POVERTY REDUCTION STRATEGIES IN THE REGIONAL AND LOCAL AUTONOMY PERIOD IN INDONESIA

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Abstract

The paper addresses one of the most pressing constraints to development in developing countries, that of poverty reduction. This is considered within the broader framework of sustainable development, with the paper identifying poverty reduction approaches relevant to the Indonesian context, in terms of balancing assets and strengthening capacity at the local level. There are two main reasons why the study focuses on poverty. One is that despite remarkable achievements in economic development and well-being in developing countries over the past 30 years, poverty continues to be an unresolved and inexcusable problem. The other is that the level of poverty represents a practical indicator of progress towards sustainable development in developing countries.

There are two significant problems in the decentralization period that the poverty reduction efforts should deal with: the failure of Indonesia's planning framework to develop effective poverty reduction strategies at the local level and limited capacity of local governments to meet their responsibilities in accordance with the Law Number 22 of 1999 (the Regional Autonomy Law)[1]. Three approaches are used to answer the problems, i.e. the articulation of the social dimension under the broad objectives of sustainable development; the identification of indicators, using the P-S-R framework, for monitoring and assessment; and the formulation of the poverty reduction strategies within the local planning framework. The approaches are used to analyse and formulate poverty reduction strategies at the regional and, specifically, at the local level.

Introduction

Most analyses of Indonesia's economy over the past decade have been premised on the assumption that the rapid economic growth, of approximately 7 percent per annum, would continue (Feridhanusetyawan 1997). In the pro-growth environment of Suharto's New Order, remarkable gains were made in reducing poverty. However, the crash in the value of Rupiah in 1997 led to an economic and political crises that returned 25 percent of the population to poverty. Indonesia's pro-growth policies during this period did not work and could not sustain the previous achievements in poverty reduction. This paper addresses the questions of why the pro-growth policies in Indonesia were not sustainable and were not pro-poor. In particular, it focuses on the development indicators that can be incorporated into planning strategies and plans to prevent those failures.

To resolve these questions, this paper uses the Pressure – State – Response approach by first identifying the pressures or the causes of poverty in Indonesia. Second, the current state of the planning strategies that impact on poverty and other poverty related indicators are assessed. As the Regional Autonomy Law was implemented in 2001, the assessment will focus on the state of poverty and planning strategies at the regional and local level. Third, in relation to the response, the efforts to reduce poverty are analysed, including the formulation

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[1] It has been revised by the Regional Governance Law no 32, 2004

of poverty reduction strategies at the local level, particularly capacity building and institutional development.

Historical perspective

The unprecedented 'economic miracle' in the early years of Suharto's New Order, from 1967 to 1996, was due largely to the exploitation of industrial raw materials, i.e. oil and timber, which produced an income boom. Indonesian's GDP grew by an average of 7 percent per annum. This rapid growth was accompanied by a reduction in poverty from 70 percent in the mid-1960s to 17 percent in the mid-1980s. This period was characterized by political stability, partial economic liberalization and government intervention that lead to an increase in resource base exports, production of rice, mining and forestry. The rapid growth, in the context of economic development, also created inequality, which was formally underlined in a presidential speech to the People's Consultative Assembly in August 1978.

The economic success of the 1970s was instrumental in focusing the development of the 1980s on manufacturing. From the mid-1980s the economy experienced slower economic growth due particularly to the end of oil boom. However, poverty continued to decrease to 15.1 percent in 1990. This was due largely to the decline in rural poverty. This period was characterized by further economic liberalization primarily through deregulation of the national banking system (Mubyarto 2001).

The macro economic policies were based on fiscal liberalization (a fiscal deregulation in reaction to falling oil prices) (Touwen 2003) and were highly dependent on foreign loans. Poverty continued to decline to 11.3 percent in 1996 (Committee for Poverty Alleviation 2003). Since 1993, poverty alleviation programs were initiated based on a report by the Coordinating Minister for Economy and Finance identifying poverty pockets (*Kecamatan*/sub districts) and later reports prepared by the Central Bureau of Statistics.

Both economic growth and poverty reduction in Indonesia were interrupted by a sudden monetary shock in mid-1997. The economic growth rate dropped 13.7 percent to minus 7 (Pritchett, Sumarto et al. 2002), while the poverty rate escalated to at least 25 percent of the population in 1998 or about 50 million people (Asra 2000). The crisis was at first considered the result of the impact of East Asia's currency crisis in 1997. But the crisis in Indonesia turned into a multidimensional crisis including economic, social, natural and political crises that led to the resignation of President Suharto in May 1998. The impact of Indonesia's crisis is still evolving today, while other countries such as Korea, Malaysia and Thailand have substantially recovered. Indonesia's inability to respond more quickly to the currency shock indicates that there were other factors at play in Indonesia's development process.

The resignation of Suharto stimulated new initiatives to reform the governance system. In 1999 the Regional Autonomy Law was enacted and implemented from 2001. This has resulted in several powers and authorities being transferred from the central government to regional and local governments, including the responsibility for poverty reduction.

The approach

We argue that a balanced approach of policy-related poverty research will provide more effective poverty reduction strategies than current partial and sectoral approaches. Recent poverty research in Indonesia has been dominated by development economics. Most studies assessing the impact of the Indonesian crisis on poverty, such as Pradhan (2001), Skoufias et al. (2000) and Strauss,et al. (2002), have focused on the economic dimension of a particular period during the crisis. The consensus view of these authors is that the multi-crisis of the late 1990s significantly worsened the economic situation and escalated the rate of poverty. However, the root causes of the crisis were multidimensional, extending well before the 1997 currency crisis. Therefore, following Kanbur (2002) and Bevan (2003), this paper adopts a multi-disciplinary approach by shifting the focus from mainstream economics to an approach that articulates the social dimension within the broader context of sustainable development. Thus the paper focuses on the integration of the three dimensions, i.e. sociology, economy and environment, as proposed by current literature on sustainable development, such as the World Bank (2001), CSLS (2003) and Diaz (2003).

Fighting against poverty requires a good understanding of what constitutes poverty. This paper focuses on the cyclical Pressure-State-Response (PSR) framework (Figure 1). The 'pressure' factors are related to the causes of poverty in several periods of Indonesia's history starting from the beginning of Suharto's New Order. The analysis focuses on Indonesia's macro policies and the economic and political structures that affected long-term poverty reduction. The lessons from this analysis provide relevant indicators to prevent a repetition of these failures in the future.

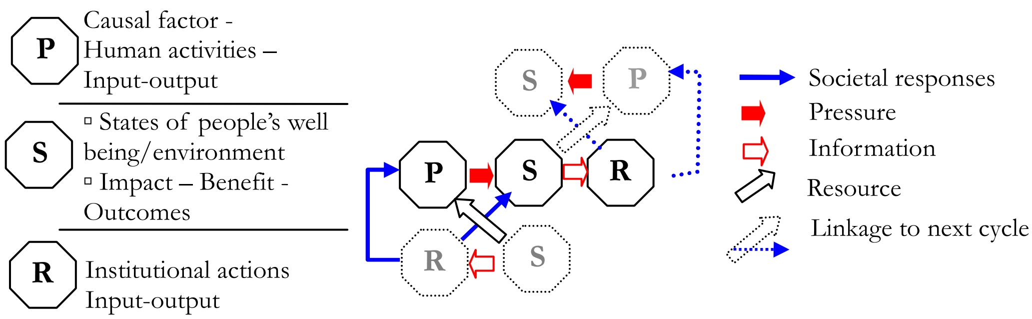

Figure1: the cycle of the Pressure-State-Response (PSR) indicator framework in relation to poverty reduction in Indonesia

The 'state' of poverty focuses on an evaluation of current (i.e. during the regional autonomy period) poverty indicators at the regional (the Province of East Java) and local level (the Municipality of Malang). While the analysis of the causes of poverty is mainly associated with macro policies and their impacts on poverty, the analysis of the state combines the macro policy and grassroots approach. Empirical studies (Pradhan and Ravallion 1999, World Bank 2000, Daimon 2001, Friedman and Levinsohn 2002, Jerve et al. 2003) show that macro policy approaches are not sufficient to guarantee the effectiveness of poverty reduction programs without incorporating grassroots approaches, including the qualitative perceptions of local people about their poverty. The responses from chronically poor people located in the Municipality of Malang are reported in this paper.

The 'response' is the formulation of strategy resulting from the macro policy and grassroots approaches. The former is important in providing strategic and operational policies, while the later contextually describes and explains the images of the poor at the community level, often in a long lasting poor area. It measures the indicators of capability poverty that provide the basis for more realistic programs and targets.

The pressure: the causes of poverty in Indonesia

The root causes of poverty in Indonesia, historically and politically can be divided into three periods: prior to the crisis; during the crisis; and post crisis/recovery. The crisis that stimulated the social and political momentum to enact the regional autonomy law, was a turning point that significantly affected poverty reduction in Indonesia (Figure 2), while the implementation of the law in 2001 provided the momentum that distinguished the crisis and post crisis/recovery periods[2].

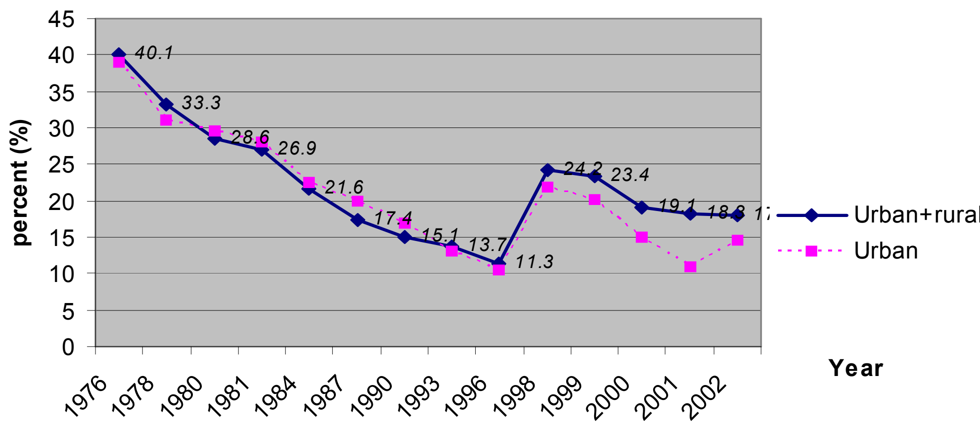

Figure 2: Changes in the percentage of the poor population in Indonesia, 1978 -2002
Source: Committee for Poverty Alleviation (2003); *Susenas* (1999)

The crisis, which doubled the number of the poor and left half of the population vulnerable to poverty (World Bank 2001), was caused by socio-economic and political factors in the pre crisis period. From the macro policy point of view, the failure of national policies contributed significantly to the economic turmoil of the mid-1990s. Many causal factors of poverty originate form the policies and governance deficiencies in the three decades of centralized and top-down approach government that focused on the paradigm of high economic growth. Three major policies that are highlighted here are economic structures, governance and the provision of public goods and asset development.

Economic structures

The pre-crisis period can be sub-divided into three stages: 1966-1973; 1974-1982; and 1983-1996. The first stage (1966-1973) was characterized by political stabilization and partial economic liberalization (free capital flow and foreign investment) (Touwen 2003). Government intervention policies were adopted in 1974-1982, while the third stage (1983-1966) was characterized by renewed economic liberalization and fiscal deregulation. Those policies increased national GDP and Indonesia became one of the 'East Asian economic

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[2] The term post crisis/recovery period does not mean that the crisis was over. Rather, it describes the ability of the people and the state to adjust their consumption expenditure in the on-going crisis. Current Indonesia's currency is still far from its pre-crisis level (Rp 2,200 to US$1)

miracles'. Those policies, however, did not trigger long-term economic improvement and created a vulnerable economic structure, which had a long term negative impact on poverty reduction goals.

A policy of free capital flow since 1966 increased the economic growth rate. However, the liberalization process was based on inappropriate sequencing. The introduction of free capital flow was accompanied by the government's repression of and intervention in the banking sector, which lessened the independence of the central bank (Indrawati 2002). As suggested by McKinnon (1993), capital control should be imposed at the final stage of the liberalization process, following macroeconomic stabilization, bank reform, and trade liberalization because balancing government's finances is imperative before privatization and financial liberalization can be introduced.

High economic growth in Indonesia was achieved in the second (1974-1982) and third stages (1983-1996). The growth was triggered by over-expansion in natural resource extraction and a boom in oil prices from 1973 to the mid-1980s. When the oil boom ended in the late 1980s, the government maintained high economic growth by introducing partial liberalization of the banking sector, as part of the fiscal deregulation. This increased the number of weakly structured banks, many of which had access to international finance (Mubyarto 2001). This liberalization, worsened by the so-called KKN (corruption-collusion-nepotism), resulted in an unrepayable debts of both the state and private debt to international financial institutions (Minister of National Planning Agencies 2003). This high level of vulnerability was influenced by the 1997 currency crisis and lead to long term multidimensional crises.

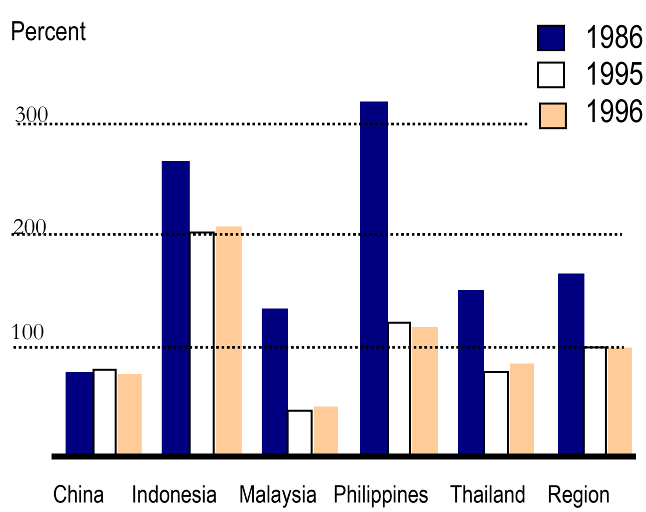

Figure 3: Debt to export ratio
Source: World Bank (1997)

The economic indicators such as annual GDP, experienced a growth of 7.1 percent between 1968 and 1997 (Cameron 2003), and masked the negative indicators, such as debt to export ratio and debt service ratio (DSR). The accumulation of debt from foreign loans, which Indonesia received from 1968, exceeded the capacity of the government to amortize the debt, and in 1999 Indonesia was for the first time unable to pay its instalment. Indonesia's debt to export ratio was the worst in the region (World Bank 1997); Jubilee Research 2002) (Figure 3).. Its debt was constantly over 200 percent of its exports, while other countries in the region had achieved a balanced ratio (100 percent)

Indonesia's debt service ratio (DSR) in the pre crisis period (1983-1996) ranged from 43 to 46 percent. The ratio was higher than the IMF's threshold of 20 percent. During this period the debt was higher than the national GDP, i.e. 147 percent of the GDP (World Bank 2000). These negative indicators, even though the GDP growth had recovered to about 4 percent, were continued in the crisis and recovery period with the DSR ratio ranging from 46 to 57.4

and from 45.3 to 52.5 percent respectively (Econit 1999; Times-Asia 2000; BUYUSA 2004). The accumulation of debt weakened the government's funding. In 2003, the interest on Indonesia's debt was higher than its development expenditures, and in 2004 the debt interest was still about 92.67 percent of the total development expenditures (Bappenas 2004)

Another economic indicator, which shows the weakness of the economic structures prior to the crisis, is the income gap. Income gaps between poor (agricultural employee) and rich (urban) households have not improved significantly. During the period of high economic growth (1983-1996), the gap increased from 1:3.66 to 1:8.48. The gap peaked during the economic crisis to 1:9.16.

Examination of these economic structures reveals that over reliance on a single aggregate economic indicator (the GDP), the dependency on foreign loans, over-exploitation of natural resources (Asra 2000), wrong sequencing of economic reform and ignorance of other significant indicators lead Indonesia into its economic crisis. Another important factor in Indonesia is that agriculture-specialized households represented 34 percent of poor Indonesians although they accounted for only 20 percent of its total population (Hertel et al. 2004). During the two decades prior to the economic crisis, significant reduction of rural poverty have contributed to total reduction of poverty headcount at the national level (Asra 2000). Therefore, agriculture sectors, which were not optimally developed during the second half of the high economic growth period, should have been given more attention in later periods.

Governance and public service provision

The poor are disproportionately affected by inefficient public service delivery, while the quality of public goods is fundamentally affected by the quality of governance. Three indicators of governance in Indonesia: democracy; rule of law and government effectiveness; and corruption (UNDP 2002), correlate to the quality of public services. The first indicator, democracy, during the recovery period was moderate, while indicators of the rule of law and government effectiveness were lowest among the neighbouring countries. An inability to fight against corruption indicates the weakness of the rule of law in Indonesia. High levels of corruption in Indonesia[3] indicate weakness in the institutions and show inefficient bureaucracies (Kaufmann, Kraay et al. 1999; Hamilton-Hart 2001; OECD 2001). Hence, it is important that graft and corruption in Indonesia are overcome, otherwise programs and projects, which are mainly funded by foreign loans, will be ineffective. The anti-corruption institutions, which have been reformed five times since 1957[4] (Kompas 2005), and the non governmental organizations such as Indonesian Corruption Watch (ICW) aim to identify and eradicate corruption in Indonesia. However, corruption has been and still is the root of many of Indonesia's current problems.

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[3] Indonesia was listed by the Transparency International as one of the ten most corrupt countries in the world (Transparency International 2004)

[4] The first state institution to eradicate corruption was established in 1957 through the command of *Panglima Penguasa Militer* (the commander of military authority), then subsequently was reformed as: Corruption Eradication Team in 1967 through the Presidential Decree No 228; Four Commission in 1970 through Presidential Decree No 12; Order Operation in 1977 through Presidential Instruction No 9; Corruption Eradication Integrated Team (*Team Gabungan Pemberantasan Tindak Pidana Korupsi*/TGPTK) in 1999; and currently is the *Komisi Pemberantasan Korupsi* (KPK) /Corruption Eradication Commission.

In relation to public services aimed at reducing poverty, prior to and during the crisis, the central government conducted two main programs, i.e. benefits in kind and job creation. These programs accounted for less than 2 percent of the total government expenditure (Daly and Fane 2002). The criticism of these programs is that most of the solutions were partial and based on case by case problem solving, such as *Inpress Desa Tertinggal* (IDT) - a job creation program literally translated as the Neglected Villages Program, which aimed to reach out to the parts of the country that were underdeveloped. Lessons from the implementation of IDT during 1994-1996 suggest that the program failed when the empowerment of local communities was insufficient. The failure could have been prevented if the program had been fully decentralized (Daimon 2001).

During the crisis and thereafter, the total spending for anti poverty programs increased to 9.67 percent of the total government expenditure. The most beneficial anti poverty program was the social safety net (SSN) program. These programs increased government spending from 0.3 percent of GDP in 1997/98 to 1.4 percent of GDP in 1998/99 and benefited most of the poor. However, a significant amount of funding was not allocated to the SSN program, but rather was focused on a variety of ineffective government subsidies and bank restructuring (Figure 4).

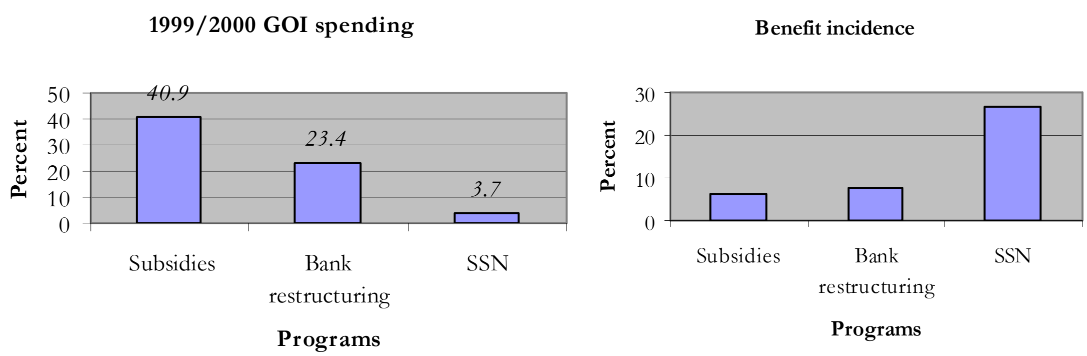

Figure 4: The Government of Indonesia spending and who benefited (World Bank 2001)

Two significant public services to poor people, within the government's social expenditure, are education and health. Health and education have instrumental values (direct impact on the main asset of the poor) and intrinsic values, which are important in improving individual capabilities and freedoms (Morrisson 2002). The main weakness of health and education service provision in Indonesia is related to the state's investment, which is lower than that in ASEAN and other East Asia and Pacific countries. The *Bappenas* estimates that in order to catch up other ASEAN countries, Indonesia should increase its social expenditure about 3 percent of GDP. This would need to re-orient budgetary priorities. The benefit of these two services to the poor is mainly provided by the primary facilities (primary education and primary health facilities), while the benefit of higher education, tertiary education and hospital services goes to the non-poor (World Bank 2001; Ministry of Finance 2003).

<u>Assets capability</u>

Before the crisis, Indonesia was estimated to have a proportion of 75:12:13 for its human/social, natural, and physical capital. The composition was similar to the decomposition of capital in wealthy countries (Central and North America, Western Europe and East Asia) (Kunte, Hamilton et al. 1998). In terms of the development of human capital, Indonesia is grouped in the medium human development countries. The share of human resources within the decomposition of capital asset during and after the crisis was lower than the pre crisis period due to the increase of open unemployment and poverty.) Since the first National Human Development Report in 2001, Indonesia's Human Development Index (HDI) rank was lowered from 102 in 2001[5] to 110, 112, and 111 in 2002, 2003 and 2004 respectively (UNDP 2002; UNDP 2003; UNDP 2003; UNDP 2004; UNDP 2004).

Another issue related to human development is the uneven distribution of development between males and females. Women, particularly in poor households, are often excluded and their contribution to household income is undervalued (McGee and Norton 2000; Narayan, Patel et al. 2000). More female headed households are found in poorer households. Therefore female headed households are more vulnerable to shocks and are more at risk of poverty (Pritchett et al. 2000). Indonesia's Gender Development Index (GDI) in 2002 was 0.685 and was ranked 90. This rank was lower than the neighbouring countries of Singapore, Malaysia, Thailand, Philippines and Vietnam.

Abundant natural resources are available in Indonesia, at both the national and local level. In the region, an estimate of natural capital per capita in Indonesia shows that Indonesia's natural capital per capita is moderate, lower than Malaysia, Thailand and Papua New Guinea (PNG), but higher than the Philippines and Vietnam. In terms of resource management, the problem is that a high proportion of the benefits from those natural resources does not go to the poor, but rather to foreign investors (Kitazawa 1990; Tadem 1990); FWI[6] 2002).

Financial assets of the Government of Indonesia are very weak due to the debt incurred by the public and private sector. The national budget for development is about 30 percent of the total expenditure, while about 70 percent is allocated for salaries, materials and interest payment. The central government's expenditure for project financing in 2003 and 2004 was less than half of the expenditure for salaries (The Department of Finance 2004). The same pattern occurs at the regional level.

<u>Some lessons related to the causes of poverty in Indonesia</u>

The examination of the causes of poverty in Indonesia shows that the sharp increase in the rate of poverty in the late 1990s did not happen by accident. The shock was temporary. Therefore, the multi dimensional crises entailing the 'long-term economic shock' can be attributed to the failure of the system or lack of good governance. Despite the high economic growth in the two decades from 1976 to 1996 and the reduction of poverty (mainly rural poverty), Indonesia suffered from several weakness and vulnerabilities in both its macro economic policies and banking sector. The weakness in its economic policies resulted in long lasting income inequality and regional imbalances, while the weakness in the banking sector, interwoven with the endemic corruption, heavily weakened the government's spending on anti poverty programs.

The lessons from Indonesia's anti poverty programs and their interrelation with the human development outcomes are:

[5] Using data in 1999

[6] Forest Watch Indonesia

- social safety net which included OPK (special market operation), scholarship and health programs, were efficient in protecting the poor from hunger and improved human capital;
- investment in human capital is important since its externalities, in the long run, will effectively reduce regional imbalances (Garcia and Soelistianingsih 1998); and
- the implementation of the IDT (job creation program) suggested that if the program was decentralized it would be able to prevent the targeting policy failure.

Indonesia's economic crisis confirmed that the macro policies should aim to return to not only economic growth but also greater equality, particularly by reducing poverty. In the decentralization period, sustainable poverty reduction in Indonesia needs a comprehensive but workable poverty monitoring system through improving strategic vision for poverty reduction, supported by readily but reliable data at the district level.

The state: poverty measures at the regional level and local level

Since the Regional Autonomy Law (check that this is upper case in all instances) has been in place (2001), regional and local governments have been responsible for reducing poverty. Three main themes will be addressed relating to the causal factors of poverty: economic structures; governance and public services; and asset capability, with their derived indicators, as discussed in the previous section, will be examined in the macro policy approach, while the grassroots approach will examine the those dimensions perceived by the poor.

<u>Macro policy approach</u>

The first theme is the outcome indicators of the macro economic policies. The overall pattern of the economic structures at the regional and local level resembles the pattern at the national level. Trends in GDP growth were similar to those at the national level because the national economy, particularly in relation to financial management, was heavily influenced by centralized decisions. Regional inequality, shown by gross regional domestic product (GRDP) per capita, household consumption expenditure per capita, and gini ratio continue to mark the economic development in East Java. The gap between local regions within the *SWP* (development region unit) was also constantly increasing (The Government of East Java Province 2002) (Figure 5). If the trends of the process of convergence in spatial inequality at the provincial level continue, it might take about 40 years to halve the gaps (Islam 2003).

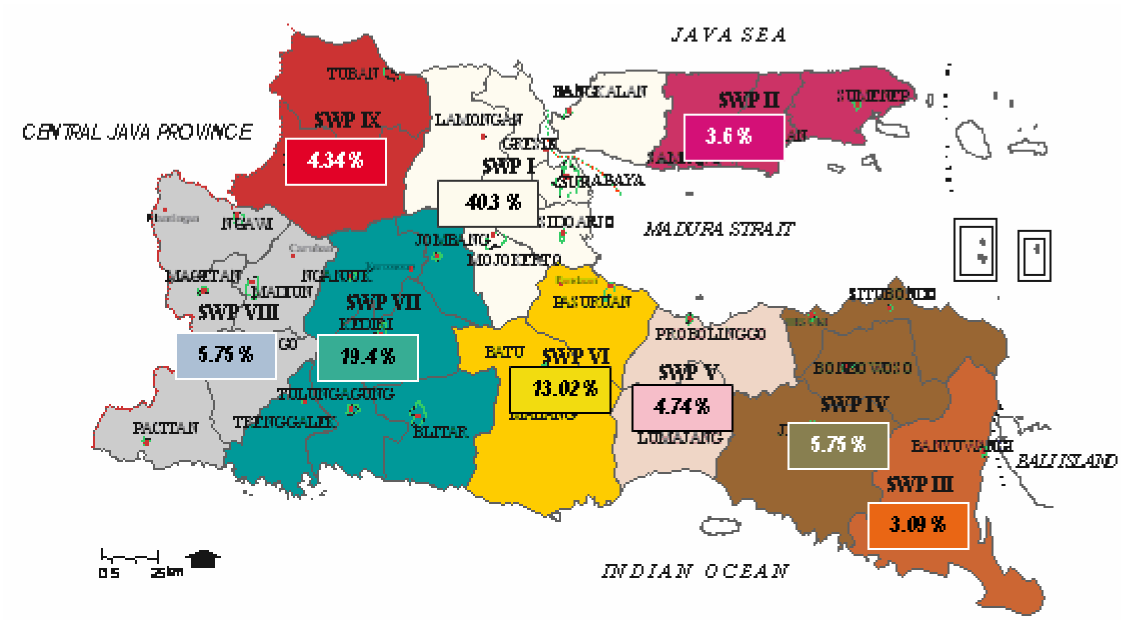

Figure 5: Regional inequality of the share in the GDP
Source: RTRW (regional spatial planning) of the Province of East Java 2002

Another acute problem is fiscal dependency of the regions to the central government. Prior to the decentralization, governments at the provincial and local level could not (or were not allowed to) manage their fiscal resources independently. Regions had low capacity to generate domestic revenue. The regional domestic revenue in East Java, since the crisis to 2002, was around half of its total budget, while the capacity at the local level was even lower. The average domestic revenue at the local level was less than 20 percent of their budgets.

The previous section suggests that the economic growth should be pro-poor. High growth in GDP is necessary, yet greater equality and poverty reduction are also important. The economic growth is pro-poor if it creates opportunities for the poor to improve their assets. Lessons learned from the recent economic crisis indicate that many of the poor 'were helped' by the activities of small and medium enterprises (SMEs), which responded more quickly to the monetary shock than large companies because they were less reliant on formal markets and formal credits (Berry, Rodriguez et al. 2001). The contribution of SMEs tended to be stable during the crisis and gradually increased from 2000 to 2002, i.e. from 48.43 percent to 50.12 percent of the GRDP at constant price. The economy in a country, where large unemployment occurs, is pro poor if it provides more employment (labour intensive). Three indicators related to this issue are the incremental capital output ratio (ICOR), incremental labour output ratio (ILOR), farmer exchange value (due to the fact that rural poor are the majority), and . ICOR and ILOR, during 1998-2002, showed an increase while the farmer exchange value remained constant. These three indicators indicate that the economic activity in East Java was labour intensive. It created more opportunity to the waged-specialized households but did not have any significant impact on the agriculture-specialized households. Another indicator is the *UMR* (regional minimum wage), which is currently four times of the poverty line. This indicator, however, does not fully workable since most labours, who worked in informal sectors, are paid less than the *UMR*.

Overdependence to foreign loans is one the causes of poverty in Indonesia and it is important that regions, since the decentralization period, do not repeat similar failure. However, significant indicators such as DSR and debt to export ratio are not found at the regional and local level during this transition period. Because current debts were made at the national level, yet all regions to significant extent also pay the national debts through the balance transfer mechanism.

The second theme, lack of good governance, which has always been part of the political landscape of Indonesia, shows that poverty reduction within the broader context of sustainable development requires strong and democratic institutions with pro-poor commitment (Save-Soderbergh 2000; Smith 2003), beyond the internationally acknowledged free and fair election process since the fall of Suharto (Islam 2003; Diamond 2004). The empirical evidence in Indonesia shows that indicators of governance, such as democracy, rule of law / government effectiveness, and corruption, are correlated with the development outcomes. However, it is hard to objectively monitor the quantitative measures of governance at the regional and local level since the framework for monitoring system has not been formulated yet. A quantitative indicator available at the regional and local level, i.e. public consultation between the executive and legislative, yet the quality of public hearing and consultation beyond the numbers is not known.

Two significant public services that are responsive to the state of poverty are education and health services. The outcomes in East Java shows that the access to education and health was not equally distributed. Provincial data on the performance of education and health revealed that many regions in East Java have achieved good performance, such as high enrolment rate for primary education (95 percent and higher), low infant mortality (lower than 15). However, among 37 districts (29 regencies and 8 municipalities), 5 districts had low performance in both education and health, i.e. 30 percent of 7-12 year old children could not participate in primary education, 35 percent and 65 percent of 13-15 year old and 16-18 year old children respectively could not enter junior and senior high schools, high infant mortality rate (30 to 46), and low life expectancy (57.5 years) (*SUSENAS*/Social Economic Survey 2002). These figures indicated spatial inequality in the province, from which the development was not well targeted to those districts.

The quality of human resources, in general, is shown by the human development index (HDI). HDI score in 2002 was improved from its score in 1999, yet several obstacles were still found. Gaps between males and females and spatial inequality in terms of wealth distribution and geographic isolation were found. According to *BPS* data in 1996-2002, among 29 regencies, there were 13 regencies that constantly had higher percentages of poor people than the average. 36.79 percent of the population in those 13 regencies were poor, while at the provincial level was 19.18 percent.

<u>Grassroots approach</u>

Lack of consultation between the government and the poor caused government programs to have very little impact on the poor and as the poor had no voice, they could not influence government programs. Therefore, in order to construct better plans and targets for poverty reduction, it is important to understand the dimensions of poverty as highlighted by the poor. The majority of Indonesian poor saw that poverty was primarily caused by the lack of means to generate income(Mukherjee 1999)[7]. The poor also perceived their lack of capability in other non-income dimensions. The category of well being, as perceived by Indonesian poor can be classified into 6 criteria, i.e. livelihoods, housing, health, human resource development, family life and community life (Mukherjee 1999).

The observation of poverty measures at Kutobedah, a long-lasting 'poverty-pocket' in the City of Malang – East Java, revealed that in such 'pocket' the poor had lack of capability for their livelihoods. Kutobedah exemplified a 'poverty-pocket' that had been the target of poverty reduction related programs, ranging from the introduction of walk-up flats by national public housing agency, *kampung* improvement program (KIP) to recently resettlement and urban renewal program. Those programs aimed at providing legal shelters for locals who were living on squatter land and improving their settlement through community based development or, vice versa, promoting community development through infrastructure based development. However, those attempts were not successfully benefited the targeted community. Incidence of capability poverty was still high. Almost 30 percent of the population[8] were unemployed, twice of the unemployment rate at the district level. The (self) employed population had unstable job and all were in informal sectors while at the city level this accounted for only one third of the work force. Scavengers and beggars were considered as jobs and were about 34 percent of the 'working' population. The average income of the population was Rp 79,237.00 per month which was lower than the poverty line in Malang and was about a quarter of the average income at the city level. 80 percent of the population were poor with poverty gap accounted for about 30 percent.

Shelter, which is related to environmental health and access to land, is the second criterion. A chronicle problem faced by the poor was that they lack of access to land/housing. All respondents lived on squatter land, i.e. a dense slum area, about 4.93 m2 per capita. The condition of sanitation, floor, drainage and safety were bad, i.e. 81.19 had no private toilet facility, 93.07 percent were on dirt floor, flood often occurred during rainy season and the houses were on unstable land (subject to erosion). Water was not free. They had to purchase clean water for about one fourth of their income per month.

The third criterion perceived by the poor is health. Morbidity rate in Kutobedah was 28.14 percent with type of illness associated with the impact of urban air, water and sanitation problems. Access to health facilities was low. This is indicated by, e.g. only 47.37 percent of birth deliveries were attended by medical personnel, 54.46 percent of the households were self medicating, 94 percent of the households claimed that the cost for public hospital as too expensive.

The fourth criterion, i.e. human development, was lower than that at the district level. 16.39 percent and 33.33 percent of 7-12 years old and 13-15 years old children respectively could not participate in primary and junior high schools. Low school participation in the area was caused by both lack of household's income capability and inability of the state to provide free 9 years basic education. 89 percent of the households, who could not send their

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[7] As part of the UNDP's program entitled Consultation with the Poor, the research was conducted at 12 districts in Java and Nusa Tenggara Islands during May-June 1999.

[8] 101 respondents who lived on the fragile land along Brantas and Bango River and were interviewed for the purpose of this study

children to school, claimed that the cost for education was not affordable. The drop-out rate 7-15 age group was 13.80 percent.

The family life of the poor in Kutobedah represented the most vulnerable households to shocks, i.e. the female headed households (20 percent of the total households), where 30 percent of them were in debt. In average, the females married at young age (20 years old), had 3 or more children, and 78 percent did not participate in the family planning program. Female's average income was less than half of male's income, yet their participation was significant in improving family's income. In terms of the decision making process in the community, 84 percent of poor households felt that they were not involved in the local development. 53 percent of the household heads stated that the roles of the head of *RT* (head of a neighbourhood unit) was enough in representing their voices, while about 18 percent of women, who were mostly the member of *PKK* (women organization in the community), were actively involved in the local development, such as the distribution of rice for poor, scholarship and other social aid programs.

The examination of the state of indicators related to poverty reduction at the regional level and local level in East Java reveals that there are gaps between the state and the desired future outcomes. The best way to describe those gaps is to relate the current outcomes (the state) to the regional targets and the Millennium Development Goals (MDGs). Findings of the gaps are significant in reformulating new poverty reduction strategies that will be set at the district level (table 1).

Table 1: Poverty reduction related indicators in the City of Malang, East Java, in response to the MDGs

Some of the Millennium Declaration associated with poverty reduction		**State Indicators in East Java's SUSENAS, RENSTRA and NHDR**	**Outcomes in the City of Malang**		
Goals	**Targets between 1990 and 2015**		**1996**	**1999**	**2002**
Goal 1	Halve the proportion of people who suffer from hunger or whose income/ consumption is less than one dollar a day	Poverty rate (based on consumption expenditure) (%)	3.33	12.83	14.27
Goal 2	Ensure that children everywhere will be able to complete a full course of primary education	School enrolment rate (%): Age 7-12 Age 13-15	 95.6 90.8	 97.5 85.1	 98 94.9
Goal 3	Eliminate gender disparity in primary and secondary education, preferably by 2005, and to all levels of education by 2015	Adult literacy rate (%) - female - male Mean years of schooling (years) - female - male		 91.6 97.4 8 9.2	 92.4 97.5 9.3 10.8
Goal 4	Reduce by two-thirds the under-five mortality rate	Infant mortality rate per 1000	18*	45	43.9
Goal 5	Reduce by three-quarters the maternal mortality ratio	Birth deliveries attended by skilled health personnel (%)	93.7	88.4	95.5
Goal 6	Have halted and begin to reverse the insidence of HIV, malaria and other	Life expectancy (years) Morbidity rate (%)	65.8	68.7	69.7

	major diseases				
Goal 7	Integrate the principles of sustainable development into country policies and programs and reverse the loss of environmental resources **)	Proportion of land area covered by forest (%) CO2 emission (metric tons per capita) Energy use per capita (kg of oil equivalent) Freshwater resources per capita (cubic meters)		1.00 652.8	 728.8 13,404.8
	Halve, by 2015, the proportion of people without sustainable access to safe drinking water	Proportion of households with access to safe drinking water (%)	51.2	57.9	61.8
	Have achieved, by 2020, a significant improvement in the lives of at least 100 million slum dwellers	Proportion of households without access to sanitation (%) Household with dirt floor (%)	13.9 7.3	5.7 3.6	5.5 2.3
Goal 8	Develop further an open, rule based, predictable, non-discriminatory trading and financial system. Includes a commitment to good governance, development, and poverty reduction	Proportion of local domestic revenue to the total of local budget (%)		18.55	10.48

*)=Malang *dalam Angka* (Malang in Numbers) 1996
**)= data only available at the national level
SUSENAS= National Social Economic Survey
RENSTRA= Strategic Plan
NHDR= National Human Development Report

Source: MDGs, *Susenas* and NHDR 2001 and 2004, Malang *dalam Angka* 1996-2002, World Development Indicators database April 2004

In terms of providing goals and targets, since the implementation of the regional autonomy law, the provincial government had established goals and targets for the development performance (table appendix A1). However, it is difficult to estimate the effectiveness of those targets since the responsibility for poverty reduction has been transferred to local governments, while most local governments had not prepared relevant goals and targets in response to the MDGs and the provincial strategic plan 2001-2005. Therefore, it is important for local governments to reformulate their strategic visions to include goals proposed by the Millennium Declaration into their minimum targets of the development outcomes as part of the efforts to provide the basic rights to all Indonesians. Current *SPMs*[9] (Minimum Service Standards) available at the local governments provide technical thresholds rather than providing realistic and fiscally sustainable goals and targets.

The examination on the state indicators reveals that the best way of prescribing new development indicators at the regional and district level is to relate them to the MDGs as the minimum standards of achievement. Related to the MDGs, there are inconsistencies of data in the existing framework, particularly related to goal 6,7 and 8. The existing strategic planning has included aggregated health indicators related to Human Development Index

[9] *SPM*= *Standar Pelayanan* Minimum (minimum service standards)

(HDI) and Human Poverty Indicators (HPI), such as life expectancy. However, it does not provide more aggregated indicators on the efforts to fight against major diseases (goal 6). Environmental indicators are not adequately addressed at the sub-national level (goal 7). The existing framework and data at the sub-national provide water qualities but lack of air and soil qualities. Trading, financial system and commitment to good governance have become significant issues (goal 8), yet formalism in indicators program has not been established.

The response: new framework and strategic visions for poverty reduction at the district level

Previous sections find that income/consumption based indicators are very sensitive to monetary shock and inflation. Income based estimation of poverty, therefore, is often disputable. Asra (2000) and Dhanani and Islam (2002), for example, argued that the official data of poverty in Indonesia (published by the Central Bureau of Statistics) was lower than the estimation based on capability poverty because larger number of Indonesians were unable to fulfil their basic needs. Hertel, Ivanic et.al. (2004) also claimed that poverty does not always fall when per-capita real income rises. Capability poverty, on the other hand, gradually responds to long-term structural changes within the country. Failure in recognizing important aspects of capability poverty in Indonesia masked inability of the state to provide basic services to all people to meet their basic rights. Therefore, in order to reformulate a poverty reduction strategy at the local level, the new indicator framework will focus on the capability poverty/basic right approach to cover more comprehensive dimensions of human poverty.

The new framework highlights several gaps found in the existing indicators framework. The overriding concern of the causes of poverty indicates that poverty in Indonesia was not caused by the shortage of resources, rather by lack of good governance and policy failure. The centralized political system during Suharto's regime was unable to provide incentives for local governments to mobilize local resource. The outcomes of such condition can be identified from, for example, the long-lasting inequality and a high profile problem of corruption. The former (inequality) shows the tension between the attempts to achieve high growth rate versus equal distribution. Preventing corruption in the regional autonomy period is becoming more important since its impacts could be more economically damaging in a decentralized political system (Hamilton-Hart 2001). Local developers and consultants in Malang have complained the increase of the level of corruption at the local level. Another important issue was the absence of links between development targets and funding mechanism. This failure led to the overdependence of funding to foreign loans and aids.

In response to those issues, the proposed new framework is based on the evolved development concept from the former paradigm that focused on economic growth through capital investment and savings to a paradigm favouring human basic rights, institutional and technical reform, and good governance. All significant indicators identified from the causal factors of poverty and their respective state indicators need responsive policies/strategic vision, programs and projects. The first set of response indicators are related to economic structures. It is undisputable that economic growth is necessary for the income of the poor to rise. The key challenge is to formulate policies which minimize the tension between the growth against distribution. Pro poor growth can be achieved through two basic policies, i.e. firstly, policies that create broad-base growth, covering the whole country and economy, and secondly, policies that increase the growth in both the regions in which the poor live and the sectors from which the poor earn for living (OECD 2004). An appropriate aggregated indicator for the broad-based growth is the average income of the poor. This indicator can be disaggregated into several indicators, such as incomes of the marginally poor and the rate at which poverty gap is falling. The former is important to measure the reduction in poverty headcount, while the later measures the time needed to eradicate poverty. The second policies (geographical and sectoral growth) can be monitored from particular indicators, such as agricultural productivity and contribution of small and medium enterprises (SMEs) to gross regional domestic product (GRDP).

The second themes, governance and public services, are closely related to the institutional reforms. The decentralization was significant step-stone. Further policies, in response to the causes and state of poverty in Indonesia, are linked to:

- eradication of corruption and improvement of the rule of law;
- improvement in productivity and provision of incentives to local stakeholders; and
- provision of incentive for entrepreneurship and investment;

Indicators that show those policies, among others, are the rate of the loss of state's budget, ratio of local revenues to local budget or GRDP, ratio of education and/or health expenditure to total expenditure, resource productivity index and ratio of credit for SMEs to all credit for businesses.

The last theme deals with policies and strategies to reduce risk and vulnerability and improve asset capability. Indicators related to regional/local policies for education, health, shelter (settlement), environmental-health and natural resources belong to this theme. To be noted here that outcomes indicators of the pressure are not necessarily distinctive to state and response indicators, and vice versa. The loss of state's budget, for an example, indicates the cause of poverty (corruption), while the falling rate of the loss of state's budget indicates the outcome of the responses (to eradicate corruption).

Another significant issue regarding the indicator framework is the absence of efficient and robust data at the local level. During past three decades, indicators used to nominate mayors and regents were political rather than improvement of social-economic standards. However, based on the Regional Governance Law no 32, 2004 (the revised version of the Regional Autonomy Law 29, 1999), from 2005 mayors and regents will be elected directly by the residents. Transparency of data regarding development performance will become more important in the future. Independence of the central bureau of statistics from political intervention together with the support from NGOs and CBOs will play significant roles in the development process. These institutional changes of value and concepts will be part of the enabling environment resulted from good governance. As stated by FitzGerald (2001), good governance is an idea about change that touches concepts and values, no matter how lightly it steps.

To be operational, the proposed framework should be integrated to the existing planning framework. Placement, type of indicators and the interaction among indicators will be adjusted to the type of planning in the existing type of plans (table 2). Indicators related

Table 2: Placement of the P-S-R indicators in the planning structure at the regional-local level

Type of plans:	Strategic plans	Programs plans	Project plans
Indicators:	***RENSTRA***	*PROPEDA*	*REPETADA*
Object:	Decisions	Decisions	Material
Interaction:	Continuous	Continuous	Until adoption
Future:	Open	Open	Closed
Time element:	Central to problem	Central to problem	Limited to phasing
Type of indicators:	• **Pressures/Causes** • **States/impacts** • **Responses/actions**	• **Responses** (mostly) • **States**	**Responses**

RENSTRA= Strategic Plan (long-term)
PROPEDA= Regional/local development program (mid-term)
REPETADA=Regional/local annual development plan

Conclusion

Within the Pressure-State-Response indicators framework, poverty reduction is a process rather than a measurable object. The function of an indicator program in the local planning framework is an integrated temporal-spatial matrix of a development policy statement specifying goals and targets. Millennium Development Goals and targets in the regional development plan can be reformulated and be used as minimum standards of achievement at the local level.

It is important that the strategies, programs and projects for poverty reduction aim at resolving and preventing the structural causes, which are heavily socio-political, rather than the symptoms of poverty, which are mainly economical. Efforts to fight against poverty in Indonesia, since 2001, conceptually have been decentralized to mainly become the responsibility of the local governments. However, current efforts to reduce poverty at the local level cannot be fully separated from problems at the national level since most of the causes of current poverty derived from multidimensional problems at the national level since more than three decades ago, such as macroeconomic environment, vulnerability of the banking and corporate institutions and weak legal and judicial systems. Poverty reduction (at the local level) is also confronted with current and evolving challenges, which will remain as acute as ever, i.e. the fiscal dependency of most regional and local governments on national government and corruption. The efforts should also be focused on the empowerment of institutions at the sub-national level. Therefore, a broader context of good governance, which includes capacity, public services, accountability, rule of law and participation, is required for sustaining reduction of poverty. Those challenges overrode problems associated with shortage of resources (natural and human resources) within the country.

The second important notion of poverty reduction in Indonesia is the need to focus on capability poverty since improvement of income (material assets) is not per se sufficient to meet basic needs of all Indonesians and belittles the challenges that remained in the dimensions of human poverty, such as shelter and living environment, health and human resource development, family life and community life. Improvement in those dimensions possesses externalities that will eventually increase income. The poverty analysis of the poor community in Kutobedah revealed the actual dimensions of poverty encountered by the poor households, such as lack of income and assets, vulnerability of health and environmental safety, and sense of voicelessness and powerlessness.

It is concluded here that to fight against poverty, a comprehensive but workable indicator framework for monitoring poverty reduction progress needs to be formalized in the existing local-regional planning system. The formalism in poverty reduction indicator program will not only lead the respective data to become more efficient and robust, but may also direct socio-political attention to the 'first order' of current development challenges, i.e. eradicating poverty and improving human welfare.

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Appendix

Table A1: The compilation of the development performance indicators in East Java Province

Development performance	Performance indicators	Performance standards/targets				
		2001	2002	2003	2004	2005
Vision:	*Aggregative indices:*					
A developed, peaceful and prosperous society Democratic and equal development	Purchasing Power Index (PPI) (Year 2000=100)	102	102	103	103	103
	Average educational level of schooling (year)	5.9	5.9	6.0	6.0	6.1
	Human Development Index (HDI)	58.5	59.2	59.5	60.0	60.3
	GDP per-capita (Rp million)	4.86	5.49	6.20	7.01	7.92
Development Paradigm						
Themes:						
Equality/equity	Regional disparity index (Williamson index)	150	150	145	140	140
Community empowerment	The contribution of *UKM* (small and medium enterprises /SME) in the Gross Regional Domestic Product (GRDP)/*PDRB (%)*;	5	6	5	5	4
	Ratio of credit for *UKM* to all credit for businesses (%)	36.0	36.2	36.7	37.1	37.3
	Poverty rate (%)	25.00	25.00	25.00	24.00	24.00
Economic growth and sustainable development	Economic growth/GDP per capita growth (%)	3.30	3.50	4.00	4.80	5.30
	Improvement of investment efficiency (ICOR)	3.34	4.00	3.80	3.50	3.25
	Ratio of Local revenue & expenditure budget *(APBD)* to *PDRB/GRDP* (%)	1.20	1.10	1.05	1.01	0.99
	Surface water quality = a. COD	36.00	31.00	26.00	22.00	18.00
	b. BOD	15.00	14.00	12.00	10.00	9.00
Strategic Objectives						
Themes:						
Education	Illiteracy rate (%)	16.09	15.80	15.60	15.30	15.10
	Participation/enrolment rate of primary education and secondary education (%): Primary school	96.50	96.80	97.00	97.20	97.50
	Junior high school	81.00	81.20	81.40	81.70	81.90
	Senior high school	53.00	53.90	54.10	54.30	54.70
	Student's ratio of *SMK* (specific skill high school) to *SMA* (general high school) (%)	0.46	0.46	0.47	0.47	0.48
Productivity	*NTP* (Farmer Exchange Value)	97.80	98	98.5	99	100
Health	Birth attended by trained health personnel (%)	59.5	60	60.3	60.7	60.1
	Infant mortality rate (per 1,000 deliveries)	44	44	42	40	39
	Life expectancy (year)	66	66.2	66.4	66.7	67
Democracy and regional autonomy	Frequency of public consultation between the executives and legislatives (in a fiscal year)	8	12	14	17	18
Natural resources development	Percentage of improvement of primary sector's contribution in the formation of GDP (%) (t-1)	100	100.1	100.3	101.0	101.3
	The improvement of government's real domestic revenues (*PAD*) (Rp billion t / t-1)		1.100	1.100	1.200	1.300
Corruption	Ratio of state's loss to state's budget, (% of reduction)		2	2	2	2
Safety and security	Reduction of the number of crimes (% of reduction)		2	2	2	2
	Reduction of crime rate/crime index (% of reduction)		2	2	2	2
Employment	Open unemployment rate		4.4	4.2	4.1	4
	Incremental Labour Output Ratio (ILOR)					

Note on terms:
UKM: Usaha Kecil Menengah/Small Medium Enterprises (SMEs)
PDRB: Produk Domestik Regional Bruto/Gross Regional Domestic Product (GRDP)
APBD: Anggaran Pendapatan dan Belanja Daerah/Local Revenue and Expenditure Budget
COD: Chemical Oxygen Demand; BOD: Biochemical Oxygen Demand
SMK: Sekolah Menengah Kejuruan/Specific Skill High School
NTP: Nilai Tukar Petani/Farmer Exchange Value
Source: East Java Strategic Plans 2001-2005