

No.

Ex-Post Evaluation Report of Japanese ODA Loan Projects 2009 (Indonesia II)

March 2011

JAPAN INTERNATIONAL COOPERATION AGENCY

**Mitsubishi UFJ Research & Consulting Co., Ltd.
SHINKO Overseas Management Consulting, Inc.**

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Preface

Ex-post evaluation of ODA projects has been in place since 1975 and since then the coverage of evaluation has expanded. Japan's ODA charter revised in 2003 shows Japan's commitment to ODA evaluation, clearly stating under the section "Enhancement of Evaluation" that in order to measure, analyze and objectively evaluate the outcome of ODA, third-party evaluations conducted by experts will be enhanced.

This volume shows the results of the ex-post evaluation of ODA Loan projects that were mainly completed in fiscal year 2007. The ex-post evaluation was entrusted to external evaluators to ensure objective analysis of the projects' effects and to draw lessons and recommendations to be utilized in similar projects.

The lessons and recommendations drawn from these evaluations will be shared with JICA's stakeholders in order to improve the quality of ODA projects.

Lastly, deep appreciation is given to those who have cooperated and supported the creation of this volume of evaluations.

March 2011

Atsuro KURODA

Vice President

Japan International Cooperation Agency (JICA)

Disclaimer

This volume of evaluations, the English translation of the original Japanese version, shows the result of objective ex-post evaluations made by external evaluators. The views and recommendations herein do not necessarily reflect the official views and opinions of JICA. JICA is not responsible for the accuracy of English translation, and the Japanese version shall prevail in the event of any inconsistency with the English version.

Minor amendments may be made when the contents of this volume is posted on JICA's website.

JICA's comments may be added at the end of each report when the views held by the operations departments do not match those of the external evaluator.

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Indonesia

Ex-post Evaluation of Japanese ODA Loan Program
First, Second, Third and Fourth Development Policy Loans (DPLs)

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1. Program Description



The Republic of Indonesia



Feedback Seminar

1.1 Background

In Indonesia, macroeconomic stability has been a matter of highest priority in the wake of the Asian currency crisis in 1997. An array of reforms such as fiscal rehabilitation, were implemented under the International Monetary Fund (IMF) program and the World Bank/Asian Development Bank (ADB) program. The IMF program was completed at the end of 2003. Subsequently, Indonesia unveiled an economic reform policy (so-called White Paper) and carried out: (1) reduction of government debt to GDP ratio below the level of 60%; (2) financial sector reform; (3) improvement of public finance administration; and (4) strengthening of the foundations for a better judicial system. President Susilo Bambang Yudhoyono, who took office in October 2004, expressed his intent to implement further reforms.

Furthermore, in dialogue with the World Bank and the government of Japan, the government of Indonesia expressed its intent to implement policies for: (1) promoting macroeconomic stability; (2) improving the investment climate; and (3) improving public financial management as well as fighting corruption – at the same time making a request for a development policy loan to the World Bank and the government of Japan. That is to say, the government of Indonesia recognized the necessity of continued structural reform and

requested the World Bank and the government of Japan for DPL assistance as a new policy assistance tool to facilitate this in the post-IMF structural adjustment loan. In response, a loan worth a total of US\$400 million was co-financed in FY2004, of which JICA¹ provided an ODA loan amounting to 10.794 billion yen (approximately US\$100 million). In 2005, the government of Indonesia added poverty reduction to the policy matrix as the fourth pillar of DPL. The World Bank, Asian Development Bank and the government of Japan co-financed loans worth a total of US\$700 million in FY 2005 as DPL II, a total of US\$900 million in FY 2006 as DPL III, and a total of US\$1,500 million in FY 2007. In addition, there were some concrete policy actions which JICA proposed to include in the policy matrix, based on dialogues with the Japan-Indonesia Strategic Investment Action Plan (SIAP)² working groups, after DPL III.

1.2 Program Context at Time of Appraisal

1.2.1 Public Financial Management (PFM) Reform on the Eve of DPL

As will be discussed (Section 3.2.1.1 Approach to Evaluation) PFM, which is one of the pillars of DPL, is a core reform area as prerequisite infrastructure for budget support type of assistance to effectively function. However, the PFM system in Indonesia had a lot of problems to be solved before DPL started in 2004. The following weaknesses were pointed out by the Country Financial Accountability Assessment (CFAA) jointly conducted by the World Bank and ADB in April 2001:

- (1) The legal and institutional environment was outdated and inappropriate.
- (2) The budget formulation process was opaque and inefficient.
- (3) Budget execution was often delayed and monitoring arrangements were weak.
- (4) Procurement processes were prone to corruption and collusion.
- (5) Accounting and reporting were fragmented and not always reliable.
- (6) The mandate of government audit entities was not clearly defined.

To cope with the weaknesses pointed out above, the Indonesian government prepared its 'White Paper – Reform of Financial Management Systems in Indonesia: Principles and Strategy, 2003' and launched various institutional reforms for implementation. A significant breakthrough was achieved with the enactment of the Laws on State Finances < Law No.17/

¹ In this report, the term 'JICA' means former JBIC when used in context before October 2008 - the term indicates the current JICA when used in context after October 2008.

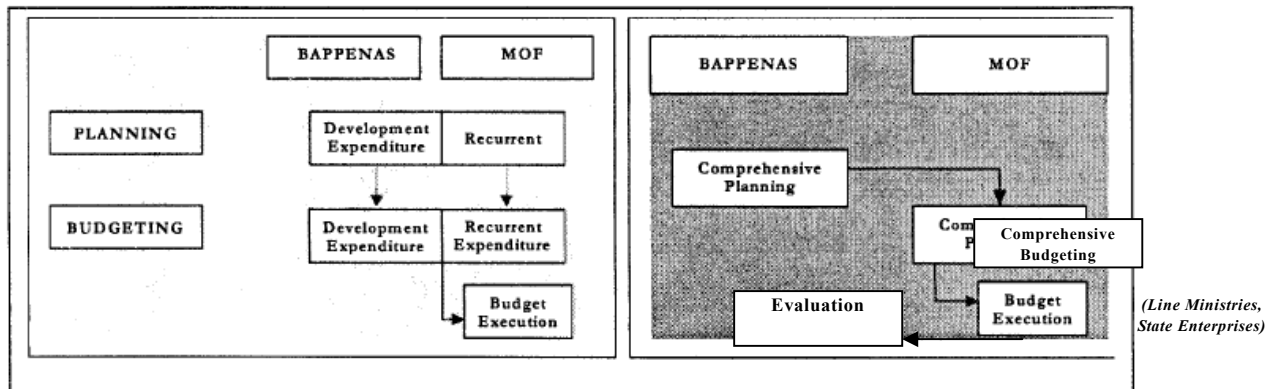
² The Japan-Indonesia Strategic Investment Action Plan (SIAP) is a new bilateral initiative between Japan and Indonesia for promoting foreign investment in Indonesia, especially from Japan, with the shared understanding that higher and sustainable economic growth through a substantial increase in investment is essential for Indonesia to alleviate poverty and generate jobs. SIAP was prepared by the High Level Public/Private Sector Joint Forum on Investment, launched in Jakarta in 2004.

2003>, State Treasury <Law No.1/2004> and State Audit <Law No.15/2004>, which were followed by State Development Planning System Law <Law No.25/2004> and Procurement Decree <Keppres (Presidential Decision) 80/2003>. The drastic institutional reform carried out, based on the series of legal arrangements indicated above, constituted an epoch-making performance in the history of public management reform in Indonesia. The following are the major areas of institutional arrangements made under the comprehensive reform where, amongst others, the core issues indicate the establishment of a clear definition and reclassification of the organizational share of responsibility and authority for planning, budgeting and evaluation, and for the structural rearrangement of development plans.

- (1) Functional Segregation between Planning & Evaluation (BAPPENAS: National Development Planning Agency) and Budgeting (MOF: Ministry of Finance) <State Finance Law>

The total system of public management consists of a cyclical process of ‘Policy Making’, ‘Planning’, ‘Budgeting’, ‘Execution’ and ‘Evaluation’: the linkage of which should not be interrupted. Since the Soeharto regime, both the planning and budgeting functions used to be divided between ‘Development’ and ‘Recurrent’ areas and separately managed by BAPPENAS (Development) and MOF (Recurrent). Budgeting and expenditure controls had been independently managed respectively, and the total public management system characterized above was thus vertically divided according to the ‘Development’ and ‘Recurrent’ categories. To avoid this vertical separation of governmental functions, the new system transferred all the budgeting functions to MOF and had BAPPENAS specialize in planning, budget execution (actually operated by line ministries and other public institutions) and evaluation: to establish a cyclical system with consistent flow of functional operations. The following figure illustrates the operations shared between the two controlling government agencies after the enactment of the State Finance Law.

Figure 1 : Changed Responsibility for Management of Planning and Budgeting
(Before State Finance Law) (After State Finance Law)



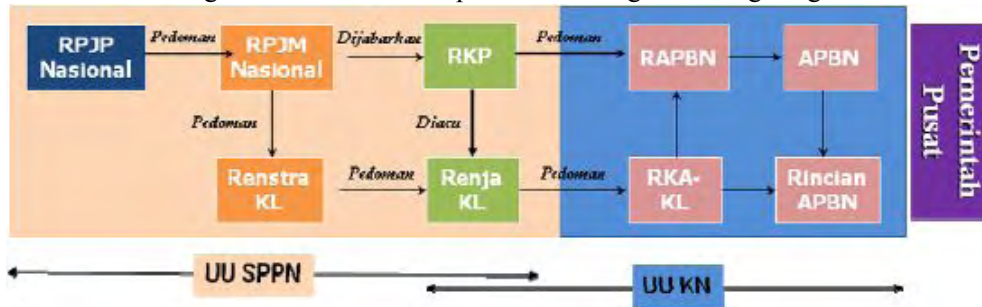
Source: Program Document for DPL I, World Bank, November 23, 2004 (partially modified)

(2) Structural Reform of Development Plan < State Development Planning System Law >

A consistent flow for preparation of the various levels of Development Plans was established: Based on the medium-term development plans ‘RPJMN: Rencana Pembangunan Jangka Menengah Nasional’ (each agency version is ‘Renstra-KL <ministerial Strategic Plan>’), which are the five-year components constituting the twenty-year long-term plan ‘RPJPN: Rencana Pembangunan Jangka Panjang Nasional’; the Government’s Action Plan ‘RKP: Rencana Kerja Pemerintah’ (each agency version is ‘Renja-KL’) is prepared. The national budget APBN and ministerial budget, ‘Rincian APBN’, are formulated with direct linkage to RKP. Thus, a consistent process directly connecting planning and budgeting has created Activity-Based (Performance) Budgeting under the system of Medium-Term Expenditure Framework (MTEF).

Figure 2 indicates the process flow as stated above at central government (Pemerintah Pusat) level and, basically, the same flow is also applied to the level of regional government. The pink portion on the left indicates the planning area and the blue portion on the right denotes the budgeting phase: the integration of both these phases in a consistent flow having made this reform most significant.

Figure 2 : New Development Planning and Budgeting Flow



Source: Pedoman Penyusunan Renstra-KL (Guideline for Preparing Ministerial Strategic Plan, Chapter 2)

(3) Reform of State Audit System (Rearrangement and Definition of BPK and BPKP)
<State Audit Law>

Indonesia has two state audit institutions: namely, BPK (Badan Pemeriksa Keuangan: Supreme Audit Agency) and BPKP (Badan Pengawasan Keuangan dan Pembangunan: Financial and Development Supervisory Board). BPK is charged with audit of national finance. It was established under the Indonesian Constitution (UUD 1945) and is independent of government, as an external auditor, reporting directly to the national assembly (DPR: Dewan Perwakilan Rakyat). On the other hand, BPKP is a national body established under the Presidential Decision (KEPRES) No. 31, 1983, as one of the Non Governmental Organizations (LPND). It is independent of other ministries and agencies and its fundamental function is to carry out supervision on ministerial internal audits, the training of internal auditors, issuance of audit guidelines, the formulation of an internal audit schedule and other supervisory functions.

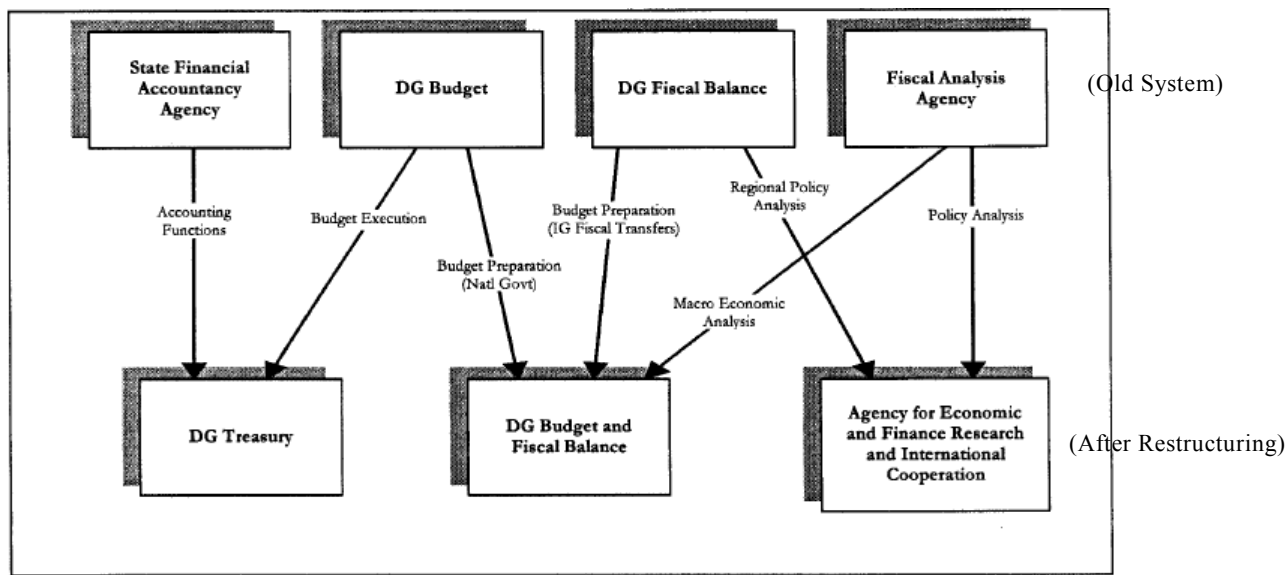
The functional division between the two audit agencies to carry out external and internal audits is thus legally clear. However, in practice, an unclear division of work and a remarkable degree of operational duplication was found to be burdening the auditors and significantly impeding efficient implementation of state auditing works. In order to improve this situation, State Audit Law intends to strengthen BPK's capacity for external audit as the Supreme Audit Institution (SAI) of Indonesia and, at the same time, to rationalize the functional duplication between BPKP and the Inspectorate Generals of each ministry and Regional Internal Audit Bodies (BAWASDA) to further strengthen the internal auditing system.

(4) Structural Reform of MOF

A large scale organizational reform of MOF was implemented, under State Treasury Law, to strengthen institutional capacity and improve the internal control system. The outline of this rearrangement and integration of the internal system is illustrated in Figure 3 below, in which the most important change constituted the separation of

budgeting and treasury functions and their respective capability enhancement.

Figure 3 : Organizational Restructuring of MOF



Source: Program Document for DPL I, World Bank, November 23, 2004

1.2.2 Investment Climate on the Eve of DPL

Improvement of the investment climate is one of the pillars of DPL I-IV in which JICA has a keen interest. In the process of policy matrix formulation, JICA undertakes policy dialogue with Japanese companies to identify problems in trade and investment and subsequently intends to reflect these issues when deciding policy actions with the Indonesian government and development partners.

When DPL started, the government of Indonesia recognized that investment would play a critical role for sustainable economic growth and, through this, job creation. The government set the improvement of the investment climate as one of the policy objectives in RPJMN 2004-2009. However, while expansion of investment was expected to help ensure sustainable economic growth, the government of Indonesia had previously been putting the priority on fiscal soundness and the level of public investment had been low before DPL started. In fact the share of investment in GDP had declined from 30% in 1996 to below 20% in 2002, due to a downturn in the Indonesian economy following the effects of the Asian financial crisis and a weak investment environment as represented by days required to start a new business, which took five times longer than Thailand or Malaysia.

In addition, according to a survey about foreign trade and investment³, companies had

³ Japan Business Council for Trade and Investment Facilitation “Issues and requests relating to foreign trade and investment in 2004”

pointed out various problems such as prohibitions and restrictions on the entry of foreign capital, complications and delays in customs clearance procedures, advance collection of corporate tax based on the performance of the preceding year, delays in VAT refunds, an unclear tax administration system, arbitrary levy application and the application of discriminatory taxation against foreign investment. As described above, in order to promote foreign investment in Indonesia, it was expected to reduce transaction costs and the effective implementation of policy actions targeted on the improvement of the investment environment became an important subject.

1.2.3 Poverty Reduction on the Eve of DPL

Poverty reduction was not included in reform items at the beginning of DPL but was added from DPL III as a pillar of "Improving Service Delivery". This is because the priority of reform shifted more towards the issues of on-site level, whilst Indonesia frees itself from the serious economic stagnation after the Asian currency crisis in 1997 and stabilization of the macro economy is attained, as mentioned below. (Refer to "3.1.1 Relevance to the Development Policies of Indonesia")

Although the macroeconomic situation was improving steadily, the situation where poor people were living on under US\$ 2 a day (1985 value) still accounts for 53% of the total population and, as approximately 2 million new workers entered into the labor market every year, further economic growth was necessary to generate employment.⁴ In addition, fuel prices were increased by 30% in March, 2005, and by 115% in October of the same year. Thus, accompanied by these reduced subsidies and the creation of greater fiscal space (an estimated US\$10 billion annually), compensation programs for the poor were introduced. Specifically, poverty programs for education, health, food, and rural infrastructure were started in March, 2005, and a direct cash transfer program for 19.1 million households was carried out in October, 2005. However, although new poverty programs were introduced, since the effects between each program had varied, effective implementation of the programs became an issue.

1.2.4 The Government's Expected Role of DPL

As mentioned above, while facilitation of reform in each area was called for, remarks from stakeholders showed that the Indonesian government was expecting the following role for DPL at the time of its start. That is to say, by taking a close-up of important policy issues through continuous policy dialogue between government and development partners and monitoring of the reform progress, the so-called "champions", who are reform promoters with a mind for governmental reform, were to be pushed up to facilitate reform. In other words, the

⁴ Data source: Ex-ante Evaluation for DPL 2
http://www2.jica.go.jp/ja/evaluation/pdf/2005_INP-28_1_s.pdf

champions in the government seem to have considered that they were going to promote reform through implementation of DPL by utilizing development partners' influence. In addition, it seems that DPL aimed to show (signal) to the government (inside and outside) and to the international community, that the Indonesian government has been tackling structural reform with major development partners. Furthermore, it seems that the government was aiming to facilitate and strengthen coordination within the government by formulating organizational structures, such as the government task-force for reform implementation.

1.2.5 The Government's Expected Role of DPL as Financial Support

At the time DPL started, the Indonesian government had budget deficit problems and needed funds to fill the financial gap. According to a JICA document on DPL I, the Indonesian government needed funds to repay its deferred debt (of US\$ 3 billion) to the Paris Club. Although the government managed the issue through privatization of state-owned companies, asset sales as well as a bond issue in and outside the country, etc., the ratio of budget deficit to GDP had become 1.1% for fiscal year 2004. Under such economic conditions, the DPL fund seemed to have been expected to fill the financial gap according to the macroeconomic perspective of the country.

1.3 Program Outline

The program aims to promote policy reforms and policy dialogue between Japan and Indonesia through evaluating the policy reform record of the Indonesian government in coordination with the World Bank and the Asian Development Bank: thus supporting Indonesian policy reforms and thereby contributing to (1) promote Indonesia's macroeconomic stability; (2) improve its investment climate; (3) improve public financial management as well as fight corruption; and (4) reduce poverty.

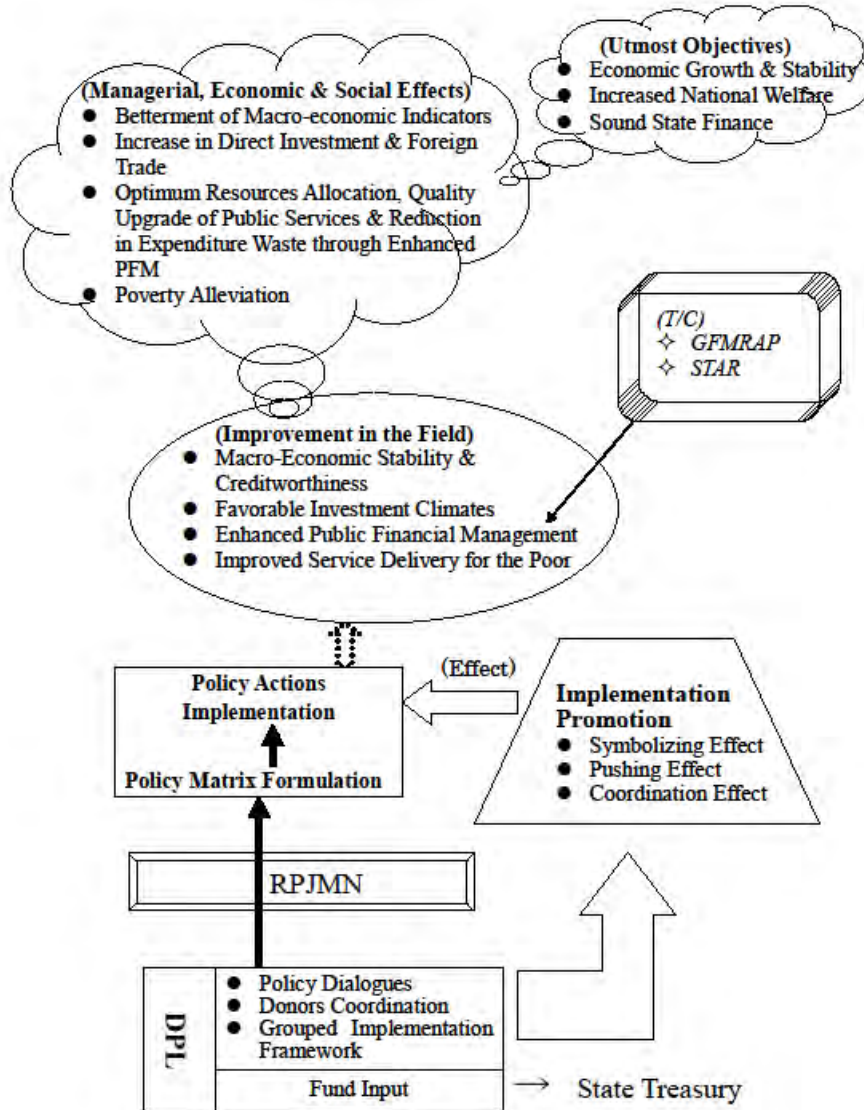
	DPL I	DPL II	DPL III	DPL IV
Approved Amount / Disbursed Amount	10,794 million yen / 10,794 million yen	11,729 million yen / 11,729 million yen	11,777 million yen / 11,777 million yen	22,080 million yen / 22,080 million yen
Exchange of Notes Date / Loan Agreement Signing Date	March 24, 2005 / March 28, 2005	March 28, 2006 / March 28, 2006	March 23, 2007 / March 23, 2007	March 18, 2008 / March 18, 2008

Terms and Conditions	1.3% interest rate, 30-year repayment period (including a 10-year grace period) , general untied	1.5% interest rate, 30-year repayment period (including a 10-year grace period) , general untied	1.5% interest rate, 30-year repayment period (including a 10-year grace period) , general untied	0.7% interest rate, 15-year repayment period (including a 5-year grace period) , general untied
Borrower / Executing Agency	Republic of Indonesia / Ministry of Finance	Republic of Indonesia / Ministry of Finance	Republic of Indonesia / Ministry of Finance	Republic of Indonesia / Ministry of Finance
Final disbursement date	March 31, 2005	March 31, 2006	March 30, 2007	March 28, 2008

1.4 Structure of DPL Assistance

Since DPL belongs to general budget support assistance, it inclines to attract attention to its effect simply in connection with the fund injection. However, expectations of the Indonesian side also reveal it to be obvious that DPL's main objective is to lend assistance to various kinds of enhancement in public systems to improve the areas of "macro economic conditions", "investment climate", "public financial management" and "service delivery focusing on poverty alleviation." The fund provided by DPL is placed directly in the state treasury as a part of government revenues, without being earmarked for implementation of the above listed target improvement efforts. The actual context of the assistance and expectations of effects around DPL could be illustrated as in Figure 4 which follows.

Figure 4 : Structure of Assistance for DPL and its Expected Effect



DPL I-IV installs a policy matrix with four target pillars comprising the areas of “macro-economy”, “investment climates”, “public financial management” and “poverty alleviation” based on the medium-term national development plan, RPJMN (2004-2009). The matrix was formulated through policy dialogues with the Indonesian government, as well as among development partners, and specifies sets of concrete policy actions to be implemented under their respective pillars. It intends to achieve “improvement in macro-economic stability and creditworthiness”, “preparation of favorable investment climates”, “enhancement of

public financial management” and “improvement in service delivery focusing on poverty alleviation” at field level. It further aims through practical improvements at “betterment of macro-economic indicators”, “increase of direct investment and foreign trade”, “optimum resource allocation, quality upgrading of public services and reduction in wasteful expenditures through efficient and effective financial management” and, “reduction in poverty population and ratio” - with the ultimate objective of attaining “national economic development and stability”, “increase of national welfare” and “sound state finance”. Although this is the apparent flow of the expected process, direct support of DPL is limited up to the stage of specifying policy actions and promoting their execution, as indicated by the black arrow → in the figure. The upper processes are also significantly affected by uncontrollable external factors with an increasing extent of phasing down the impact of DPL.

It should be noted that those processes (or “policy matrix process”) could be advanced even without DPL under the framework of the new system of development plans formulation depicted in Figure 6 below, and that each policy action is expected to have been carried out by their respective implementing agencies. Furthermore, the new system requires BAPPENAS to regularly monitor progress of implementation and to evaluate the performance. The overall institutional framework has, thus, been established. However, the practical capacity to implement it has not been satisfactorily prepared.

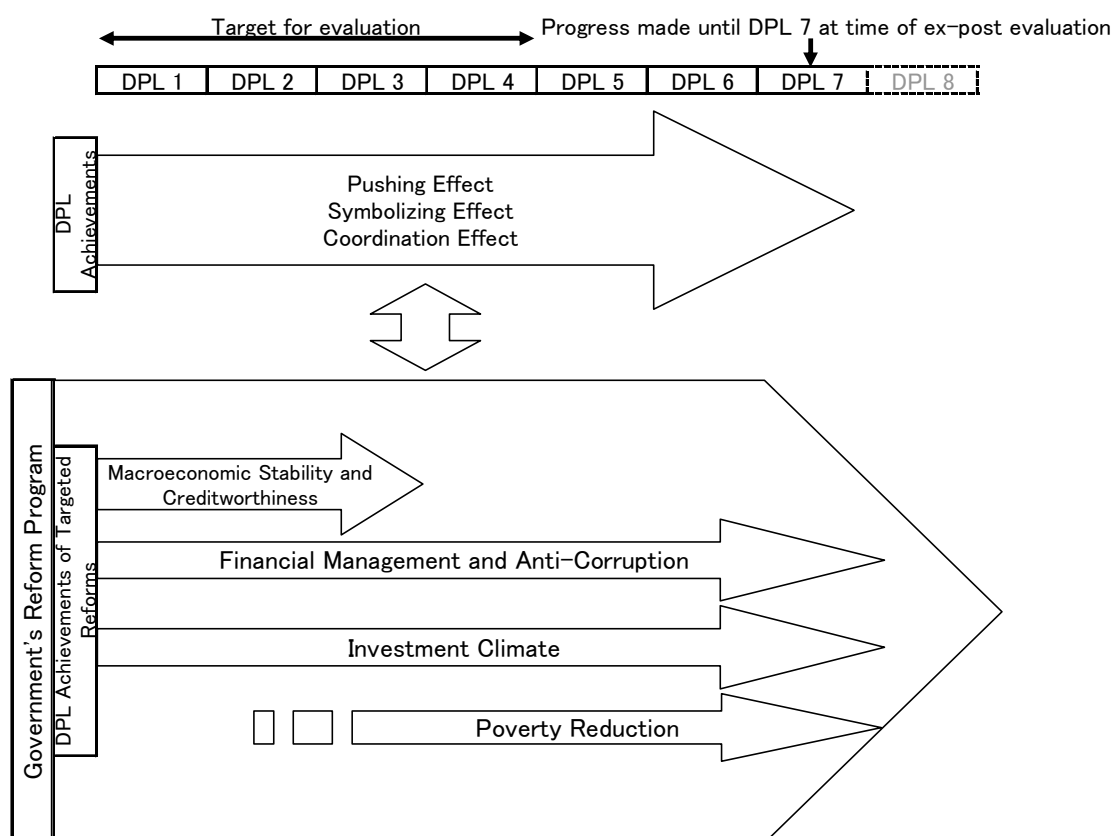
There is another aspect of DPL that gives flank support to promote the progress of action taking (or “supporting process”), which is advanced through policy dialogue, coordination among development partners during the entire DPL process, and grouped institutional frameworks such as the organization of collaborative taskforces. The “pushing effect”, “symbolizing effect” and “coordination effect” generated from the above mechanisms strongly support implementation of the required actions specified in the policy matrix. Different from the “policy matrix process”, this “supporting process”, as indicated by the white arrow ⇨ in the Figure, could never have taken place spontaneously through self-momentum on the Indonesian side, without DPL. In view of this important point, this “supporting effect” should attract major attention in DPL evaluation.

1.5 DPL Evaluation Approach

In conducting DPL evaluation, close attention was paid to the context of DPL in Indonesia and the incentives of relevant parties in government when conducting analysis. The three effects: “pushing effect”, “symbolizing effect”, and “coordination effect”, as mentioned above, are to be called “DPL achievements” in this report and are to be analyzed separately from “DPL achievements of targeted reforms” (See Figure 5). Evaluation paying attention to “DPL achievements” is carried out in neither the World Bank nor the Asian Development Bank. As mentioned below, “DPL achievements” and “DPL achievements of targeted

reforms” are the arguments on another dimension, and it is difficult to consider them on an equal footing. Furthermore, “DPL achievements of targeted reforms” contain different significance, implications and levels of reform according to each reform area – and the progress of reforms also differ. Therefore, since it is impractical to apply the existing five criteria of DAC, analysis based on these criteria was not used and, instead, perspectives on: (1) DPL relevance; (2) DPL achievements and progress of targeted reforms; (3) DPL attempts and achievements; and (4) DPL sustainability were taken up. With regard to (2), (As mentioned in 2.3 Constraints during the Evaluation Study, see below), this evaluation has the nature of a mid-term review and it is still premature to see the achievements. Therefore, assessment was made for reference information, and rating was not undertaken in this report. Whilst the meaning and effect of a DPL fund are created on a different dimension from implementation and facilitation of reform, focus has been placed on the reform aspect in this evaluation. Therefore, in this report, description about DPL funding is limited.

Figure 5 : Conceptual Diagram of “DPL Achievements” and “DPL Achievements of Targeted Reforms”



2. Outline of Evaluation Study

2.1 External Evaluators

Ms. Masumi Shimamura (Mitsubishi UFJ Research and Consulting Co. Ltd.)

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2.2 Duration of Evaluation Study

Duration of Study: December 2010-March 2011

Duration of Field Study: 9-22 May 2010; 8-13 August, 2010

2.3 Constraints During Evaluation Study

Although the scope of this evaluation is DPL I-IV, DPL is a dynamic process and has been continuing until now (2011). Considering the situation and nature of DPL, it is difficult to separate out DPL achievements of targeted reforms during DPL I-IV from those of subsequent DPLs. In addition, since interviews in the field study were mainly conducted with people in charge of current DPL implementation, the information collected was not necessarily targeted on DPL I-IV. Therefore, the analysis and evaluation of this report covers not only DPL I-IV but also a part of subsequent DPLs. Considering the different progress and time required for achievement of targeted reforms, it is still premature to see the achievements. In this sense, this evaluation has the nature of a midterm review – though it is entitled Ex-post evaluation.

DPL is a program that contributes to framework setting such as the rules and regulations for policy and institutional reform. Therefore, no changes could be expected to occur on the ground, except through the implementation of policy actions. In evaluating the effects of DPL achievements of targeted reforms, it is important to observe the effects of reforms on the ground. However, in reality, expected tangible effects have not yet appeared in some areas, such as public financial management. Therefore, in this evaluation, areas where expected tangible effects have not appeared are only examined and the progress of action taking summarized.

Furthermore, a time lag exists before tangible effects may be expected to appear, and various external factors positively and negatively affect the processes of achieving DPL's policy level objectives, which makes it very difficult to see the direct effects of DPL's policy actions on achievements of its policy level objectives. In this sense, it is difficult to separate out Japan's contributions to achievements of policy level objectives or to measure their effects in a quantitative manner. Taking into account these constraints, this evaluation used both quantitative data as well as the actual voice of relevant stakeholders gathered through various interviews.

3. Results of Evaluation (Overall Rating: A)

3.1 Relevance (Rating: a)

In evaluating relevance, analysis was made from four viewpoints: (1) relevance to the development policies of Indonesia; (2) relevance of DPL's function; (3) relevance of JICA's participation in the DPL framework; and (4) relevance of DPL funding. The viewpoint of each evaluation is as follows: 1) the extent to which the targeted reform areas of DPL are aligned with the government's development policy and development needs and priorities of the Indonesian government; 2) whether DPL had an appropriate function that met the expectations of the Indonesian government when looking back from the time of appraisal; 3) whether, having chosen DPL as a support tool, it was appropriate to fulfill JICA's needs, taking into consideration its assistance environment at the time of appraisal; and 4) whether it was appropriate for JICA to provide DPL funding.

3.1.1 Relevance to the Development Policies of Indonesia

The targeted reform areas of DPL I-IV are summarized in Table 1. All are in line with the important reform items of the Indonesian government at the time of appraisal. At the start of DPL I, the main development agenda, contained in each of the areas as shown below, is now manifest in the Major Development Agenda of 2004 to 2009 that the new Yudhoyono government prepared, and in the "100-day Plan" instituted in a cabinet meeting of October, 2004. In addition, the following reform items were specified as major agenda items in RPJMN (2004-2009), and are also in conformity with important reform items at the time of evaluation.

Table 1 : Reform Areas of DPL I-IV	
1.	Macroeconomic Stability and Creditworthiness
2.	Investment Climate
3.	Financial Management and Anti-Corruption
4.	Poverty Reduction

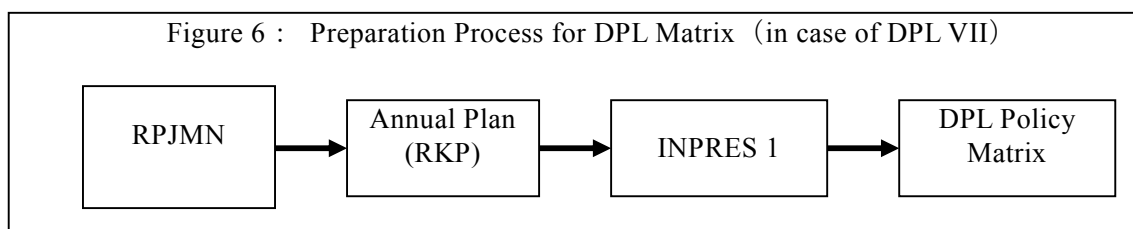
DPL policy actions are an integral part of the Indonesian government's own reform program, and it is difficult to separate out DPL policy actions from the government's program.⁵ When looking at the preparation process of the DPL policy matrix (in the case of DPL VII⁶), the government prepares an annual plan⁷ based on RPJMN⁸, then selects high

⁵ Therefore, in the evaluation, the movement of a government's reform program is generally referred to in analyzing DPL reform initiatives for each area.

⁶ As information was not available for the cases of DPL I-IV, the case of DPL VII was taken up. While policy documents equivalent to INPRES 1 were not identified for the period of assistance for DPL I-IV, there were remarks that the preparation process for DPL I-IV and that of DPL VII would have no big difference – the information was judged as reliable.

⁷ Based on RPJMN, annual government action plan, RKP is prepared and, based on RENSTRA-KL, annual plans for each ministry and agency, RENJA-KL is prepared.

issues of priority to come up with INPRES 1.⁹ The DPL policy matrix is prepared by selecting policy actions mainly from INPRES 1 and the annual plan in areas of investment climate, public financial management and poverty reduction. It is then finalized through policy dialogue with the Indonesian government. Since DPL policy actions are prepared through such a process, DPL is perfectly in harmony with the development policy and development needs of the Indonesian government.



Source: Information from the World Bank Indonesia Office

As described below, because DPL is changing its priority issues and areas of support – flexibly in accordance with the changing development priorities of Indonesia – it can be said that DPL is completely in line with the priority of governmental reform.

Table 2 summarizes the evolution of priority issues and areas for each round of DPL. They are aligned with priority issues and areas of the government's own reform, and DPL is said to be evolving flexibly by continuously improving its reform program over time, according to changes of governmental priority issues. In fact, since DPL IV, “Macroeconomic Stability and Creditworthiness” was dropped from the targets for reform, whereas Poverty Reduction was added under “Service Delivery” from DPL III.

The macroeconomic environment has been improving in a general sense: the real GDP growth rate has increased in a sustained manner¹⁰ for 5 years from 2002 to 2006 and the inflation rate went down to 6.4% in 2007, although it has gone up temporarily (13.1%) because of fuel subsidy reduction in 2006. The current account balance has been in the black and, supported by global primary-goods demand, external reserves have reached 6.8 months of import parts. As such, macroeconomic stability has been in a stable condition and, therefore, this reform area has been dropped from DPL IV. However, in a situation where improvements in the country’s employment generation and poverty reduction have been limited (the unemployment rate was 9.7% and the poverty rate was 16.6% in 2007), sustainable economic growth and improvement of public institutions remained an issue and,

⁸ The 5-year strategy plan prepared by each ministry and agency is the RENSTRA-KL.

⁹ Presidential Instruction No.1

¹⁰ GDP growth rates were: 4.8% (2003), 5.0% (2004), 5.7% (2005), 5.5% (2006), 6.3% (2007). (Information from JICA on DPL IV)

therefore, poverty reduction was added as a new reform area for DPL support.

Table 2 : Indonesia's Development needs and Priorities	
DPL I	Macroeconomic stability after graduation from IMF program
DPL II	Creating more fiscal space for more pro-poor expenditure
DPL III	Improving service delivery
DPL IV	Deepening institutional reforms

Source : World Bank Implementation Completion and Results Report

From the viewpoint of both changes in priority of reform issues and areas at the time of the DPL start and afterwards, DPL has been highly in conformity with Indonesia's development policy (completely aligned).

3.1.2 Relevance of DPL Function

The Indonesian government had decided to request DPL as a new assistance tool in the post IMF era. It was expected that the government itself would exercise ownership and leadership in reform planning and implementation, and would facilitate reform through maintaining partnership between the government and development partners based on a relationship of mutual trust. Continuous policy dialogue, coordination among the development partners and formulation of grouped institutional frameworks – such as the organization of collaborative taskforces to implement policy actions in the DPL process – all seem to have responded to the government's policy direction and intention. In other words, when looking back from the time of appraisal, the activities injected by DPL implementation have been accompanied by: (1) a “push up” function impacting on the Indonesian government's reform initiative itself, through supporting champions within the government; (2) a “symbolizing” function to demonstrate the strong commitment of the government towards reform, both in and outside the country; and (3) a “coordination” function to formulate an institutional framework for reform implementation and to facilitate and strengthen coordination within the government. Therefore, DPL has responded to the Indonesian government's expectations for its own reform initiatives. Other assistance tools, such as individual project assistance, would not necessarily have been able to respond so fully.

Policy actions identified in DPL are those from among the government's important reform issues (Table 1) expected to gain attention through the government having identified them: although their recognition had still been low before or at the time of their selection. In other words, DPL is structured to contain reform issues so as to raise attention in government by identifying policy actions for which some champions in the government recognize their importance and priority, and so are to be pushed up through development partners utilizing the DPL framework. If such incentives were absent in the government, it would not be necessary to identify DPL policy actions because the government would have advanced

reform on its own for the highest priority policies even without DPL. Moreover, policies widely recognized as the most important government issues at present may have been in such state at the time identified as DPL policy actions. Therefore, DPL incorporates a function to facilitate the government's overall reform by focusing on its reform issues of priority as well as those with less attention in the absence of DPL and, thus, providing an overall consistent "push up" (See 3.3.1. DPL Pushing Effect). One government official interviewed indicated that the DPL's reform targets and indicators have substantially become the Indonesian government's own key performance indicator (KPI), and that DPL "pushes up" the everyday efforts (planning, implementation, monitoring, and evaluation) of the government towards reform – playing a role as the "judge", who checks progress and the results of reform.

In addition, DPL has a function to signal, both inside and outside of government, as well as to the international community, that the Indonesian government has been tackling structural reform with major development partners through utilizing their influence. To this effect, there was a remark in an interview that, "DPL contains a function to facilitate reform by inducing high-level attention through sending "signals" to government officials."

Furthermore, DPL incorporates the function to facilitate coordination to enhance policy decision-making for cross-sectoral reform issues.

It is evident from the remarks of government officials that institutional structures of the government, which tend to become vertical divisions for each ministry and agency, would be systematized to formulate the organization of collaborative taskforces and, thus, coordination in the government would be facilitated and enhanced.

These functions are needed for the Indonesian government to resolve development challenges, and have been recognized as value added through DPL.

Therefore, these DPL functions are considered relevant in order to respond to the expectations of the Indonesian government at the time.

3.1.3 Relevance of JICA's Participation in the DPL Framework

According to interviews with the relevant stakeholders, at the start of DPL JICA seemed to have the following objectives in participating in the DPL framework: (1) to strengthen policy dialogue with the Indonesian government and to take on the country's democratic process and reform; (2) to understand Indonesia's policy challenges from a comprehensive viewpoint and to participate in the latest discussion on the country's policy and institutional reforms as well as to be actively involved through DPL co-financing; and (3) to tackle Indonesia's development issues and to enhance aid effectiveness by undertaking both project type assistance, which JICA has been providing to date, and DPL as both sides of the same coin. This section will analyze the appropriateness of choosing DPL as an assistance tool in order

to respond to the aid environment where JICA was placed at the time of appraisal.

At the time DPL started, when JICA's development assistance and economic cooperation activities were activated, JICA seemed to be calling for the following needs: 1) to strengthen the sending out of information and the message on JICA's country assistance strategy to Indonesia (strengthening outgoing transmission); 2) to strengthen policy dialogue with the Indonesian government (strengthening of strategy on their bilateral relationship; and 3) to respond to reform needs within Japan on ODA (facilitating internal reform). These can be inferred from JICA's overall aid policy and direction at the time, which aimed at further activation of ODA Local Task Force and strengthening of local functions. Originating within this context, momentum seemed to have increased in JICA to further actively engage in Indonesia's policy and institutional reform. In fact, the newly established Yudhoyono government requested the Japanese government and World Bank for DPL assistance as a new policy tool to facilitate reform in the post-IMF era. Acting upon this request, JICA seemed to have entered into the DPL framework as a large donor to Indonesia, so as to obtain opportunities to participate in Indonesia's overall institution building and to assist the country's reform. In addition, DPL was expected to play the role as a platform for donor coordination after the Indonesia Consultative Group (CGI) was abolished in January 2007 and the situation in which it had become difficult to acquire information on the overall picture of donor assistance across sectors. The DPL assistance tool was then anticipated to be a means to resolve such JICA issues, as has been realized at the time of evaluation. In view of the above, the fact that JICA has chosen DPL is deemed to have been the right decision.

In addition, in light of JICA's objective for DPL co-finance to "facilitate Indonesia's government policy," the targeted reform areas of DPL seem to be generally moving forward: whilst there is variation in accordance with each area. So long as Indonesia's reform process is proceeding, continuing DPL co-finance in support of such reform would be considered relevant.

Furthermore, unlike project type assistance, DPL is a scheme which can enjoy added value which is unique to policy assistance type general budget support. Activities to continue policy dialogue with the Indonesian government to raise the issues of concern to JICA directly with high-level reform promoters in government; to obtain high-level commitment for reform from them; and, to continuously monitor the government's implementation of reform – have all been realized through DPL. DPL as a tool is also expected to have a complementary relationship with project based loans and technical cooperation, which JICA has been implementing in the past, and to further enhance aid effectiveness. These objectives have been realized at the time of evaluation.

To make a comprehensive assessment, it can be said that participating in DPL co-financing

was the right policy decision for JICA.

3.1.4 Relevance of DPL Funding

The relevance of JICA's providing finance to DPL is deemed appropriate from the perspectives of: (1) getting on the platform for policy dialogue with the Indonesian government; and (2) providing assistance to help bridge Indonesia's financial gap.

As mentioned above, JICA needed to achieve its objective to obtain an opportunity to participate in dialogue regarding Indonesia's overall institution building. In order to fulfill this objective, there were no other means than to participate in DPL and, thus, providing the DPL fund was necessary in order to attain the policy dialogue platform.

In addition, as mentioned (See section 1.2.5 The Government's Expected Role of DPL as Financial Support), from the country's macroeconomic perspective, JICA needed to provide support to fill Indonesia's financial gap with the DPL fund.

During the interview survey, officers from MOF indicated the significance of DPL funds as follows: "If it were not for DPL funds, budget shortages would occur and financing would be necessary to fill the gap" and, "DPL funds are important as a preparation or guarantee in case of economic downturn." According to the Indonesian government's revised budget for FY 2010¹¹, the overall balance, after deducting annual expenditure from annual revenue, is a deficit (minus 133,700 billion rupiahs) and it is assumed to fill this financial gap through domestic and foreign funding. Among these, foreign funds come from the program loan of 29,400 billion rupiahs and the project loan of 41,400 billion rupiahs. DPL funds are included in the program loan, which accounts for about 3% of the total annual revenue. The scale of funding from the program loan corresponds to that of the deficit of the government's primary balance (28,100 billion rupiahs). While the Indonesian government is financing this gap through domestic bank loans and the issuance of government bonds, DPL funds are also regarded as an important source of funding. Therefore, it is relevant for JICA to provide DPL funds in order to assist the country's macroeconomic financial needs.

3.2 DPL Achievements and Progress of Targeted Reforms

In this section, amongst the four pillars of DPL, the reform areas of Public Financial Management, Investment Climate and Poverty Reduction are taken up and the state of their implementation and progress is analyzed. The section looks into the reform areas which were targeted by DPL assistance. As mentioned above, rating has not been conducted because this evaluation has the nature of a midterm review and, thus, it is too early to see the results.

"DPL achievements" to be described in next section and "DPL achievements of targeted reforms", taken up in this section, represent analysis of different dimensions and is difficult to

¹¹ Budget data obtained from MOF during field survey.

treat them in a similar manner. The former represents the direct effects coming from DPL, whereas the latter is regarded to be that which the Indonesia government itself may have advanced in its reform effort – even in the absence of DPL. The effect of DPL on the facilitation of reform and the strengthening of implementation is difficult to analyze quantitatively in each of the reform areas and, therefore, assessment has also been based on the actual voice of the relevant stakeholders and their narrative descriptions.

3.2.1 Public Financial Management

3.2.1.1 Approach to Evaluation

Public Financial Management (PFM) is an area that aims for institutional strengthening to rationally manage the government’s financial operation and constitutes one of the four policy areas to be improved by DPL I-IV. Simultaneously, PFM is a prerequisite for budget-support type of assistance, including DPL, to effectively function and serves as an institutional infrastructure¹². In other words, PFM is the core area of DPL in terms of its cyclical relation with DPL; DPL aims at PFM enhancement while sufficient capacity of PFM itself is a prerequisite for sound DPL. It should be regarded, therefore, as an area of more than one of the policy areas of DPL and should not be treated in the same dimension as other pillars. The following figure shows this concept.

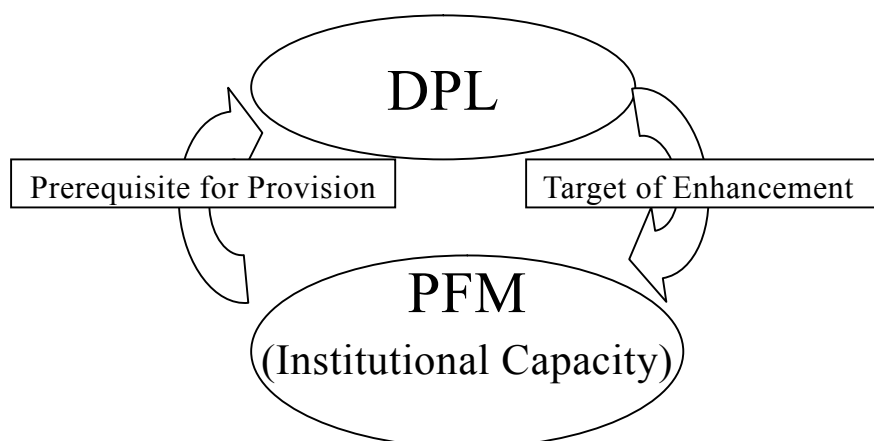


Figure 7 : Relation between DPL and PFM (Institutional Capacity)

Indonesia carried out a drastic PFM institutional reformation on a large-scale on the eve of DPL during 2001-2004, and it is the task of DPL I-IV and succeeding DPLs to breathe life

¹² “DPL operation sets out to provide general budget support to the Indonesian Government and will be executed through its public financial management system.” (Program Document for DPL VII, August 26, 2009)

into that established new institutional framework. Although progress was made by taking required policy actions throughout DPL I-IV, expected tangible effects¹³ have not yet appeared in the field of the intended institutional reform. Therefore, this DPL evaluation only examines and summarizes the progress of action taking by reviewing the results of the preceding World Bank's evaluation and analyses in "Program Documents" up to DPL phase VI and in the "Implementation Completion and Results Report on DPL I-IV."

3.2.1.2 Reforms Targeted by DPL I-IV

The institutional reform already mentioned (See 1.2.1 Public Financial Management (PFM) Reform on the Eve of DPL) has established an overall framework, which should be followed by an effort to put it into practice. Two devices were prepared: namely, DPL to set out the implementation framework and to institutionally support its progress and two technical cooperation projects¹⁴ to directly assist necessary improvement.

(1) Areas to be Assisted by DPL

A series of assistance was launched by DPL I signed with the World Bank in December, 2004 (loan signing with JICA was in March, 2005). Public Financial Management as the third policy pillar consistently tackles the following areas [excepting (v) which was added in DPL III]:

- (i) Further development of the legal framework for public financial management
- (ii) Improvement of national budgeting and implementation management
- (iii) Enhancement of public procurement system
- (iv) Improvement of public audit system
- (v) Civil service reform (added in DPL III)

(2) Two Technical Cooperation Projects

(A) Government Financial Management and Revenue Administration Project (GFMRAP), World Bank (2004-2012)

Technical cooperation to MOF and BAPPENAS with wide range covering 'Budgeting', 'Budget Execution', 'Treasury Modernization', 'Public Procurement System' and 'Tax, Customs Management'

(B) State Audit Reform (STAR), ADB (2005-2009)

Technical cooperation to BPK as the supreme audit institution of Indonesia and BPKP; leading institution of internal audit, to comprehensively strengthen the legal

¹³ Cf. Section 1.4 Structure of DPL Assistance

¹⁴ Additionally, other technical cooperation projects that directly assist individual management areas were being provided by such multi-lateral donors as the Asian Development Bank, IMF, UNDP, UNCTAD and World Bank and by bi-lateral agencies including AusAid (Australia), CIDA (Canada), EU, GTZ (Germany), USAID (USA) <Source: Program Document for DPL I, World Bank, November 23, 2004>

and institutional framework of external and internal public auditing

3.2.1.3 Implemented Policy Actions in DPL I-IV

(1) Preparation of Operational Framework for Laws and Regulations on Public Financial Management

Operational procedures and other necessary arrangement to put the institutional framework developed by the basic laws and regulations (See 1.2.1) into practice were prepared.

(2) Treasury Single Account

More than 18,000 bank accounts and other accounts unknown to the government used to be handling government funds before the commencement of DPL. Steps to integrate these chaotic bank accounts into a Treasury Single Account (TSL) were proceeding throughout DPL I-IV; TSL for expenditure accounts was completed at the end of DPL IV. This represents a momentous achievement towards increased transparency of government expenditures.

In relation to that performance, organizational reform of MOF was carried out to segregate budgeting and treasury functions and to strengthen the internal control system (See Figure 3: Organizational Restructuring of MOF). This represents one of the pivotal improvement areas in the reform of national budget execution management.

(3) Improvement of Budgeting System

Indonesia is moving toward a Medium-Term Expenditure Framework (MTEF) and an activity/ performance based budgeting system. As stated earlier, a consistent development planning process – from central to regional levels – and activity-based budgeting directly linked to the planning process were established under the State Development Planning System and State Finance Law. This reform established a framework for planning and budgeting integration and its implementation would later be practiced in the 2008 national budget formulation.

(4) Improvement of Public Procurement System

The National Public Procurement Office (NPPO) in BAPPENAS was functionally enhanced and established as an independent institution directly under the President.

(5) Anti Corruption

Since 2003, a number of anti-corruption institutions – including the Corruption

Eradication Commission (KPK), the anti corruption taskforce (established in the Public Prosecutor's Office) and the Anti Corruption Court – have been established and are increasingly active. The number of cases prosecuted has dramatically increased and high profile corruption investigations have been launched at every level of government including mayors, governors and ministerial level officials. However, it should be noted that those activities only tackled corruption that came to the surface and that rational and transparent control of public activities by well prepared PFM should play a more important role as an automatic controlling managerial infrastructure. This area also comprises an integral part of budget execution management reform.

(6) Public Service Reform

This area was added in DPL III. The reform includes a review of systems of the official duties and emoluments of the government sector in order to remove low staff incentives which had been one of the significant bottlenecks for smooth execution of public policies. Surveys regarding performance-based payroll and the allowance system were conducted and trial a application was piloted in MOF.

Policy actions to be taken in each DPL phase and their state of performance is summarized in the following table.

Table 3 : Action Performance of Public Financial Management

	Policy Actions	Status
DPL I	◆ Issuance of implementing regulations for State Finance Law	Fulfilled
	◆ Organizational reform at the Ministry of Finance, including first steps to establish a Treasury Single Account	Fulfilled
	◆ Presidential Decree on Government Procurement	Fulfilled
	◆ Continuation of special audit program for SOEs.	Fulfilled
DPL II	◆ Issue additional Implementing regulations for State Finance Law, Treasury Law and State Audit Law	Fulfilled
	◆ Treasury Single Account timetable and activity Plan adopted for the consolidation of bank accounts	Fulfilled
	◆ Investigation unit is established and fully operational in the IG MOF, vested with the necessary legal powers to investigate all MOF employees	Fulfilled
DPL III	◆ Extend the pilot for zero-balance non-salary accounts to at least 50 KPPNs	Fulfilled
	◆ Improved fiscal reporting by timely presentation of aggregate Central Government financial statements for fiscal Year 2005	Fulfilled
	◆ Develop a separate unit that handles the modernization program on a full-time basis	Fulfilled
	◆ Issue ministerial decrees for blue-book and on-granting procedures	Fulfilled

	◆ Pilot civil service reform through the design of a new job classification and remuneration policy for high-ranking state officials	Fulfilled
DPL IV	◆ Implement Medium-Term Expenditure Framework with a system of clear forward estimates for the 2008 budget	Fulfilled
	◆ Continue to consolidate core government (revenue and expenditure) bank accounts	Fulfilled
	◆ Implement transparent accountability arrangements for RDI and RDA accounts	Fulfilled
	◆ Fully operationalize NPPO and issue draft procurement law	Fulfilled
	◆ Complete the regulatory framework for issuance of sub-national government bonds	Fulfilled
	◆ Establish a Remuneration Commission or interdepartmental team to recommend pay policy and pay levels for high-level state officials.	Fulfilled
	◆ Develop a comprehensive civil service reform plan on a larger scale	Fulfilled

Source: Implementation Completion and Results Report for DPL I - IV, World Bank, January 30, 2008

3.2.1.4 Evaluation of Action Performance

A series of DPLs have continuously assisted in the long-run improvement of public financial management by providing its implementation framework and overall support coupled with separate technical cooperation. DPL I-IV is the first phase of a long-range process, which efforts are to be continued by succeeding DPL phases. All policy actions at each stage of DPL I-IV have been taken as expected and their fulfillment should be evaluated as satisfactory. As summarized in Table 3, the evaluation of the Project Completion and Results Report of the World Bank also concluded that all actions in the area of public financial management have been fulfilled.

3.2.1.5 Improvement Effect of Taken Policy Actions

As discussed in previous sections, stable steps toward total PFM improvement are observed by the satisfactory performance of action taking. However, the improvement process has a long way to attain the final goal, which is intended to be continued by succeeding DPLs V-VII. Accordingly, tangible effects in their respective fields of implementation have not yet clearly appeared up to now.

The Program Document for DPL VI (August 2009), which details the latest status at the time of this evaluation, reports the current conditions of the major areas of PFM to be as follows:

(1) Improvement of Budgeting System

1. Budget Formulation

The jointly developed operating manual by BAPPENAS and MOF for implementing MTEF and Activity/ Performance-Based Budgeting (PBB) was completed, and

dissemination activities to line ministries and other government agencies are ongoing. In addition, Budget Submission Templates (RKA-KL) have been prepared to simplify budget submissions and link them more closely to programs and are going to be piloted for budget formulation in six ministries in the 2010 fiscal year. Concurrently, Directorate General Budget of MOF will collect budget documents prepared under the new framework and analyze their properness.

2. Budget Execution

As discussed above, steady progress in the area of planning and budgeting reform based on MTEF and PBB has been observed. On the other hand, the progress of improving weaknesses in the field of budget execution is not so satisfactory and 50% of capital expenditures are still occurring in the last quarter of the fiscal year. To improve this situation, the government is planning to introduce an IT-based 'State Treasury & Budget System' (SPAN) and succeeding DPLs coupled with the technical cooperation GFM RAP will also support that effort. Its turn-key contract was signed in July 2009. However, the idea to solve the problem at one time through reliance on a single IT technology system, with poor attention to practically attack field issues, should be carefully reviewed.

(2) Treasury Single Account (TSA)

DPL I-IV has improved the previous situation where more than 18,000 bank accounts and other accounts unknown to the government were handling government funds; TSA has been achieved for the time being. However, the annual census on the government's bank accounts revealed that there are still a large number of accounts prevailing outside the coverage of TSA. In addition, the current TSA arrangement does not adequately cover bank accounts used for revenue collection. Thus, the completion of TSA still remains to be solved as a future problem.

(3) Improvement of Public Procurement System

The National Public Procurement Office (NPPO) in BAPPENAS was established in December, 2007, and its organizational arrangement and staffing is shortly going to be finalized. Activities have already partially started. Time is needed to complete the basic Procurement Law. However, the preparation of individual subsidiary procurement rules is progressing. The biggest bottleneck is a lack of human resources with adequate knowledge and capacity, which awaits a future solution.

Although tangible improvements in effect in their respective fields has to await the further

progress of actions required to be taken in succeeding DPL phases, it can be concluded that steady steps of improvement toward the goal are clearly recognizable.

3.2.2 Improvement in the Investment Climate

3.2.2.1 Approach to Evaluation

The Indonesian government has been recognizing that increased investment is a matter of the highest priority and has set improvement of the investment climate as an important policy agenda. DPL I-IV sets improvement of the investment climate as one of the principal pillars of the reform agenda and aims to promote investments in Indonesia through this. In DPL I-IV, JICA has attached particular weight to improving the investment climate. In the process of policy matrix formulation, JICA had policy dialogues with Japanese companies in order to identify problems in trade and investment and intended to reflect those issues in formulating policy actions with the Indonesian government and development partners. This evaluation focuses attention not only on the results of process evaluation conducted by the World Bank (focusing on the progress of actions taken and analyzing whether or not policy actions have been carried out as planned), but also on whether or not the effects of policy actions taken have been appearing on the ground. To be more precise, in this evaluation interviews with Japanese companies considered as beneficiaries of reforms were conducted; both quantitative data, as well as the actual voice of the relevant stakeholders gathered through various interviews, are used as sources of information to assess the effects of reforms on the ground.

3.2.2.2 Reform Targeted by DPL I-IV

DPL I-IV aimed to reduce the transaction costs of business operations, strengthen the financial sector and develop infrastructure in order to improve the investment climate. The followings are the main areas where policy actions were carried out during DPL I-IV:

- (i) Tax administration and customs reform
- (ii) Financial sector reform
- (iii) Regional tax items reform
- (iv) Public-Private Partnership for infrastructure development
- (v) Policy reform on SME development

3.2.2.3 Implemented Policy Actions in DPL I-IV

Improvement of the investment climate will not only contribute to promoting Indonesian's economic growth but also to benefiting companies operating in Indonesia. Therefore, improvement of the investment climate has been one of the reform item pillars throughout DPL I - IV. The following table shows achieved items and agreed policy actions in each phase

of DPL I-IV.

Table 4 : Achieved Items and Agreed Policy Actions in Each Phase of DPL I-IV

	Achieved Items	Agreed Policy Actions
DPL I	<ul style="list-style-type: none"> • Progress in establishing a financial sector safety net • Progress in tax administration reforms (eg. Establishing large taxpayers office) 	<ul style="list-style-type: none"> • Continue progress of tax administration reform (legal reform etc) • Continue progress of establishing a financial safety net • Strengthen non-bank financial institutions • Develop a medium-term plan for infrastructure development that encourages public-private partnerships. • Develop a medium-term action plan and effective framework to coordinate the development of SMEs
DPL II	<ul style="list-style-type: none"> • Complete draft amendment of Law 34 to move from negative to positive list for regional tax item • Continue development of financial sector safety net • Strengthen non-bank financial institutions * • Develop a medium-term plan for infrastructure development that encourages public-private partnerships. • Develop a medium-term action plan and effective framework to coordinate the development of SMEs 	<ul style="list-style-type: none"> • Clarify legal status of local government-controlled corporations • Promote efficiency in domestic and international commerce • Continue development of financial sector safety net • Restructure Capital Market Supervisory Agency and Directorate General of Financial Institutions • Diversify financial sector • Improve business environment • Risk Management function to be fully operational
DPL III	<ul style="list-style-type: none"> • Clarification of the legal status of regional government enterprises * • Improving efficiency of domestic and international trade • Continuation of development of financial sector safety nets • Complete the reorganization of Bapepam/ DGFI • Enhancement of risk management (function to be operational and empowered) • Establishment of public- private partnership (PPP) 	<ul style="list-style-type: none"> • Implementation of supporting documents related to new investment law • Shortening of VAT refunding period for exporters • Issue Ministry of Finance (MOF) Decree on tax audit procedures that allows tax payers to request audit findings and a review in case of disputes • Streamlining of investment process • Issue a comprehensive SME policy package
DPL IV	<ul style="list-style-type: none"> • Preparation of detailed rules for the New Investment Law * • Shortening of the period taken for the refund of value-added tax (VAT) for exporters • Promulgation of Ministry of Finance order enabling the filing of objections concerning taxation • Expanded the target applicable to unification of windows for import and export • Improvement of policies for small and medium-sized enterprises 	<ul style="list-style-type: none"> • Preparation of detailed rules pertaining to the Investment Law, review of the list of persons ineligible to invest • Implementation of monitoring of the time required for VAT refunds and time for the process of the objection examination to taxation • Issue the decree on The Tax Administration Law • Study of appropriate customs tax rates and other import regulations by a customs tax task team • Improvement of the credit system for small and medium-sized enterprises

*Policy actions which were partially fulfilled

The above table was made based on information in the implementation completion and

results report and DPL I-IV program documents issued by the World Bank (ICR: issued on January 30, 2008), and on information in the Ex-ante Evaluation report and related documents on DPL I-IV issued by JICA. Except for certain policy actions, almost all of the agreed policy actions were implemented appropriately and achieved their policy objectives.

In addition above, operation and effect indicators set for DPL I-IV are summarized in table 5 below. The status column in the list was completed based on information stated in ICR and DPL I-IV program documents issued by the World Bank, and Ex-ante Evaluation report issued by JICA. Regarding progress of operation and effective indicators, targets were achieved in DPL I and II. In relation to the progress of DPL III and IV, targets related to “establishment of bureaus to promote implementation of PPP” and “investment to GDP ratio”, were achieved. However, the target related to days required to start a new business (30 days) – which is equivalent to that of Thailand and Malaysia – was not achieved, and the average number of days remained 76 at the end of the year 2008. Although the number of days required to start a new business did not achieve its target, certain improvement was observable by taking into account the fact that the days required to start a new business were shortened from 151 in 2003, to 76 in 2008.

Table 5 : Progress of Operation and Effect Indicators

	Baseline (2003)	Target	Status
DPL I	Develop a medium-term plan for infra-structure development that encourages public-private partnerships	• Development of a medium-term plan for infra-structure development	Fulfilled
DPL II	Risk management function to be fully operational	• FY2007 budget appropriation with respect to Public-Private Partnership (PPP) assistance	Fulfilled
DPL III DPL IV	• Investment to GDP ratio: 18.9% • Days required to start a new business: 151	• Establishment of bureaus to promote implementation of PPP • Investment to GDP ratio: 23%-25% • Budget for risk management appropriated in the 2006 revised budget and the 2007 budget plan • Days required to start a new business: 30 days	• Investment to GDP ratio: 26.0% • Number of days required to start up a new business: 76

- 1) Target for DPL was measured in 2005, DPL II measured in 2006, DPL III and IV measured in 2008.
- 2) Common targets were set for DPL III and DPL IV.
- 3) Figures in the status of DPL III and DPL IV cited from report on Ex-ante Evaluation of DPL V

3.2.2.4 Effects of Reform on the Ground

In assessing the effects of implemented policy actions, it is necessary to study whether or not implemented legal and institutional reforms have produced effective results. In the following section, the report focuses on effects of implemented policy actions in the area of tax administration and customs clearance and provides an evaluation of these areas based on

the qualitative information on effects of implemented policy actions on the ground collected through interviews with Japanese companies operating in Indonesia.

Tax Administration

The following table 6 shows items described in the policy matrix and concrete actions taken in the area of tax administration through DPL I-IV.

Table 6 : Policy Actions in Tax Administration Area of DPL I-IV

	Items in Policy Matrix	Concrete actions
DPL I	<ul style="list-style-type: none"> • Progress in tax administration reforms 	Establishing large taxpayers office
DPL II	<ul style="list-style-type: none"> • Complete draft amendment of Law 34 to move from negative to positive list for regional tax items 	Complete draft amendment of Law No. 34/2000 to clarify the authority of central and local government and to move from negative to positive list for regional tax items to restrict the creation of nuisance and/ or economically harmful charges and levies.
DPL IV	<ul style="list-style-type: none"> • Reducing the time for VAT refunds for exporters 	Improve VAT by, amongst other things, reducing time for VAT refunds through the implementation of the DG tax regulation No. 122/2006. 7878 VAT refund claims from previous fiscal years have been settled during the last 12 months.
	<ul style="list-style-type: none"> • Promulgation of Ministry of Finance order enabling the filing of objections concerning taxation 	Ministerial Decree on tax audit procedure and tax payer rights and accompanying regulations for implementation have been issued. Extended taxpayer rights are also embedded in tax law package as passed by Parliament in March 2007.

Source : World Bank Program document for proposed DPL I-IV

Implementation of the policy actions above contributed to improving transparency of tax administration law and to reducing the tax burden for companies by restricting the creation and arbitrary application of economically harmful charges and levies and by reducing the time needed for Value-Added Tax (VAT) refunds for exporters. On the one hand, in relation to the effectiveness of these legal and institutional reforms, a Japanese company stated, “Reducing the time for VAT refunds is only for export specialized trading companies and this company recognizes there is no change in the time required for VAT refunds”. Additionally, the company stated, “The payment of the required amount of VAT (10% on export and import offset amount in Indonesian Rupiah) means the same thing as having the same amount of account receivables in Indonesian Rupiah, which results in a burden on the company in terms of interest cost and exchange risk”. On the other hand, according to a questionnaire survey involving more than 500 enterprises in the major cities as carried out by the Social-Economic Research Institute of Universitas Indonesia (during June through August 2006): the number of days required for receipt of VAT refunds has been reduced from 6.3 months in 2005 to 5.1

months in 2007¹⁵. According to interviews with Japanese companies in Indonesia, a company pointed out, “Previously, it took 4 or 5 months to receive a VAT refund but this time has now been shortened by about one month, which brings economic benefits equivalent to several millions Japanese Yen”. Thus, in the real world of business, different views and actual feelings about the effects of the reduction in time for VAT refunds were expressed by different types of businesses.

In the interview with the Directorate General of Tax, speeding up of reform through monitoring as well as tax payer-oriented reform implementation, were pointed out as being an added-value of DPL and that, had it not been for the DPL program loan, reforms from the viewpoint of the tax payer – such as reducing the time for VAT refunds – would not have been prioritized in the reform agenda. Given the above remarks about the value of DPL, it can be concluded that including the VAT refund issue in the DPL policy matrix had a certain effect on reducing the time required for VAT refunds.

Regarding reform of tax assessment/ audit procedures, while previously taxpayers were required to pay 100% of the disputed amount in advance, Ministerial Decree on tax audit procedure and tax payer rights now allows taxpayers to appeal tax assessments and audits without having to pay 100% of the disputed amount in advance and, in fact, during interviews companies mentioned that they were allowed to appeal tax assessments without having to pay 100% of the disputed amount in advance – which means that effects of the reform reached and were recognized on the ground. However, some Japanese pointed out, “Even if the company wins in the tax court, the exact amount and when it will be refunded are unclear due to lack of a standardized refund procedure”. Considering the above, while DPL served to realize reform in tax audit and assessment procedures and the effects of the reform were perceived to a certain extent by companies themselves, further regulatory and institutional improvement in tax administration procedure is required in order for them to recognize that the tax administration procedure is functional in a truly effective manner.

Customs Clearance

The items described in policy matrix and concrete actions taken in the area of customs clearance are shown in the following (table 7).

While exporters and importers were previously required to individually apply to various governmental institutions such as customs offices, the Ministry of Commerce, Food and Drug Administration and quarantines: implementation of the policy action above has contributed to building a framework of integrated customs procedure allowing exporters and importers to apply through a single window. In addition, a pilot project for Tanjung Priok, which is the

¹⁵ Japan Business Council for Trade and Investment Facilitation, “Issues and requests relating to foreign trade and investment in 2009 - Indonesia”

largest trading port in Indonesia and handles about 60% of Indonesia's trade, was also implemented.

Table 7 : Policy Actions Relating to Customs Clearance in DPL I-IV

DPL IV	Expansion of the region where customers procedures are centralized	The blueprint of the National Single Window (NSW) has been released. A pilot project for Tanjung Priok, which handles about 60% of Indonesia's trade, is currently under preparation with a launch date scheduled for December 2007. (After pilot implementation of NSW, the number of governmental institutions joined increased from 5 to 15 and the areas increased by 4 ports)
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Source : World Bank Program document for proposed DPL I-IV

In relation to the assessment of reform in customs clearance procedure and effects of the reform on the ground, one person in charge of logistics in a Japanese company operating in Indonesia stated, "If it were not for the implementation of National Single Window (NSW: integrated custom clearance system) the visibility of the customs clearance process would still be very low and decisions on customs clearance left up to the discretion of customs officers, which might result in the situation that officials ask some fees to accelerate clearance of the corresponding cargoes through customs". Therefore, the implementation of NSW produced a certain positive result in the way in which the progress of customs clearance was visualized (Once the form for customs clearance is submitted, the information is automatically registered in the system, which allows users to track progress of customs clearance). Furthermore, according to a questionnaire survey conducted by the Social-Economic Research Institute of Universitas Indonesia, the number of days required for import customs clearance was reduced from 6.1 days in 2005, to 3.1 days in 2007¹⁶. In fact, Japanese companies expressed similar recognition on the number of days required for import customs clearance. In interviews with Japanese companies they mentioned, "The number of days required for import customs clearance is shortened by one day and import items are now cleared on the same or the next day after implementation of the NSW system". Japanese companies also pointed out, "One day reduction for customs clearance contributes to cutting a day's inventories¹⁷, saving a day's storage space, reducing man-hours for inventory control and improving productivity by reducing a day's manufacturing lead time".

While some Japanese companies positively assessed the change in customs clearance, other Japanese companies pointed out various problems. For example, minor errors in customs documents results in all the items shipped in the same lot being stopped in the clearance

¹⁶ Japan Business Council for Trade and Investment Facilitation, "Issues and requests relating to foreign trade and investment in 2009 - Indonesia"

¹⁷ Some Japanese companies point to the fact that the cost burden of having one day's excessive inventory is not small, given the 7% interest rate in Indonesia.

process. Other problem raised by Japanese companies include numerous cases of differences of views over the HS Code and preferential tariff application, as well as changes and enforcements of law and regulations without enough coordination with related governmental institutions and time for dissemination. Considering the above, it can be assessed that, whilst policy actions were taken to reduce the number of days required for import customs clearance and to streamline customs procedure and that the effects of the action taken were recognized on the ground, further improvements in investment climate are still needed to attract foreign investments.

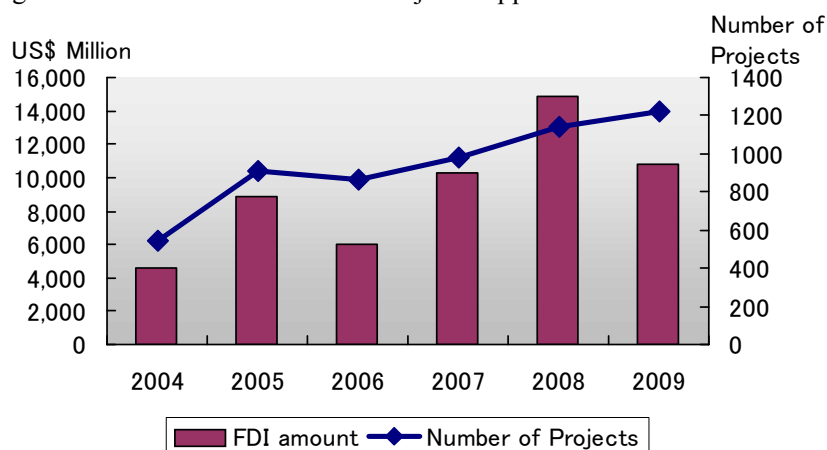
3.2.2.5 Trend of Investment-Related Macroeconomic Indicators

Generally speaking, it seems that an improved investment climate has positive impacts on the amount of trade and investment. However, various external factors such as world economic trends and individual corporate strategies can have an effect on both the decision and actual amount of investment. Therefore, improved investment climate through implementation of policy actions does not necessarily lead to increased investments. As explained above, it is almost impossible to separate JICA's contributions to improved investment climate from others and to exactly measure only its contributions in the DPL since various external social, political and economic factors both positively and negatively affect improved investment climate. However, DPL I-IV has contributed to solving issues in tax administration and customs clearance, which improvements have a great impact on the business activities of companies operating in Indonesia through the related institutional reforms. Furthermore, during interviews with Japanese companies, one of the beneficiaries of the reforms, recognition was expressed that they had found certain improvement in the area mentioned above.

In addition, figure 8 shows the number of investment projects approved and their value in USD. Compared with the number of investment projects approved and their value in 2004, when the DPL started, and those of 2008, when DPL IV was implemented, a great increase in both has been recorded. Furthermore, as indicated in figure 9, the volume of trade between Indonesia and Japan largely shows an increasing tendency¹⁸ throughout the period of DPL I-IV.

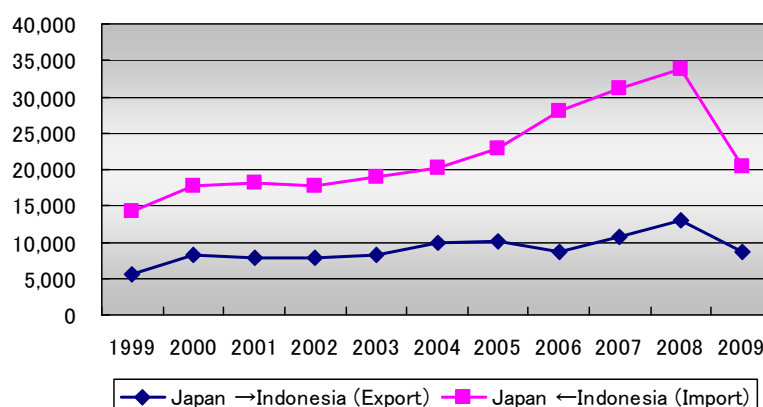
¹⁸ Significant drops in the amount of both export and import in 2009 would be largely a result of an exceptional factor: namely, international financial and economic crisis being triggered by the United States.

Figure 8 : The Number of FDI Projects Approved and their Amount¹⁹



Source : BKPM

Figure 9 : Volume of Trade between Japan and Indonesia



Unit: hundred million JPY. Source: Trade Statistics of Japan

3.2.2.6 Effects for JICA

The High Level Public/ Private Sector Joint Forum on Investment was launched for promoting foreign investment, especially that of Japan, in 2004. The forum prepared SIAP, which consists of concrete actions affecting business operations – such as a reduction in the time required for VAT refunds and speeding-up of customs clearance procedures. The DPL program has created pushing effects to support progress in the reform agenda of the government of Indonesia and, through policy dialogue, JICA has contributed to these reforms by including some actions from SIAP into the policy matrix after DPL III.

Apart from JICA's contribution to an acceleration of the reform agenda, mutually complementary efforts – such as the technical cooperation project for modernization of tax

¹⁹ Both the number of projects and its amount are approval basis. FDI in oil & gas, banking, non-bank financial institutions, insurance etc is excluded from the figure. Drop in the FDI amount in 2009 would largely depend on the impacts of global financial crisis that occurred in 2008.

administration and dispatch of experts with DPL I-IV – have been implemented in the area of tax administration and customs clearance reform. Considering the above, the DPL I-IV program was effective from JICA’s point of view.

3.2.2.7 Conclusion: Achievements Regarding Improved Investment Climate

Several Japanese companies expressed the view that, “The reforms of investment climate go in the right direction but Indonesia’s investment climate has been improving at a very slow pace.” From the viewpoints of companies operating in Indonesia, the pace of the improvement is far from at a good rate. However, if it were not for DPL I-IV, it would be difficult to share concrete concerns about problems on the ground – such as reduction of time required for VAT refunds, with the so-called “champions” who are reform promoters within the government of Indonesia and it would also be difficult to realize reform. Therefore, this report positively assesses the progress of the reforms, rooted in concrete awareness of the problems on the ground. It is the assessment of this report that DPL I-IV has contributed to improving Indonesia’s trade and investment climate through reducing the time required for VAT refunds, visualizing and streamlining the customs clearance process and that it has also indirectly contributed to increasing investment in Indonesia. It is neither possible to find the direct causal relationship between DPL I-IV and the increased amount of investment in Indonesia, nor to quantitatively measure the contributions of DPL I-IV. However, investment related macroeconomic indicators show steady performance, although significant drops were recorded in 2009 due to the global financial and economic crisis. Furthermore, as explained above, several Japanese companies stated that reforms in the investment climate were proceeding in the right direction and that, from the viewpoint of Japanese companies, several effects had appeared and were recognizable on the ground. Considering all of the above, this report concludes that the effects of the taken policy actions were apparent on the ground in the area of improvement in the investment climate. However, it is worth mentioning that no Japanese company, interviewed in the field study, recognizes JICA’s efforts to improve the investment climate through DPL I-IV. From the viewpoint of promoting both collaboration with the private and public sectors and PPP, sending out and sharing information about DPL initiatives with the private sector (especially to Japanese companies operating in Indonesia) would be advisable.

3.2.3 Poverty Reduction

3.2.3.1 Approach to Evaluation

Policy actions regarding poverty reduction have been added from DPL III as a fourth DPL pillar, “Service Delivery”. Because policy actions have been achieved after DPL III, DPL III and IV are taken up in this report. As information gathered during the field survey – including

interviews with relevant parties – were limited in terms of undertaking a full assessment for poverty reduction, a relatively large number of references have therefore been made to existing documents including the World Bank’s Program Documents and Implementation Completion and Results. Review of relevant research surveys related to DPL policy actions has also been made in order to formulate an evaluation of achieved actions.

3.2.3.2 Reforms Targeted by DPL III-IV

This reform area aims at improving the quality of public expenditure and improving basic social services and access for the poor, thereby facilitating the achievement of MDG goals on poverty reduction. The Indonesian government has been considerably increasing its public spending on social sectors including education and health since 2005. However, sufficient improvement has not been taking place. Moreover, in an assessment that was made of more than fourteen poverty programs, it was identified that some were ineffective. Therefore, monitoring and evaluation of these poverty programs was required: to improve the programs and to change resource allocation based on an evaluation of their results so as to enhance the efficiency of resource utilization and to facilitate greater achievements. In addition, strengthening financial resources for local government was necessary, especially for the development of local infrastructure. In order to resolve these issues, relevant policy actions were identified to facilitate reform under the DPL framework.

3.2.3.3 Implemented Policy Actions in DPL III-IV

(1) Monitoring Related to the Implementation of Compensation Programs

Independent evaluation of compensation programs for the poor, which were introduced at the time of a rapid increase in oil prices in 2005, was conducted. A concrete, rapid evaluation of a cash transfer program that ultimately reached 19.1 million households was conducted (in December 2005) and its results were utilized by BAPPENAS for future improvement of the program. Qualitative assessment of education, health and rural infrastructure programs for the poor, were respectively conducted (in June 2006), and the results were utilized as inputs for succeeding planning and budgeting of the programs.

(2) Establishment of Standards for Granting Teacher’s Licenses

Based on the 2005 Teacher Law, the National Education Standards Board has written standards for each subject within the school curriculum. A ministerial decree (Kepmendiknas No. 18/2007) formalized these standards for teacher certification and the mechanisms and instruments for certification. The Ministry of National Education began the certification process for about 190,000 teachers in July 2007.

(3) Preparation of Regulations for Issuance of Local Bonds

This policy action aims at strengthening local governments' financing mechanisms, including sub-national government bonds, as part of enhancement of local public service delivery in closing Indonesia's infrastructure gap. Local governments are granted the issuance of local bonds by Law No. 33/2004 on Fiscal Balance and by Government Regulation No.54/2005 on Regional Borrowing. In addition, the Ministry of Finance has issued further details on the regulatory framework (in 2006), for local government bonds via Minister of Finance Decree No.147/2006. Furthermore, the MOF's Capital Markets Regulatory Agency has released six decrees on various technical aspects related to the issuance of sub-national government bonds.

The list of policy actions and their status under poverty reduction for DPL III and IV are summarized as follows.

Table 8 : Action Performance of Poverty Reduction

	Policy Actions	Status
DPL III	◆ Monitoring related to the implementation of compensation programs	Fulfilled
DPL IV	◆ Establishment of standards for granting teacher's licenses	Fulfilled
	◆ Preparation of regulations for issuance of local bonds	Fulfilled

Source : Implementation Completion and Results Report for DPL I - IV, World Bank, January 30, 2008

3.2.3.4 Evaluation of Action Performance

As mentioned above, each policy action has been fulfilled and its progress can be evaluated favorably. The World Bank's Implementation Completion and Results Report also concluded all policy actions were fulfilled, as listed in Table 8. The monitoring result of more than fourteen compensation programs for the poor has identified those which were not effective, such as village infrastructure. Issues about duplication of programs and the need for strengthening targets for the poor, who should be provided services, were also revealed²⁰. Based on these results, shifting resources into programs that were stronger, such as PNPM (see below) and the direct cash transfer program, has become possible; the basis for implementing a more efficient poverty program may be said to have been formulated.

²⁰ According to a research study conducted in April 2010, that endeavored to quantitatively analyze the effect of IDT (Inpres Desa Tertinggal), one of the poverty programs, 22% of the program fund has not reached the intended poverty group and leakage has taken place at the village level. In addition, a positive correlation has been observed between the organizational capacity of villages and the extent to which the program fund has reached the targeted poverty group.

3.2.3.5 Improvement Effect of Taken Policy Actions

The establishment of a poverty reduction team under the Vice President by Presidential Instruction No.15 (2010) can be regarded as tangible change on the ground. The team has been in charge of coordination for overarching poverty reduction issues.

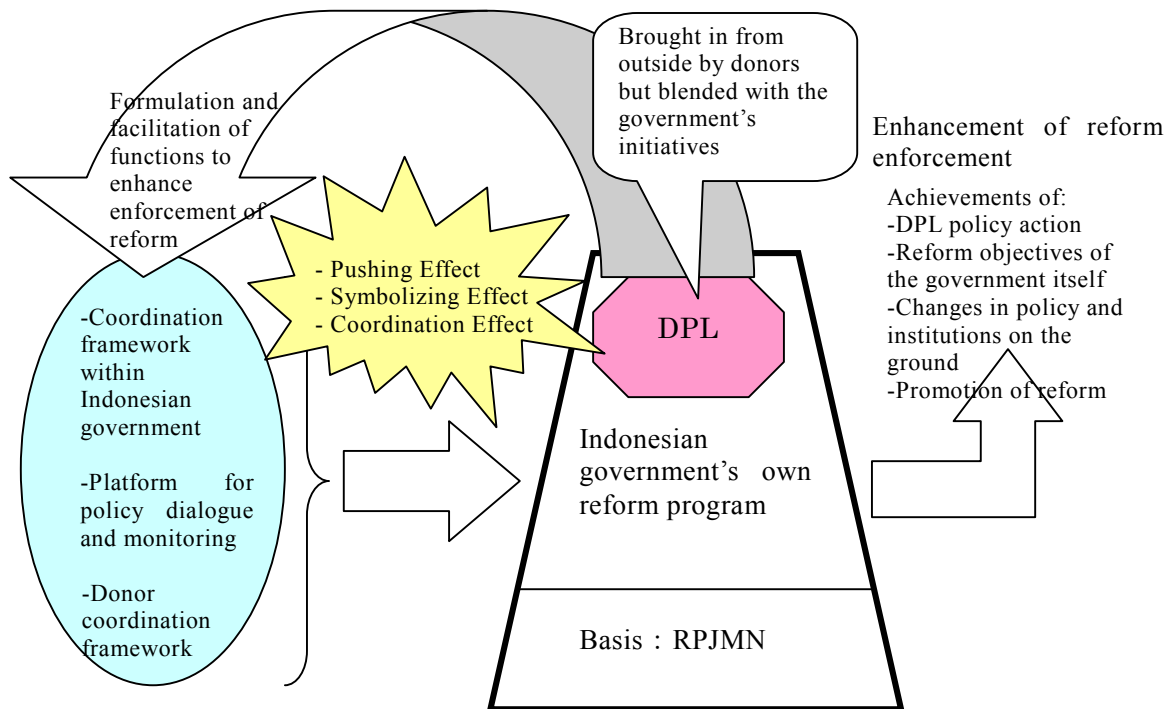
In the succeeding DPL V-VI, policy actions regarding the establishment of an evaluation mechanism for poverty programs, strengthening of financial sources, enhancement of social service delivery, and improvement of poverty targeting have been identified. These actions were built upon the initiatives for further reform under DPL III-IV. In addition, the Indonesian government itself has initiated the scaling up of its own existing poverty program (PNPM) from 2007. As reported above, the experience of monitoring of compensation programs for the poor, identified as policy action under DPL III, has become the basis for this. The Indonesian government has initiated a direct cash transfer program to 700 thousand poor households as a pilot initiative. The increase of community block grant under PNPM has become a benchmark action for DPL V.

3.3 DPL Attempts and Achievements (Rating : a)

This section looks into DPL's three effects: (1) the pushing effect; (2) the symbolizing effect; and (3) the coordination effect, which have been created out of DPL processes of policy dialogue, donor coordination and grouped institutional frameworks such as the organization of collaborative taskforces (evaluation of DPL achievements). These were the expected roles of DPL at the time of its inception and, during interviews, many government officers repeatedly emphasized that these very much represent the added value of DPL from the Indonesian government's point of view. Whereas on-going reform initiatives by the Indonesian government itself may have proceeded in the absence of DPL, functions to enhance the implementation of reform have been formulated and facilitated through DPL – which was brought from outside – and have come to be recognized as the above-mentioned three effects. Therefore, it is considered that DPL has fully achieved its intended objectives. This is evident from the remarks of relevant government officials during the field survey: “It was thought that Indonesia would graduate from DPL when macroeconomic stability was attained, however, the significance and added value of DPL are not only the funding effect but the reform facilitation effects. Considering the fact that reform issues are expanding and diversifying, as long as the credibility of DPL is secured and the Indonesian government is satisfied with its mechanism, Indonesia may not graduate from DPL for the time being.”

A conceptual diagram of DPL's three effects is shown below.

Figure 10 : Conceptual Diagram of DPL's Three Effects



In analyzing DPL achievements, counterfactual perspectives were taken in – what would have been the difference in the absence of DPL? Functions formulated and enhanced by DPL are described below. It is difficult to prove what would have happened to these functions if it were not for DPL. However, it is evident that these three effects were brought about by DPL and would not have been created if DPL had not been implemented. As mentioned in the previous section, progress of reform under each DPL area varies, but is generally moving forward. Therefore, it is considered that the contribution of DPL to facilitate reform was satisfactory.

3.3.1. DPL Pushing Effect

In the absence of DPL, the speed and degree of achievement of reform would not have increased as compared to those of the present situation in each area. This can be understood from remarks made by relevant government officials, “Possibly the champions in the government would not be able pursue reform so much, if the DPL pushing effect were not there.” As one of the pushing effects of DPL, the facilitation effect induced by the time pressure of setting deadlines can be considered as a good example. Because DPL requires the yearly attainment of policy actions in every year, based on its cycle, this time pressure is thought to create a facilitation effect. In other words, DPL and co-financing donors are considered to have played the role of an important catalyst towards promotion of reform. On the other hand, since the identified DPL policy actions also have restrictions concerning what

may be attained in one year, relevant government officials pointed out that policy actions tend to be fragmented and that grand design of reform cannot be easily understood when viewed throughout the DPL process. Although the existence of DPL is recognized by those (governmental high level officials) directly engaged in the process it is not, however, necessarily so for those at the working level. Since DPL is integrated with the government's own reform program, line ministries and agencies in charge of reform implementation have a tendency to take them as part of their overall reform agenda and so, too, its time management. Therefore, the actual effect of fragmentation of DPL policy actions is regarded as small.

Besides the facilitation effect as coming from time pressures, there are other DPL pushing effects. There were remarks made during the interview survey to the effect that DPL may push forward reform implementation by raising to a high-level recognition of reform issues which tend to be behind schedule, due to "various reasons", even when their priority is high in the government. For example, in the area of investment climate, the action related to the revision of negative list which was included from DPL V, was at the stage of waiting for political judgment – whereas preparation within the government was already fulfilled at working level. Under such circumstance, DPL was utilized to facilitate early political judgment from ministers and politicians, by highlighting this action within the DPL framework.

Concrete supportive remarks have been made regarding the DPL pushing effect as distinct from those of others involved in DPL and it can, thus, be concluded that the effect has fully materialized. In addition, it can be said that such an effect basically applies to all policy actions, not just in the above-mentioned case.

3.3.2. DPL Symbolizing Effect

The DPL symbolizing effect has been exerting satisfactorily. One champion in the government, who had a critical role in DPL I-IV implementation, indicated the DPL symbolizing effect as follows: "People look for signals and symbols. DPL is a symbol which sends out the strong commitment of government towards reform and the Indonesian government still needs this symbol in the future. Therefore, it is important that the government carries out its word and continues reform. This signal effect is not limited to the domestic audience, but also to overseas investors." Another government official indicated as follows, "The Indonesian government has been sending out the message, both inside and outside of the country, that it is facilitating reform, and strengthening transparency and good governance and moving towards international best practice through DPL. DPL is an effective symbol of reform." Furthermore, one donor indicated that, "DPL has played a role as a symbol of reform in the government. For those outside the government, DPL has contributed to strengthen trust in the Indonesian government moving towards reform."

These remarks, presented from those involved in the process of DPL, are highly persuasive

and deserve attention. The DPL symbolizing effect has the effect of showing the Indonesian government's commitment to reform, both inside and outside of the country, and is contributing to strengthen trust in the government. The effect is regarded as satisfactory.

3.3.3 DPL Coordination Effect

3.3.3.1 Coordination Framework within Indonesian Government

An enforceable coordination framework has been developed within the government through DPL implementation. Specifically, through the initiative of development partners, collaborative taskforces across ministries and agencies have been formulated in accordance with reform issues in the policy matrix. The taskforces monitor implementation of each policy action and reform progress. Government officials pointed out that: "Compared with the earlier stages of DPL, coordination within the government has improved and government officials have been exerting ownership and leadership in implementing DPL. The coordination capacity in the government is improving", and: "The DPL process has contributed to enhance the coordination function across ministries, agencies, and departments." The DPL coordination effect is worthy of note in the sense that it facilitates collaborative efforts among different ministries and agencies in order to achieve common objectives effectively and efficiently, by removing government structures which tend to become vertical divisions for each ministry and agency.

A concrete example of the DLP coordination effect may be drawn from NSW, a policy action mentioned under investment climate. The following remark was made in the interview survey: "The implementation of this policy action is led by the Director General of Customs and Excise, with the participation of relevant organizations on port, quarantine, and various licenses. In usual practice, it takes time to coordinate among the different organizations. However, by utilizing DPL, recognition by the ministers and vice ministers of this reform policy was elevated and, by getting their support, time schedule management would be conducted more effectively compared to the situation without DPL."

The Coordinating Ministry of Economic Affairs (CMEA) plays the role of being the focal point within the entire government. Under Deputy of CMEA, the steering committee is organized. The focal point for each relevant organization has become clearer for each reform issue and coordination has been facilitated. (See Figure 11)

According to an interview survey, government officials indicated that at the beginning of DPL it was unclear which organization would become the focal point for policy dialogue. However, CMEA came to undertake this role as more organizations participated. In fact, the focal point of the entire DPL program has shifted to CMEA as Indonesia's macro economy stabilizes. (See Table 9)

Figure 11 : Coordination Framework within the Government

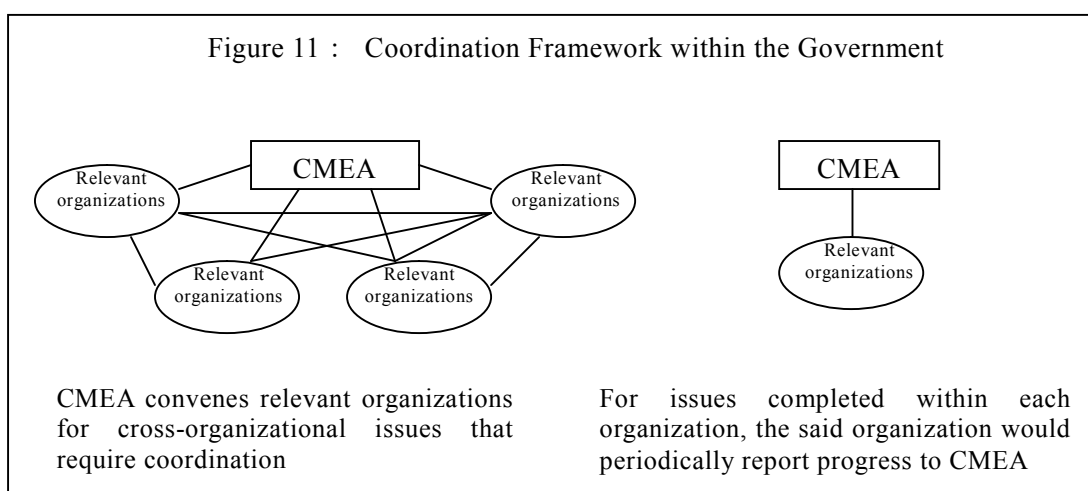


Table 9 : Focal Point in the Government for each reform area

Area	Focal Point
Macroeconomic Stability and Creditworthiness	MOF
Investment Climate	CMEA
Financial Management and Anti-Corruption	
Poverty Reduction	

On the other hand, there were remarks as to differences in recognition on DPL’s cross-organizational coordination function that exist between DPL core organizations (CMEA, MOF) and other line ministries. It is thought that the coordination effect in government would not have been exerted in the absence of DPL but that, however, coordination issues still exist. There were voices indicating that, “Incentives for participating in DPL are not very strong, since it does not bring specific project assistance.”

Reform may create people who lose vested interest and who may then become resistance forces in the government. Even though the coordination function within the government is strengthened through DPL, if the fundamental recognition of reform differs among relevant government officers, coordination may be hampered. This can be considered as a risk factor of DPL implementation.

3.3.3.2 Framework for Donor (Development Partner) Coordination

Donor coordination has been conducted with the World Bank being the focal point and with the participation of JICA and ADB as co-financing donors. According to the interview survey, a clear division of role among development partners does not exist and communication and coordination amongst them has been taking place in a fluid manner on a daily basis. As indicated in the interview, transaction cost among development partners has been reducing

through donor coordination in the DPL framework.

From the fact that substantial cooperation (conducting long interviews, offering related data and information, actively participating and contributing to the feedback seminar etc.) was given to the DPL evaluation mission by the World Bank and ADB staff in charge of DPL, it can be observed that a relationship of mutual trust has been built among development partners. Through a common DPL platform, cooperative relations among development partners are deepening, and consensus building is being developed to support Indonesia's reform. As support is provided based on the consensus of three large donors, it is considered that the significance of reform has been conveyed to the Indonesian government, leverage towards the government's reform initiative has increased, and the reform facilitation effect has been enhanced.

3.3.3.3 Coordination Between Indonesian Government and Donors / Development Partners

Since DPL I started in 2004, the program has been continuously provided every year up until DPL VII at the time of ex post evaluation. This fact shows that while transaction costs exist in implementing DPL, they are within a manageable level for both government officers and development partners. In other words, it is considered that a basis for healthy decision-making and policy dialogue has been reinforced through the DPL framework, and that transaction costs accompanying this have been kept within the level to which government and development partners can respond. In reality, it seems that DPL is designed to create incentives for both government and development partner sides to "achieve policy actions" and that, in this sense; the government side seems to be utilizing DPL to manage development partners effectively.²¹

3.4 Sustainability (Rating: b)

Sustainability is evaluated from three aspects: 1) sustainability of the DPL mechanism itself; 2) the functional sustainability of the DPL mechanism; and 3) continuity of JICA's participation in DPL. In consideration of the constraints, because of which this evaluation has more of the nature of mid-term review, it is difficult to assess the continuity of DPL policy outputs and outcomes. Given that the criteria for Indonesia's graduation from DPL have not been set, either at the time of appraisal or evaluation, it is uncertain until when DPL will continue. As such, analysis has been made taking into consideration the view that Indonesia may exit from DPL series in the future.

²¹ Donors leverage is not relatively strong for DPL (compared to the past IMF program). This comes from the nature of program design of DPL – DPL is to confirm whether policy reform which the recipient country is trying to tackle has actually been implemented. It is natural to think that DPL for the Indonesian government is a tool to efficiently gain ideas, knowledge and funding from donors, and its value added is in the "pushing effect", "symbolizing effect" and "coordination effect" that strongly back up champions within the government.

3.4.1 Sustainability of DPL Mechanism Itself

From the viewpoint of whether DPL can respond to the development issues which the government considers as highly critical policy issues from the big point of view, different opinions exist within the government. While DPL core organizations (CMEA, MOF) indicated that DPL could generally respond effectively to the important problems of each reform program, other ministries (line ministries etc.) called for more systematic measures –based on a grand design for reform rather than addressing the issues in a fragmentary way.²²

Provided that preparation of DPL VII was underway at the time of evaluation, both Indonesian government officials and development partners shared their observations that the level of identified policy actions has becoming smaller in scale as the round of DPL progresses. The fact that the level of policy actions has been getting smaller can be regarded as a consequence to which big reform issues are moving forward steadily, and the focus of each reform area is gradually shifting from a framework setting stage to an enforcement stage. On the other hand, when considering the original role of DPL – coping with the government's highly critical policy issues from a comprehensive viewpoint – it is desirable for project base loans and technical cooperation to take charge of the facilitation role of reform on the ground, in a complementary relationship with DPL. It is therefore important to consider DPL's balance, with project assistance, as to what extent DPL should take up concrete individual matters. From this viewpoint, sustainability cannot necessarily be considered as high.

3.4.2 Functional Sustainability of DPL Mechanism

The coordination mechanism within the Indonesian government (See 3.3.3.1) is highly valuable, not only for the future DPL operation *per se*, but also for the Indonesian government's overall policy making and reform initiatives over the longer term – after it graduates from DPL.

The government has translated such functions into their daily work – through enhancing communication and coordination mechanisms and strengthening channels for policy dialogue within the government as well as with development partners. On the other hand, there were indications that if it were not for the pushing effect and symbolizing effect of DPL, the pace of reform could have been slower, and that DPL therefore continues to be necessary. It is judged that time is still required for mechanisms fostered by DPL to secure sustainability within the government.

Strengthening institutional capacity through reform of public financial management, which is one pillar of DPL, plays a fundamental role in securing the sustainability of DPL. This is

²² However, it should be noted that the interviewees were those officials who were involved in the DPL operation at the time of evaluation, and their remarks were not based on their assessment of DPL I-IV.

because the management of DPL itself is performed through a healthy public financial management system as previously mentioned (See 3.2.1.1 Approach to Evaluation, footnote 12). Progress towards strengthening an extensive range of public financial management through a steady DPL process, and the systematized enforcement mechanism formulated and fostered to facilitate implementation of policy actions (See 3.3, Figure 10, Conceptual Diagram of DPL's Three Effects) is expected to take root in Indonesian government and can be considered to greatly strengthen the sustainability of DPL achievements.

3.4.3 Continuity of JICA's Participation in DPL

Criteria for judging sustainability for this aspect would be whether JICA can formulate good policy proposals for both countries that lead to Indonesia's sustainable economic development in the future – through making good use of the DPL mechanism as a platform for policy dialogue and deepening understanding of mid-term reform issues. Sustainability of JICA's participation in DPL is examined on the condition that Indonesia will graduate from DPL in the future.

In response to the question, “Would it be possible to identify some Indonesian officials and important persons with whom it would be difficult to hold policy dialogue in the absence of DPL?”, representatives from JICA Indonesia Office replied, “Although there is not necessarily any person that cannot be met in the absence of DPL, JICA does, however, enjoy the benefit of creating networks and holding discussions with key persons in each reform area on a regular basis where they gather in one place.”

To be specific, JICA Indonesia Office has secured channels for periodical dialog with important persons who have an important influence on the ministerial classes in the area of investment climate. Whilst obtaining the latest information on the government's reform initiatives, JICA can share issues on investment climate, which it considers to be important. Moreover, for cross-ministerial issues (rolling-out NSW and One Stop Shop for investment procedures, for example), identification of the key person has become easier and the efficiency of acquiring detailed information has been enhanced. Furthermore, on tax issues: “creation of guidelines for transfer pricing taxation system”, regarded as a high priority issue among private investors, has been identified as a policy action for DPL VII. In light of the fact that no other tool exists which requires government to ensure achievements within a specific timeline, it can be said that JICA has been taking advantage of DPL to facilitate reform.

In addition, there was an indication that, even if there were a case where proposals and opinions eventually did not become policy actions, the fact that JICA had conveyed and shared various proposals and opinions with government officials in DPL meetings proved

useful from the viewpoint of fostering awareness of the issues in the government. Furthermore, it should be noted that it has become possible to take up and put needs from the bilateral relationship between Japan and Indonesia on the multilateral table and to discuss them through the DPL framework. In other words, it has become possible to advance suggestions to the Indonesian government as general issues for improvement, which does not restrict the needs of Japan, through DPL's multilateral framework. Moreover, since the World Bank and Asian Development Bank do not necessarily take hold of concrete issues regarding the investment climate for business activities on the ground, Japan's concrete proposals to improve the business environment, which enables DPL discussions to reflect the reality of the situation, can be regarded as valuable.

Through remarks from JICA Indonesia Office representatives and experience from the evaluation process itself, many positive effects for JICA can be acknowledged from DPL – such as ensuring a channel for periodic dialog with government officials; expanding and enhancing networks; effectively acquiring important government information; facilitating reform through establishing specific time limits and effectively sharing and presenting issues which are of concern to JICA. To this end, JICA continues to possess incentives to support Indonesia's sustainable growth through participation in DPL and presenting suitably appropriate policy recommendations for both countries. From this point of view, until the Indonesian government graduates from DPL, the sustainability of participation in the DPL framework, for JICA, is high.

From a comprehensive standpoint, sustainability is regarded as modest. The difficulty which is inherent in DPL serves as a backdrop. DPL is a highly challenging program for all people concerned. Unlike infrastructure projects, the actual conditions and problems are not visible, and the reform process which DPL handles evolves dynamically in accordance with changes in incentives and balance of power among the people concerned. It is also subject to external factors etc. In addition, DPL reform deals with strengthening the country's total management capacity which, at the same time, is a premise of DPL implementation. Since sustainability of DPL cannot be discussed on the same dimension as that of infrastructure projects in view of the difficulty peculiar to DPL: sustainability is not necessarily regarded as high.

4. Conclusion, Lessons Learned and Recommendations

4.1 Conclusion

Although DPL is a highly challenging program and there is room to enhance sustainability by entrenching mechanisms that have been fostered through the DPL process within the government, the program as a whole is evaluated to be highly satisfactory as (A).

4.2 Recommendations

4.2.1 Recommendations to Executing Agencies

< Importance of the Role of Line Ministry / Agency >

Framework setting through DPL and improvement of service delivery on the ground exist in a complementary relationship for the facilitation of reform. Therefore, strengthening initiatives undertaken by line ministries becomes important. Line ministries participate in both the decision making process and coordination within the government through the DPL framework as well as having responsibility to implement reform on the ground. Therefore, in proceeding reform, it is important that line ministries become conscious of the two flows: from policy to field, and from field to policy.

< Importance of selecting policy actions that corresponds to the original role of DPL >

There were indications that the level of policy actions identified are becoming smaller in scale as the round of DPL progresses due to transition of reform from the framework setting to implementation stage. DPL is expected to cope with the government's highly critical policy issues from a comprehensive viewpoint. It is possible and desirable that project base loans and technical cooperation take charge of the facilitation role for reform on the ground. Therefore, when preparing policy matrix in the future, it is important to ensure balance between tackling concrete individual issues on the ground and the government's essential issues for reform.

4.2.2 Recommendations to JICA

JICA will be further expected to send out and share information with the private sector (especially local Japanese companies) about its DPL initiatives. No Japanese company which was interviewed recognized JICA's efforts to strengthen the investment climate through the DPL framework. It is also important, from the viewpoint of DPL sustainability, that JICA sends out such information to show that it is making continuous efforts through policy dialogue with the Indonesian government and that it is attempting to expand opportunities for collaboration with the private sector and the perspective of PPP.

The demand for economic infrastructure development that contributes to improving investment climate is continuously high in Indonesia. With improvement in economic standards, players and funding sources for infrastructure development are expected to diversify, and the preeminence of the market would proceed in this area. In such a situation, mobilizing private funds and knowledge and know-how become the key to future development. A trusting relationship with the Indonesian government, a framework for policy dialogue and rapport with high-level officials – which have been formulated through DPL –

can, for example, become important means to promote “package-type infrastructure exports” to Indonesia. By utilizing functions which have been formulated and strengthened through DPL and leveraging DPL, it is expected that JICA will, for example, firmly build foundations to realize package-type infrastructure exports from an All-Japan perspective through ascertaining the needs of government and maintaining close communication with government officials from the project identification and preparation stage. In order to advance such infrastructure development, further utilization of DPL is necessary to facilitate policy and institutional reform for improving the investment climate.

4.3 Lessons Learned

DPL is a program that contributes to framework setting, such as rules and regulations for policy and institutional reform. Therefore, no change would occur on the ground just by implementing policy actions alone. Enforcement of DPL’s targeted reforms would take place by carrying out finely-tuned technical cooperation (TC) on the ground. In other words, achieving DPL policy action is one thing, whereas facilitating reform on the ground is another. From the perspective of the donors DPL and TC are complementary with each other and are expected to generate synergetic effects throughout the various stages of the reform process. Now that new JICA has been established, through the JICA-JBIC merger, coordination between DPL and TC has been facilitated and opportunities are increasing for JICA to further utilize experts and actively participate in Indonesia’s policy and institutional reform. Therefore, it is crucial to bring into DPL policy dialogue the issues identified on the ground through TC. At the same time, in order to advance reform, it is equally important to hand on policy issues that have been discussed in the DPL framework to TC on the ground.