poor and highly vulnerable.

Box 1: Snapshot of PNPM Scale Up

Expenditure:	$314 million
Duration:	6 years (2009/10 – 2014/15)
Goal:	- To contribute to the improved management and effectiveness of the Program - To assist the GoI define and execute a strategy for Cluster 2 – Community driven development programs – that embeds the program in the Indonesian planning and budgeting cycle
Philosophy :	Support for better management; reducing GoI's risks when innovating; and promoting the incorporation and scale-up of activities that support better local-level governance and social inclusion
Activities:	Technical assistance, scale up of pilot programs, new pilots, evaluations + studies
Beneficiaries:	40 million
Vehicles:	PNPM Support Facility (PSF), Poverty Reduction Support Facility (PRSF) and AusAID Direct

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[1] PNPM draws heavily on the World Bank assisted Kecamatan Development Project, which was launched in 1998 and was the basis for the 2007 scale-up of PNPM. Several of the data measurements used in this project paper include data from KDP, and are labelled accordingly. Because PNPM included no significant technical or design changes from KDP, including KDP data allows for longer-term assessments of issues such as impact, sustainability and so on.

Australia's current commitment to PNPM is $215 million over 5 years (2009/10 – 2013/14). Based on a formal request from Bappenas, this strategy proposes an increase of $99 million, taking the total commitment to $314 million over 6 years (through to 2014/15). This time frame covers the production of the government's PNPM road map, that will install PNPM in the regular government budget, and, it provides support for the first two years of implementing the road map strategy by the new government that will take over from the SBY presidency in 2015.

This project proposal is divided into five sections. This introduction is followed by an analytical review of PNPM's performance to date. The third section of the proposal presents the issues that must be addressed by the government's PNPM road map, the long-term plan for putting PNPM into the regular budget and using PNPM as the community platform for poverty service delivery. Section Four describes how AusAID's contribution will be used and what particular advantages are attached to AusAID's joining the national program. The fifth, final section focuses on the proposed implementation arrangements, the project's risk assessment, and the plans for assessing and attributing the benefits from AusAID's contribution. The paper concludes with a recommendation for financing.

II. Assessing PNPM's performance

PNPM's overall objective is to reduce poverty by promoting community participation in development planning and management. Its core idea is that given adequate information and some technical assistance to improve designs, communities will negotiate a range of cost-effective, economically useful investments that will raise local productivity and benefit the poor. To translate this idea into an operational project, PNPM funds are used to support: (a) building community capacity for the formation and institutionalisation of elected representative organisations that are accountable to communities; (b) provision of grants to communities directly and transparently to finance an open menu of poverty alleviation activities; and (c) enhancing the capacity of central government and local governments to partner with community organisations.

The whole PNPM program now covers 6,703 sub districts with an annual budget of approximately $1.7 billion (2011). The program continues to perform well despite some of the implementation challenges that the program has faced in its speedy scale up to national coverage and which are discussed further, below. PNPM Rural, the largest of the PNPM programs, constitutes approximately 80% of the total budget and operates in approximately 63,000 rural villages.

PNPM has benefitted from a comprehensive system of results measurements. The first step in assessing the program's performance is to summarise how the funds were spent. Table 1 summarises the physical outputs from the program's community investments.

Table 1: PNPM/KDP Outputs 1998-2011

Type of sub-project	KDP/PNPM-Rural (1998-2011)
km of farm/rural roads built	109,192
# bridges built	17,191
# irrigation systems built	17,589
# clean water systems built	40,782
# public toilets and washing facilities built	20,923
# school buildings built or rehabilitated	28,587
# health facilities built or rehabilitated	14,704
# village electricity units built	2,243
# education activities supported	244,427
# health activities supported	2,338
# women's revolving loan funds supported	301,003

Several peer-reviewed quantitative assessments have measured the extent to which these investments translated into effective, attributable poverty reduction. Key findings confirm that:

- Benefits are heavily skewed to the poor, with the two lowest quintiles of the participating population receiving the largest share of project benefits.

- Benefits are significant. Household expenditures among the poor increased by an average of 11% as a result of project investments, benefitting approximately 40 million poor people.

- Benefits are sustained. Physical assessments of infrastructure built by PNPM and its predecessor the *Kecamatan* Development Program (KDP) found that 85% of the infrastructure built by communities was in good to very good condition five years after its completion. Impact simulations found that after three years the majority of benefits came from increased economic activity attributable to the investments made by the program, not from project grants.

- Benefits are shared. Labour composition in PNPM programs averages 40-70%, which is on the high end of global measurements. PNPM created over 20 million person-days of paid employment. PNPM's focus on financing public rather than private goods ensures that investments benefit a broad range of poor people.

- Investments are efficient. Simulations and re-costings found that infrastructure built by communities was 40-60% cheaper than building it through normal government systems. In a program as large as PNPM, a 40% saving on infrastructure cost represents a very large sum that can be freed up for other development purposes.

Several evaluated pilot programs and targeted studies carried out under PNPM identified useful opportunities for improving the program:

- A randomised, controlled evaluation of the $45 million community based conditional cash transfer called 'PNPM Generasi', supported by AusAID funding, found large, significant benefits to the poorest quintile as measured by critical indicators for infant mortality, child nutrition and stunting, maternal health, and educational enrolment. This pilot will now be scaled up.

- Another randomised controlled trial found that increasing the frequency of audits from 5 to 20% and modifying the audit procedures to include community presentations of audit findings would produce significant drops in corruption and leakage. This finding was incorporated into the program's audit procedures for 2011.

- A pilot program for micro hydro development and natural resource management ('Green KDP') built over 200 community run, technically sound facilities for generating electricity that included management and cost

recovery systems in communities that otherwise would not have received electricity. This pilot will be extended.

- PNPM pilot programs for social inclusion, of which the most familiar to AusAID is the support program for female-headed households ('PEKKA') have been generally successful, and the program has been relatively open to proposals for expanded coordination with poverty focused civil society groups.

- A quantitative summary of a pilot to use cultural performances in areas of high poverty incidence and high rates of illiteracy found order of magnitude improvements in the participation of the poorest villagers if support for cultural media were included in PNPM's procedures.

Not all of PNPM's evaluation results are so positive. Of concern are:

- Quantitative evaluations found little sign of systematic spill overs from PNPM's participatory planning procedures into other domains. PNPM's high rates of women's participation (>35%) in particular did not turn into changed roles for women in other programs.

- Recent evaluations suggest a falling off in returns to PNPM investments in wealthier sub districts, where issues of access to existing facilities are more likely the binding constraint on poverty reduction than further investments in additional infrastructure.

- With some exceptions, line agency programs did not use PNPM procedures to deliver technical services. PNPM priorities did not successfully enter the government's general development planning and allocation process.

- PNPM's revolving loans to women's groups, which account for approximately 20% of the program, are not sustainable in the long-term and do not go to the poorest of the poor. Ongoing studies are assessing indirect poverty benefits (i.e. do community loan beneficiaries hire the poor).

- Over time the community planning process is susceptible to elite capture.

Qualitative and monitoring reviews of PNPM also point to several areas where PNPM's implementation performance has been unsatisfactory. Most of PNPM's weaknesses have to do with the size of the program and the weak or inadequate systems that the government is able to use to manage it. They include:

- Overlapping and unclear mandates between government staff and technical consultants

- Out-dated systems for information management
- Breakdowns in the planning, budgeting, and feedback cycles
- Overstretched operational staff caused by inadequate HR planning and management
- Lack of adequate supervision and oversight by government staff
- Unclear accountabilities for local government performance
- Unwillingness to enforce sanctions

Other implementation issues include:

- Decentralisation to local government has not been successful. A first attempt in 2009 to devolve responsibilities to provincial and state authorities did not take into account political economy risks such as elite capture, corruption, and political intervention. As a result, procurement and oversight responsibilities were pulled back to the centre in 2011. While decentralisation is government policy, PNPM's future devolution will need to follow a more sequenced and measured path.

- PNPM relies heavily on its Management Information Systems (MIS) but these were not up to the challenge of the national scale-up. Management information is increasingly delayed and unreliable.

- PNPM's potential to respond to situations of disaster and post-conflict recovery is hampered by rigid procedures for budgetary revision and approval. GoI has tried several times to improve the program's responsiveness given its national presence, but progress has been slow.

AusAID's current and proposed future support aims to address many of these deficiencies. AusAID will continue to support GoI to manage PNPM through the provision of technical assistance and by supporting the complete redesign of PNPM's MIS. AusAID is supporting a program to improve the sustainability of the revolving loans fund, and another to help reach the poorest and most marginalized members of Indonesian society.

The main achievements of AusAID's current support include:

- ***Assisting the GoI scale up PNPM Rural to National Coverage.*** AusAID has assisted the Government of Indonesia scale up PNPM Rural to its current coverage of approximately 63,000 villages across the country. AusAID's emphasis has been on strengthening key systemic issues within the central management team, such as procurement, fiduciary oversight, facilitator training and human resource management. While achieving national coverage is a significant achievement in itself, challenges remain with ensuring that the appropriate systems for planning, implementation and oversight are in place to manage a program as large as this, and that the teams responsible for managing the program are resourced well and are capable.

- ***Doubling the Coverage of PNPM Generasi.*** PNPM Generasi began in 2007 as a pilot program to address Indonesia's lagging health and education MDGs. With AusAID's support, the program has scaled up from 1,605 villages across five provinces in 2007 to 3693 villages across eight provinces in 2012. The Generasi program continues to show significant improvements to the lives of pregnant women and children in the health and education indicators in which the program targets. Findings from a three wave randomised impact evaluation conducted from 2007 – 2010 found that Generasi had a statistically significant positive impact across the twelve indicators it was designed to address with a long-term impact on malnutrition rates[2]. The evaluation also found that Generasi had the greatest impact in areas with low baseline health and education indicators, a finding that has now become a key criterion for program scale up. AusAID support allowed the GoI to scale up program coverage that otherwise would not have been possible.

- ***Supporting a new pilot program to improve the revolving loan fund component.*** AusAID has supported the development of a new pilot that is currently working with 507 small loan management units servicing 5000 revolving loans groups (approximately 50,000 borrowers) across four provinces. The pilot is aimed at linking poor women to the formal financial sector and making improvements to current fund operations. The revolving loan fund operation continues to be of significant interest to the Vice President's office and discussions are ongoing regarding options for the poor to access financial services. A number of in-depth assessments of the borrowers and the sub district fund management units have been conducted during this period and will contribute to the future direction of this component. Dialogue is also underway with a range of commercial banks on possible opportunities and linkages. Results from these, together with results from the legal review (ongoing), will inform the future direction of not only this component of work but for the broader policy on financial inclusion.

- ***Assisting GoI to develop key policies.*** AusAID funded advisory support has been integral to a number of high level policy and program reforms including: the draft concept for the future of PNPM that is being led by TNP2K, to be presented to Vice President Boediono, the PNPM Road Map which outlines key design directions through to end 2014, input to the formulation of the Master Plan for Poverty Reduction through to 2025 (MP3KI) being led by Bappenas. AusAID technical experts now work with the central policy and management team of PNPM Rural which extends across the Vice President's office and three central ministries including the Coordinating Ministry for People's Welfare, Bappenas, and the Ministry of Home Affairs.

- ***Financing quantitative and qualitative evaluations that provided input to new policy and programming.*** PNPM operates an extremely advanced program of results measurement through the PSF, a multi-donor fund managed

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[2] See Benjamin A. Olken, Junko Onishi, and Susan Wong, 'Should Aid Reward Performance? Evidence from a field experiment on health and education in Indonesia' *National Bureau of Economic Research Working Paper*, Paper No 17892, March 2012. Paper is available at http://www.nber.org/papers/w17892 .

by the World Bank to which AusAID is the largest contributor. PNPM's strategic evaluation program is reviewed by the PSF's Joint Management Committee, which is chaired by Bappenas and the Coordinating Ministry for People's Welfare. It combines rigorous quantitative and qualitative evaluation designs for measuring PNPM impacts. Topics covered that have been peer reviewed and can be found in professional publications or on publically available websites include:

- Poverty impact assessments
- Targeting assessments
- Sustainability of PNPM infrastructure investments
- Economic efficiency of PNPM investments
- Gender reviews
- Randomised evaluation of PNPM Generasi
- Randomised evaluations of anti-corruption regimes
- Evaluations of counterpart local government matching grant programs
- Anthropological studies of local level institutions

- ***Redesign of PNPM's Information Management System.*** At the request of the GoI, a total overhaul of PNPM Rural's Information Management System is currently underway. With AusAID support, a new system is being designed, and will provide the GoI with a simplified yet comprehensive information system that will be able to generate timely and accurate information for program reporting and decision making.

- ***Strengthened Systems for Facilitator Training and Performance Evaluation.*** Facilitator training modules, management guidelines and a system for evaluation of facilitator performance have been developed by AusAID-funded advisers. These modules will be used for the 16,000 PNPM program facilitators nationwide. Australia has also supported the establishment of a Professional Certification Institute for Community Facilitators. This will serve as a formal certifying institute for community facilitators nationwide, beginning with PNPM facilitators. The Institute has high-level GoI backing and was formally launched in late 2012.

III. TNP2K and the 2014 PNPM Road map

TNP2K has prepared a first draft of the road map and action plan for PNPM. This action plan lays the foundations for guiding PNPM through 2014 and for the regulatory and management systems that an incoming government will need to sustain community development through the budget[3]. Its key objectives are to provide a

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3 First drafts of the Master Plan for Acceleration of Poverty Reduction (MP3KI) include a PNPM-like program.

coherent policy basis for the extended PNPM program, to integrate PNPM into normal government systems, and to provide a sustainable financing basis, and to define a set of financing instruments to sustain the program. This package will be presented to Indonesia's parliament for endorsement in 2014.

There are a number of key directions in the road map that should result in significant impacts and improvements to PNPM. Firstly, the road map proposes to consolidate several programs using the community driven development model ending the current proliferation of individual projects and replacing them with a single, policy-based program for community transfers. Under this proposal, all line agencies will use the consolidated, multi-year village plan developed using PNPM's participatory planning approach as the basis for locating village-level sectoral services. Secondly, the road map proposes to identify a set of core criteria applicable to all PNPM programs but then allowing provincial and district governments to adapt the design to local needs and circumstances. A franchised approach that agrees on a core rule book but then allows for local adaptation will let PNPM targeting reflect local configurations of poverty and social structure. Thirdly, the road map provides a greater role for sub national governments. Embedding PNPM in local governments opens the door to better linkages between community planning and district level service delivery. Fourthly, TNP2K is beginning to look at cross-program synergies, such as using PNPM meetings as a forum to validate the accuracy of the social safety net eligibility lists. Finally, the road map team will be cooperating with the Ministry of Finance to identify the range of possible financial instruments that can continue PNPM's system of direct community transfers.

This overall strategy is what provides guidance to AusAID's scaled-up support to PNPM. AusAID's decision criteria for allocating its PNPM funding will continue to be support for better management, reducing GoI's risks when innovating and promoting the incorporation and scale-up of activities that support better local-level governance and social inclusion. Successful interventions will be scaled up. Decisions on activities and funding will be made together with GoI and other development partners supporting PNPM to ensure a coherent and coordinated approach and to ensure that interventions are in line with GoI priorities. Preliminary discussions on this proposal with AusAID's development partners and with GoI are already well advanced, with the proposed areas for support being viewed positively.

Key Policy Issues - A number of key policy questions that must be addressed through the road map development process are still being discussed. AusAID support will help the government assess the options and trade-offs involved, improve and monitor the quality of implementation, and, enable the government to carry out high quality evaluations so that it can make policy decision based on empirical evidence.

- *National program coverage versus targeting the poor.* The issue of national versus targeted program coverage for PNPM is an ongoing debate within GoI. Results from a number of impact evaluations of the PNPM Rural program show that PNPM has greater impact on poor households in poor areas[4], raising the question of whether the program should be targeted to poor areas only. GoI

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[4] Findings, PNPM-Rural Impact Evaluation, 2012, available at http://pnpm-support.org/sites/all/sites/default/files/PNPM+IE+Final+REVISED%20done.pdf

has publicly committed to support national coverage of the program through to the end of 2014. The trade-off under discussion is whether to reduce coverage to the bottom third of the country's sub districts – still a huge number – or whether to retain national coverage but with a differentiated model that can more effectively reach the many poor people who live in the upper strata of sub districts. This is a key topic to be addressed going forward.

- *Decisions on central versus regional budget allocations.* The financing instrument and the co-financing arrangements for central and regional budget allocations are yet to be determined for PNPM post-2014. However, it is likely that a co-funding arrangement will be proposed, with the central and regional budget[5] both contributing to the block grant. As the financing policies become clearer, the Ministry of Finance (MoF) will need to develop appropriate financing instruments, counterpart financing requirements, sanctions protocols and financial monitoring indicators, auditing mechanisms, and tracking instruments. Determining appropriate budget allocations and the financial instrument for fund transfers post 2014 is a key piece of work to be conducted by the team.

- *Entry criteria for transferring responsibilities down to sub national levels.* The entry criteria for districts to take on a greater role of the management and implementation of PNPM are yet to be finalised. It is likely that the central Government will maintain responsibility for overall program strategy, monitoring and technical oversight, audit and the procurement of sub national advisers. Sub national governments would prepare their own operating manuals appoint provincial management and oversight groups and be required to provide a matching grant. This decentralised model would accommodate varying levels of capacity and local government readiness to take on a greater role of the program.

- *Normalising PNPM into district government planning.* At present PNPM's planning procedures and budgets operate largely outside of normal district planning process. The benefit of this has been the relative integrity and transparency of community management and the cost has been that most (though not all) other government programs do not coordinate with PNPM planning or management procedures. The government now wants to change this, both by mandating that all government community programs use the PNPM platform, and by finding ways to stimulate the encounter between community priorities and district government suppliers. There are a number of practical barriers that can be removed through the road map process, but there is also a large body of regulatory issues that will require clarification and follow-up. Experience from PNPM Generasi, where for the first time health and education 'suppliers' had direct encounters with the PNPM planning system, shows that achieving this policy objective will require hands-on investment in pilot programs and other mechanisms to create 'facts on the ground'.

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[5] It is likely that the regional budget allocation will be in line with regional fiscal capacities.

- ***How to promote spill overs from PNPM's participatory planning into other development programs.*** Global reviews of community development programs shows that while more participatory planning by the poor can be achieved through programs like PNPM, turning project-based participation into normal practices is rare and how to make it succeed is not yet well understood. Nevertheless, GoI is firmly committed to this objective. A preliminary hypothesis is that most community programs do not include the regulatory and fiscal alignments that GoI is proposing to develop through the road map. AusAID will target support to MoF, Bappenas, TNP2K, Ministry of Home Affairs and relevant local governments to produce the appropriate regulations and government staff training programs, with a particular emphasis on carrying out careful evaluations of which interventions stimulate spill over.

IV. Proposed AusAID Support to PNPM

The overall purpose of the proposed support is:

1. To contribute to the improved management and effectiveness of the national program.

2. To assist the Government to define and execute a strategy for Cluster 2 – community driven development programs – that embeds the program in the Indonesian budget and planning structure.

The scale up will be implemented over a 3 year period (FY 2012/13 – 2014/15) at an estimated value of AUD 99 million (detailed budget below). The program will continue as originally planned through to end of FY 2014/15. The scale up will include a mixture of new areas of focus as well as the scale up of areas from the original program design. It is intended that this package of support build on the successes and lessons of the current program.

AusAID's incremental support to PNPM will cover the following components:

- ***Strengthening government management*** – A key element of making the road map operational will consist of strengthening government management. The government is aware of the issues summarised in Section II, and actions are being taken in each of these priority areas. However, in several of these areas, government budgeting and procurement restrictions limit the speed and efficacy of their ability to respond to problems. Australian assistance will be critical for ensuring that problems such as these get addressed as the program consolidates and become embedded within GoI's normal development management practices. AusAID will also be involved with developing the systems for certifying and monitoring local governments as functions are transferred to them through the road map.

- ***Improving PNPM's accountability and governance*** – PNPM has under-invested in governance training and community monitoring of overall program performance. GoI has made some positive noises about wanting to work more closely with NGOs, but it is still a long way off from using its own budgetary resources to do this, nor could very many NGOs survive the Indonesian budget system. This component will make a significant investment in a consortium of NGOs who would train government facilitators and sub district management groups. It will also support NGOs to strengthen the role of communities in the monitoring of the program and establish a robust mechanism for providing feedback to the public on program performance and on other development issues such as information on health and education services. This component will be executed by both AusAID and PSF.

- ***Increasing the participation of the poor and marginalised*** – While PNPM reaches a significant number of Indonesia's poor, many, including a number of marginalised groups, are not being reached. These groups include those living

with HIV, widows, people living with disabilities, unemployed, victims of domestic violence etc. This component will scale up the PNPM Peduli program, which is implemented by the PSF, to allow for increased program coverage of such groups. Innovative approaches to increase community participation in PNPM such as the use of cultural activities will also be supported under this component building on the programs successes in increasing participation of the poor in PNPM meetings. This component will be implemented by the PSF and will work primarily through CSOs already experienced with working with these groups.

- *Maintaining PNPM infrastructure* – At present Indonesia has no system in place to maintain infrastructure built by PNPM or other village programs. At the same time, evaluations have shown that while routine maintenance can be performed by communities using voluntary labour, heavier maintenance that requires replacing pipes, hiring machinery or other capital expenditures is simply beyond the capacity of poor communities.[6] Adding a district-level maintenance window that communities bid on would be even more efficient than introducing a full transfer because it would provide concrete incentives for local government engagement. GoI has included this pilot in its 2012/13 work plan.

- *Support to PNPM Respek* – PNPM Respek is Papua and West Papua's local adaptation of the PNPM program. Significant challenges face the PNPM Respek program. Villages are remote and human resources limited. The ability to retain trained staff is difficult. A number of programs promoting the 'barefoot approach' (intensive training courses for Papuan school graduates) have proven successful to skill up local facilitators in a relatively short time frame. This component will provide targeted support to the PNPM Respek program to support the scale up of such trainings, as well as support to overall program management and implementation, including greater analysis into some of the key issues facing implementation a large community poverty program in a geographically challenging area. This component will be implemented through the World Bank managed PSF but also work closely with AusAID's Australia Indonesia Partnership for Decentralisation program.

  Support for Green PNPM expansion – Green PNPM is now operating in eight provinces across the country supporting activities with a focus on micro hydro power, environmental conservation and renewable energy. To date 2,243 sub-projects have been implemented across these eight provinces ranging from tree planting/seedling for conservation, micro hydroelectricity to households and communities. Green PNPM has been received well in participating communities but implementation has been challenging, with a lack of technical expertise community understanding in a number of areas. GoI and donors are becoming aware of the need to revisit elements of the design of Green PNPM to foster greater community ownership of the Green agenda and ensure that the program aligns with PNPM Rural to deliver positive environmental and socio-economic outcomes in village development.

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[6] Community cash flows and their implications for infrastructure maintenance were exhaustively reviewed in the 2009 VRRI study.

GoI and donors alike are also recognising the role Green PNPM has to offer in answering a number of questions on implementation mechanisms for the community components of Reducing Emissions from Deforestation and Forest Degradation (REDD+) programming. The implementation team is now reviewing the approach and design of Green PNPM to address these factors. A draft concept note has been prepared by the PSF and AusAID has already been consulted on this.

- *Point of Payment Pilot Program* – This proposed pilot fits into the general diagnostic that in the poor, remote communities of Indonesia a critical constraint on poverty reduction are the high levels of absenteeism. However, rather than addressing absenteeism from the 'supply' end, this pilot proposes an innovative way to use 'demand' to deal with absenteeism. With distances introducing major costs for regular monitoring from the central district office, communities could play an important role in providing oversight in remote schools. The 'point of payment' pilot will work with PNPM to test whether community-based school and clinic management can reduce absenteeism and, by doing so, improve the MDG achievements of poor children living in isolated areas. Its key mechanism for reducing absenteeism will be to transfer responsibility for paying a portion of teacher and nurse salaries and benefits to a village school committee that is registered and overseen by the Ministry of Education or Health, respectively.

- *Demonstrating Results* – AusAID will continue to support a strong program of analysis and evaluation. The specific list of studies will be driven by the design of the final PNPM road map and AusAID's country priorities, but studies and evaluations that are currently being pulled into the scale up of the analytic work plan include:

  - Maintaining the panel for poverty impact evaluation
  - Pilot programs to maintain assets built by the program
  - Mapping gaps in village infrastructure
  - Experimental interventions to improve poverty service delivery
  - Randomised evaluations of community-based poverty targeting and verification
  - Poverty returns to livelihood programs (including pilots to promote formal sector employment)
  - Surveying the effects on people with disabilities from the PNPM Generasi program

- *Support for planning and pilots 2014 and beyond* – This funding line will support GoI in implementing the road map and action plan for PNPM after 2014. AusAID together with GoI will also explore opportunities for innovative options to work on poor people's livelihoods, particularly areas that can be developed in tandem with AusAID's emerging work streams on private sector and rural development.

- ***Support for AusAID corporate activities (such as G20 + South-South Cooperation)*** – Nominated by Indonesia as its contribution to G20 south-south learning, PNPM has a lot to offer AusAID sectoral programs and other AusAID country programs. PNPM has already hosted a number of international visits, including Afghanistan and Timor Leste, as part of South-South cooperation and learning. This component would ensure that learning exchanges of this type continue. Support for cross program and cross sectoral work, such as incorporating and mainstreaming Australia's disabilities strategy, HIV, disaster risk reduction, and gender would also be supported from this component.

Table 2: Proposed AusAID Support to PNPM (AUD)

| Components	2013/2014	2014/2015	TOTAL
On-going components			
Component #1 TA for PNPM	1,000,000	2,500,000	3,500,000
Component #2 Monitoring and Evaluation	1,000,000	1,200,000	2,200,000
Component #3 LG Capacity Development	1,000,000	7,300,000	8,300,000
Component #4 PNPM Generasi	4,000,000	20,000,000	24,000,000
Component #5 Access to Finance	-	5,000,000	5,000,000
Strengthening government management	-	1,000,000	1,000,000
Accountability and governance	2,000,000	2,000,000	4,000,000
Participation of poor and marginalised	6,000,000	6,000,000	12,000,000
Infrastructure maintenance pilot fund	4,000,000	6,000,000	10,000,000
RESPEK	2,000,000	2,000,000	4,000,000
Green	7,000,000	6,000,000	13,000,000
Point of payment pilot	3,000,000	4,000,000	7,000,000
Demonstrating result, pilots and planning beyond 2014	2,000,000	2,000,000	4,000,000
G20 + Cross program learning	500,000	500,000	1,000,000
TOTAL	33,500,000	65,500,000	99,000,000

Implementation Arrangements

AusAID is contributing to an already designed and operational national GoI program. This document presents a single strategic initiative that uses different instruments to support the PNPM program. Like Australia's initial package of support to the program, this package of support will be implemented through three modalities:

1. PNPM Support Facility, a World Bank-managed Multi Donor Trust Fund

2. Poverty Reduction Support Facility (PRSF), an AusAID managed facility

3. AusAID Direct

1. *The PNPM support facility ('PSF')* – PNPM is supported by a World Bank managed multi donor trust fund, which supports the inter-ministerial coordination team and is co-chaired by GoI and the World Bank. Donors contributing more than US$1 million sit on the PSF management committee, which meets quarterly or as needed. Pooling funds through the PSF avoids duplication and also allows AusAID to share oversight costs and responsibilities with other agencies[7].

PSF Funds are utilised through four functional 'windows' (Chart 1), which are:

a.   Through national and district budget co-financing channels (direct support to the PNPM block grant programs).

b.   Through the national budget to support national coordination and supervision.

c.   On-granting to intermediary NGOs and philanthropies that then on-grant to grassroots organisations working on poverty.

d.   Technical assistance to PNPM by donors, such as special reviews, advice and programs commissioned by the Steering Committee and administered by the PSF.

Chart 1

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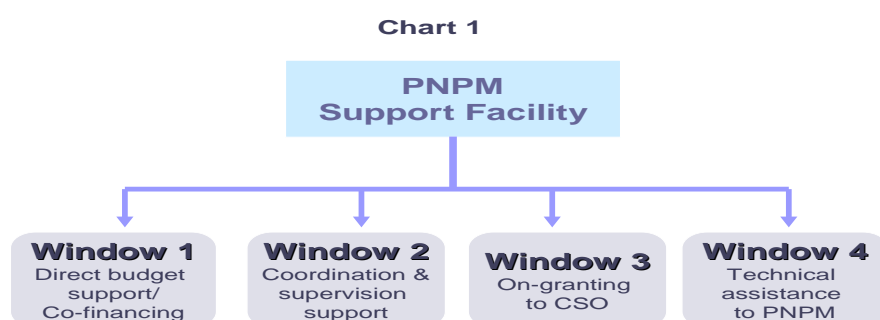
[7] At present donors to the PSF include: AusAID, The Netherlands Embassy, USAID, and the EC. The Millennium Challenge Corporation is also considering contributing to the PSF next year.

To date Australia has channelled $142.850 million[8] through the PSF.

The World Bank provides technical support to the PSF through its social development and poverty teams. At present the government members of the PSF are also requesting the World Bank to manage all PSF procurement. The Bank charges its costs the PSF. AusAID will continue to supervise World Bank oversight for PNPM.

All specific uses of funds from the general budget must be approved by PNPM's joint management committee (the JMC), which is co-chaired by GoI, and then reflected in the PNPM Project Digest. This design recommends that AusAID continue to follow this procedure. There are a number of strong arguments in favour of this approach. First, GoI's track record on the PSF is good. Decision-making has been open and transparent, and by consensus. Experience from the current program has been for the most part positive. As a core member of the Facility, AusAID will continue to retain oversight and veto power. Second, and perhaps most importantly, the approach allows the government to work from an integrated strategy that combines inputs from many donors rather than dealing with one donor project at a time. It is likely that other donors will want to join some of the bigger activities. For example the Millennium Challenge Corporation is planning a large contribution to the Generasi program. A structure that pools funds allows the government to apportion project sites in an integrated way and then just report on incremental outputs. Finally, working through the PNPM system reduces substantially the direct costs to AusAID itself.

For funds transferred to the PSF, AusAID retains the right to join any of the PSF's supervision missions (which occur almost monthly). AusAID will continue to supervise World Bank oversight for the PSF and ensure that findings and recommendations are communicated as part of AusAID-World Bank dialogue.

2.   ***Execution through the Poverty Reduction Support Facility (PRSF) that channels AusAID support to TNP2K*** – AusAID will contract out parts of this work to the PRSF. The PRSF has already been managing the Technical Assistance component for the PNPM team for the current program. Going forward and in line with PRSF's mandate, the PRSF will continue to manage PNPM's TA and any other activities to support cluster two that cannot be implemented by the PSF. As agreed by donors and the GoI when the PRSF was established, the PRSF will only support PNPM activities if and when determined by AusAID and GoI to be a more effective modality for delivery, or, if for some reason the PSF was not an option.

Activities likely to be contracted out by the PRSF include activities under Accountability and Governance and Technical Assistance components, and support to the GoI for planning and pilots for community development post 2014.

Should PRSF not be the best mechanism to channel additional scope under this proposal, AusAID will consider going to market to engage a different managing contractor to deliver the work.

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[8] This figure also includes an additional $10.55million that was contributed to the PSF prior to AusAIDs $215m commitment.

3. ***Direct execution by AusAID*** – is confined to a limited amount of technical assistance where more control is needed; and for selected studies, reviews, and workshops of special interest to AusAID.

AusAID-supported programs such as the Australian Community Development and Civil Society Strengthening Scheme (ACCESS) and AIPD potentially offer useful training for PNPM participants. Where GoI and AusAID identify such opportunities, AusAID would manage these initiatives directly (through the relevant program) or through the PSF or PRSF if deemed more appropriate.

AusAID Resourcing. AusAID is now a key player in PNPM and highly involved in technical policy discussions as well as with implementing agencies on quality of implementation. The current PNPM team consists of 6.5 people. While a large portion of AusAID's support is being channelled through the World Bank managed PSF, the AusAID team engages with the GoI and the World on a daily basis and resources will be required to keep up the level of engagement and oversight that has been employed in the current program of support.

Risk and Risk Management. Program risk can be categorised around three areas. 1) Political (P) 2) Fiduciary (F) and 3) Managerial (M). The risks presented below represent the high level program wide risks. Individual risk management frameworks either exist or will be developed for individual activities and components.

Table 3: Program Risks

Risk	Type	Mitigation Measure	Rating (Low, Medium, High)	Comment
PNPM is used by political parties / individuals as a political campaigning tool for 2014 presidential election	P	AusAID and PSF/WB to ensure that PNPMs evidence base drives policy, program and budgeting decisions at present and in future.	M	It is highly likely that PNPM will become a political campaigning tool for parties in the lead up to the 2014 election
Lack of clarity on key PNPM policy and programming decisions	P / M	AusAID to work closely with TNP2K and the PNPM Oversight Team to ensure clarity of roles and responsibilities and where possible support implementation of respective mandates.	M	A formal division of labour between the two teams has recently occurred (April 2012). A detailed work plan of the two teams is now being prepared.
The PNPM Road Map and future directions for CDD are not evidence based	P / M	AusAID to continue working closely with the GoI and PSF to ensure lessons and an evidence base are the basis for finalisation of the road map and implementation.	L	AusAID to also ensure the PSFs AAA work supports the Road map.
Central level Management does not have the appropriate staff or systems in	M / F	- AusAID and PSF to ensure the program secretariats are resourced well to ensure the appropriate fiduciary oversight	M	This will involve a collaborative effort of PMD, WB/PSF, Bappenas,

place to manage the national program		systems are in place and are functioning. - Regular meetings both informal and formal to monitor progress and agreed actions by team. - Role of AusAID TA to be reviewed regularly.		Menkokesra and AusAID
Sub national Governments take on tasks and roles within program before they are ready	M / F	AusAID to continue close working relationship with the GoI (TNP2K and the Coordinating Ministry for People's Welfare) on timeline for implementation of the road map	M	Potential for AusAID Decentralisation programs to play a role in monitoring this
The PSF / WB is not staffed adequately to provide the appropriate oversight to PNPM	M	AusAID to monitor PSF resourcing and ensure concerns are raised and addressed through appropriate Governance mechanisms (JMC)	L	AusAID may wish to consider adding a clause into its PSF contribution agreement

Corruption. Corruption is a risk to PNPM. Corruption risks are of three types. First, while for the most part PNPM offers none of the rent-seeking opportunities that programs such as natural resource licensing or large scale procurement do, there have been reports of political parties attempting to capture the PNPM machinery in the period leading up to elections. To date the government has reported and acted upon all such attempts. Actions to prevent future attempts include a public awareness campaign and enhanced training for program staff on how to report political interference.

PNPM's second area of corruption risk is in its use of government systems. These risks lie largely in the domain of firm procurement and government payment systems. PNPM's organisational design minimises the number of procurement transactions, and donor support to PSF also increases the Bank's ability to provide the staff needed to monitor financial transactions. By and large these appear to have been effective. As Indonesia develops systems for mobile money it may be possible to largely eliminate this source of leakage.

The third domain for potential corruption risks is in the use of the block grants. Early corruption diagnostics pointed to diversions by local government officials but since the scale-up these have largely disappeared. Instead, the majority of corruption cases now involve either frontline facilitators or else village financial management units charged with managing the revolving funds.

AusAID and the World Bank have worked closely with the government to develop an anti-corruption framework. A full review of PNPM's anti-corruption action strategy has been produced by the PSF and reviewed by the World Bank's Integrity Department. It is updated every six months based on field reviews and discussions

with donors, including AusAID, and it is then posted on the web. GoI is also planning to sign an MOU with Indonesia's respected National Anti-Corruption Bureau (KPK), which has legal powers to investigate and prosecute cases of corruption that involve state funds.

GoI, PSF, and AusAID all maintain a zero tolerance approach to corruption. However, in a program this big it is worth summarising briefly how those principles translate into effective actions and how AusAID plans to strengthen them further. First, in a high fiduciary risk environment like Indonesia, the key principles for fighting corruption are close attention to design, and effective systems for monitoring and reporting. PNPM's fiduciary architecture minimises the number of transactions and the discretion people have to modify terms, both of which are key drivers for leakage. Second, AusAID's support for a comprehensive management information system and provision of fiduciary specialists to the GoI managers allows the government to track cases and monitor responses. Third, allied programs such as the PSF's Justice for the Poor program are providing better protocols for handling corruption cases through the justice system and for helping communities gain access to the legal system.

PNPM's practical experience over the past decade also highlights the system's vulnerabilities. The large majority of corruption cases are discovered and reported by program staff, not by outside monitors. Supportive oversight systems strengthen their ability to detect and prevent corruption, which is why so much of AusAID support is intended to strengthen these systems. Indonesia's judicial system is not at the point where it provided a reliable, consistent mechanism for redress; cases brought to the courts can drag on for years. Finally, corruption risks are, not surprisingly, correlated with the degree of poverty and isolation. Donors such as AusAID can help the government and CSOs extend an oversight presence into areas of high poverty incidence, but the fact remains that these lagging regions are high risk operating environments.

Under this proposal, very little of Australia's support funds are at direct risk. Funds directly executed by AusAID or AusAID contractors all follow AusAID fiduciary standards. Funds executed through the PSF must meet World Bank fiduciary requirements. World Bank field oversight is buttressed through the PSF to standards several times what is normally provided by the Bank to its field operations. Finally, for the areas where AusAID is co-financing pilot programs such as Generasi, donor funds will reimburse rather than finance government payments. This provides a further firewall since any reported qualifications mean that funds do not get transferred to GoI until any queries or qualifications have been lifted.

To minimise risk, donors to the PNPM continue to strengthen PNPM's oversight systems. Under the scale-up program, GoI and the PSF donors are providing increased resources and training for CSOs and other independent monitors who can provide additional surveillance, particularly in the more remote areas where both corruption risks and poverty benefits from PNPM will be heightened. Finally, AusAID supports significantly increased oversight and supervision by qualified auditors and the PSF.

The AusAID team continues to work closely with the World Bank to increase safeguards on funding to PNPM, and undertakes regular reviews and field-based monitoring missions to assess safeguards in operation. In addition, in late 2011, two full-time AusAID funded specialists were appointed to assist the GoI in the fiduciary oversight of the program. A financial specialist was appointed to assist the executing agency of PNPM Generasi (Ministry of Home Affairs) ensure the appropriate fiduciary oversight systems are in place and to provide fiduciary oversight over AusAID funds on granted to PNPM Generasi, while an Anti-Corruption and Good Governance Specialist was appointed to the Coordinating Ministry for People's Welfare, the Ministry responsible for technical oversight of the program nationally.

*Corporate risks and prioritie*s. PNPM builds in a range of safeguard mechanisms, including operating guidelines for dealing with land acquisition, involuntary resettlement, indigenous people, and environmental impacts. These have all been reviewed by specialised units of the World Bank. However, the 'bottom line' for safeguards such as resettlement is that the program does not allow for involuntary land acquisition; a review of 200 districts (50%) found no cases of land acquisition or involuntary resettlement that did not conform to World Bank safeguard policy objectives. Similarly, the small scale of PNPM infrastructure produces few adverse environmental impacts and argues for a mitigation strategy that is built around technical training and oversight.

PNPM has made steady progress towards a satisfactory gender strategy. Its main challenge is that on balance the program achieves less than it could rather than that it does not factor gender into its framework. Key gender considerations adopted by the program include mandatory representation of women in all phases of planning and decision-making, targeted gender training materials and reporting requirements; specialised subprograms for marginal women; and the inclusion of gender in PNPM evaluations. Overall studies have found that women participate in PNPM at rates several times those of other government programs. However, for the proposed scale up PSF has commissioned a gender review whose recommendations will be included in the 2013 program.

The program does not specifically target people with disabilities, however anecdotal reports, including AusAID mission reports, suggest that PNPM Generasi has included activities to help people with disabilities. PSF has recently hired a disabilities specialist to carry out assessments of disability issues as part of a program to increase the program's ability to engage such groups. The AusAID and PSF Generasi team is looking into options for improvement to reporting system to ensure that program benefits to the disabled are captured. To build up Indonesia's Disabled People's Organisations so that they can become drivers for helping people with disabilities benefit from development programs. PNPM Peduli recently approved a grant of $1.2 million to support a program of capacity building, advocacy, and operational engagement.

Measuring Results. PNPM has a sophisticated system for tracking results and impacts. More than 25 studies have already been completed and both the studies and

annual reports, including fiduciary reviews, are posted on publically accessible websites. As in the original program design, it is proposed that AusAID's internal results framework report only on activities funded by AusAID, with all other reporting following the GoI and World Bank's regular reporting processes (annual, mid-term and completion reports).

The PNPM Unit has also developed a tool to assist in the management and monitoring of the current program of support. It will be modified to address the new components of work. The monitoring framework has been developed in line with AusAID's annual reporting requirements and is an effective management and reporting tool for the team.

AusAID Visibility. AusAID support to PNPM is already highly visible, but there are a number of options for providing a more general picture of how AusAID is helping to reduce poverty through PNPM. As the lead donor for Generasi, GoI would promote heightened visibility for AusAID's contribution to this program across all AusAID priority provinces. Having existing AusAID programs such as AIPD, LOGICA and ACCESS cooperate more closely with PNPM will also highlight the overall support that we are providing. The unit has developed a communications strategy for Australia's support. A number of human interest stories have been published and a follow up to the Invisible People book funded by the PSF is being developed at present in collaboration with Lontar foundation. Finally, PNPM's Communication and Information working group, which operates under the Ministry of Information in close coordination with the PSF, can arrange for journalist briefings and site visits to PNPM sites and cooperative visits for the Australian media.

Alternatives. PNPM is the national government's sole Cluster 2 poverty program so beyond an assessment of PNPM's performance in the current phase of AusAID's assistance, no alternative was considered in the design of this proposal. However, several alternative options for delivering the program were reviewed with partners:

- Transferring all of the AusAID funding to PSF would have reduced AusAID's administrative costs. However, the AusAID team has played an active role in strengthening the PSF and overcoming some of the limitations of World Bank HR systems. Transferring all of the funds to PSF would also have reduced AusAID's ability to document and share experiences of PNPM of relevance to other parts of AusAID.

- Only supporting the analytical and technical assistance work rather than co-financing pilots – This option would have significantly reduced the costs to AusAID. However, AusAID's participation allows for a more rigorous evaluation design that would not have been feasible through national budget sources alone. For this reason AusAID co-finances those pilots with the greatest potential to support the Australia-Indonesia Partnership's development goals.

- Not financing the areas of potentially higher risk, such as revolving funds, lagging regions, or government procurement support – AusAID's help with those parts of PNPM that work least well will be reflected in performance measurements and the costs of oversighting the quality of engagement.

Against those costs is the benefit of fixing parts of a much bigger national program that would not have been capable of resolving problems satisfactorily.

V. Recommendation

This proposal recommends that Australia allocate an additional $99 million to 2014/15 to support the PNPM program. This sum will contribute significant benefits to approximately 39 million poor Indonesians who will be able to invest in social an economic infrastructure. In addition, approximately 4 million Indonesians living in provinces of high poverty incidence will demonstrably improve their health and education indicators.

VI.   Additional Website References

PNPM Support Facility
http://pnpm-support.org

Ministry of Home Affairs - PMD
http://www.pnpm-perdesaan.or.id/

National GoI Oversight Team
http://www.pnpm-mandiri.org/