

Document of  
The International Fund for Agricultural Development

**REPUBLIC OF INDONESIA**

**SMALLHOLDER LIVELIHOOD DEVELOPMENT PROJECT IN EASTERN INDONESIA**

**PROJECT DESIGN REPORT**

**Main Report**

Asia and the Pacific Division  
Programme Management Department

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May 2012



**REPUBLIC OF INDONESIA**  
**SMALLHOLDER LIVELIHOOD DEVELOPMENT PROJECT IN EASTERN INDONESIA**  
**PROJECT DESIGN REPORT**

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**REPUBLIC OF INDONESIA**  
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**PROJECT DESIGN REPORT**

**CURRENCY EQUIVALENTS**

Currency Unit	=	Indonesian Rupiah (IDR)
USD 1.00	=	IDR 9 100
IDR 1 000	=	USD 0.1098

(October 2010)

**FISCAL YEAR**

1<sup>st</sup> January – 31<sup>st</sup> December

**WEIGHTS AND MEASURES**

Metric System

**ABBREVIATIONS AND ACRONYMS**

<i>APBDI</i>	<i>Anggaran Pendapatan dan Belanja Daerah</i> (Provincial Annual Budget)
<i>AFBDI</i>	<i>Anggaran Pendapatan dan Belanja Daerah</i> (District Annual Budget)
<i>APBN</i>	<i>Anggaran Pendapatan dan Belanja Negara</i> (National/State Annual Budget)
AFS	Agency for Food Security (MOA)
AFSE	Agency for Food Security and Extension
AHW	Animal health Worker
AIATS	Assessment Institute for Agricultural Technology
AsDB	Asian Development Bank
BIC	Bureau of International Cooperation (MOA)
AWPB	Annual Work Plan and Budget
<i>Bappeda</i>	<i>Badan Perencanaan Pembangunan Daerah</i> - Regional Development Planning Agency
<i>Bappenas</i>	<i>Badan Perencanaan Pembangunan Nasional</i> - National Development Planning Agency
<i>BPKP</i>	State Finance and Development Supervisory Board
<i>BPD</i>	Elected village representative body
<i>BPP</i>	Sub-district Extension Office
<i>Bupati</i>	District Mayor
CBS	Central Bureau of Statistics
COSOP	Country Strategic and Opportunities Programme
CVO	Commercial Village Officer
<i>DEMAPAN</i>	Village Self Help Food Reliance Programme
DTEC	District technical and Extension Committee
<i>Dinas</i>	Department
<i>DIPA</i>	Annual Budget Document
DPIO	District Project Implementation Office
DTEC	District Technology and Extension Committee
EIRR	Economic Internal Rate of Return
FF	Farmer Facilitator
FSEA	Food Security and Extension Agency
<i>Gapoktan</i>	Federation of Farmers' Groups at Village Level
<i>GERNAS- Kakao</i>	Cacao Development Programme
GDI	Gender Related Development Index

GDP	Gross Domestic Product
GNI	Gross National Income
GRDP	Gross Regional Domestic Product
GRF	Group Revolving Fund
HDI	Human Development Index
HPI	Human Poverty Index
IAARD	Indonesian Agency for Agricultural Research and Development
ICATAD	Indonesian Centre for Agricultural Technology Assessment and Development
IDR	Indonesian Rupiah
IRR	Internal Rate of Return
KADIN	<i>Kamar Dagang dan Industri</i> – Indonesian Chamber of Commerce and Industry
KPPN	Ministry of Finance Treasury Office
LPM	Committee for developing community programmes (village level)
MCDC	Mars Cocoa Development Centre
M&E	Monitoring and Evaluation
MDG	Millennium Development Goals
MIS	Management Information System
MOA	Ministry of Agriculture
MOF	Ministry of Finance
MOHA	Ministry of Home Affairs
MTDP	Medium-Term Development Plan (2010-2014)
MTR	Mid-Term Review
NGO	Non-Government Organisation
NSC	National Steering Committee
O&M	Operation and Maintenance
NPMO	National Project Management Office
PCR	Project Completion Review
PDR	Project Design Report
PIDRA	Post-Crisis Programme for Participatory Integrated Development in Rainfed Areas
PM&E	Participatory Monitoring and Evaluation
<i>PNPM-Mandiri</i>	National Programme for Community Empowerment
<i>PMD</i>	Directorate General of Village and Community Empowerment (MOHA)
<i>PPL</i>	<i>Penyuluh Pertanian Lapangan</i> - Government employed extension workers
PPCO	Provincial Project Coordination Office
PTEC	Provincial Technology and Extension Committee
<i>PUAP</i>	Village Agribusiness Development Programme
R&D	Research and Development
READ	Rural Empowerment and Agricultural Development Programme
RIMS	Results Impact Management System
DA	Designated Account
SDR	Special Drawing Rights
SHG	Self-help Group
SOLID	Smallholder Livelihood Development Project in Eastern Indonesia
SPADA	Support for Poor and Disadvantaged Areas
SVA	Sustainable Village Approach
TA	Technical Assistance
<i>THL</i>	Contracted government extension staff
TNA	Training Needs Assessment
TOR	Terms of Reference
UNDP	United Nations Development Fund
USD	United States Dollar
VC	Value Chain
WA	Withdrawal Application
WFP	World Food Programme
WSSLIC	Water Supply and Sanitation for Low Income Communities

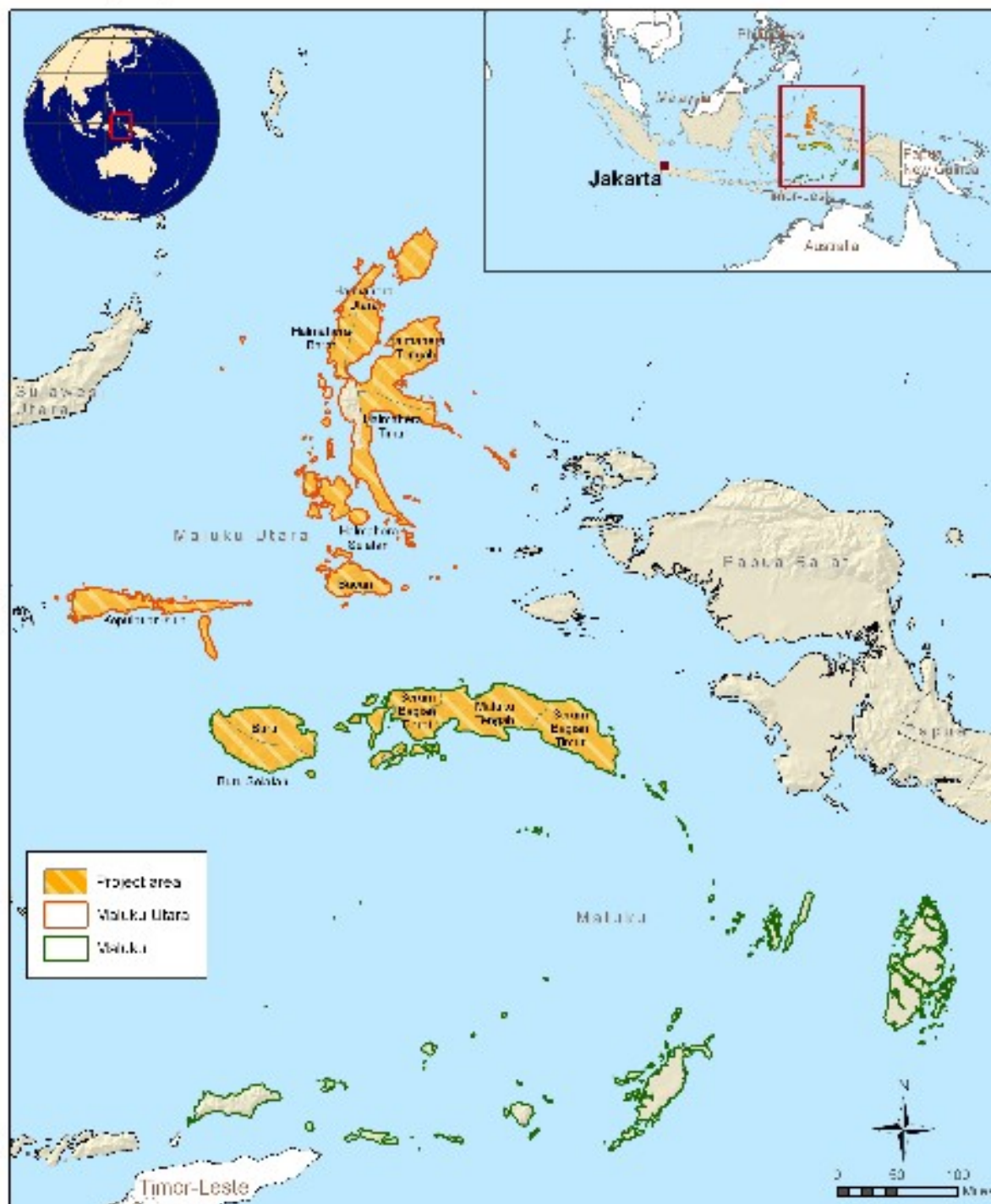


## Map of the Project Area

### Indonesia

#### Smallholder Livelihood Development Project in Maluku and North Maluku (SOLID)

Design report



This design has been prepared and the presentation of the material in it is made solely for the expression of any opinion whatsoever on the part of IFAD concerning the delimitation of the frontiers or boundaries, or the authorities thereof.

Map compiled by IFAD

2017/2019



## EXECUTIVE SUMMARY

### A. Summary and Objectives

1. The project will focus on: (i) improving the skills and empowering local communities, farmers' groups and their organisations; (ii) diversifying the sources of household food supply and adding value to food crops through local processing and marketing; (iii) improving post harvest handling, including local processing of crop and fishery/marine products; (iv) facilitating links between producers and markets; (v) providing small-scale rural infrastructure to improve agricultural productivity with community participation; and (vi) strengthening the coordination and management of project implementation at the national and regional levels. The project is expected to directly benefit a total of around 49,500 farm households belonging to the Self Help Groups (SHGs) and Federations. The project design and implementation arrangements takes into account the lessons learned from the recently completed Post-Crisis Programme for Participatory Integrated Development in Rainfed Areas, IFAD Loan No. 539-ID and other IFAD and donor supported projects in Indonesia.
2. The **objective of the project** is to improved the livelihoods (incomes and food security) and reduce and the incidence of poverty for people in the targeted villages in the two provinces.

### B. Components

3. **Component 1: Community Empowerment.** The output of this component is that communities are mobilised and SHGs and Federations established. The project will adopt a Sustainable Village Development Approach which will include: establishing and capacity building of the smallholders' institutions (SHGs and Federations), mainstreaming the use of local social capital, improving smallholder competitiveness and farming systems, value chain management, and environmentally sound resource management.
4. **Component 2: Productivity Improvement and Integrated Farming Systems.** The output of this component is that the extension services are improved to facilitate increased agricultural productivity by smallholders. Following a menu of options, the focus will be on productivity and quality improvement in the production of agriculture and livestock products in which the provinces enjoy a natural comparative advantage, e.g. increasing cocoa, nutmeg and coconut production, improving the productivity of annual food crops (rice, cassava etc.) within the farming systems, improving production of vegetables for villages with access to urban markets and develop small semi-intensive units for livestock.
5. **Component 3: Value Chain Development and Marketing.** The output of this component is the availability of services to improve market returns by the SHGs and Federations. The project will support the development of Federations and their integration in the value chains through the provision of financial (equity and/or working capital as a grant), technical and management support, based on sound business plans. Links will be developed between the Federations and key value chain participants to provide incentives for farmers to adopt the interventions and produce higher (export) quality products, to grade produce and ensure good primary processing (drying and storage). An additional potential opportunity for cacao is exploring the possibility of linking with the fermented bean market and encouraging farmers to enter this higher value market chain.
6. **Component 4: Productive Rural Infrastructure.** The output of this component is that small-scale rural infrastructure improved. The project will finance investments in small-scale productive rural infrastructure through the provision of community grants, in response to proposals submitted by the villages and to complement the project's support for agricultural productivity improvement. Examples of possible investments include: upgrading access from village to the farmers' fields, micro-irrigation schemes, small crop drying and storage facilities and rehabilitation of previously cropped areas.
7. **Component 5: Institutional Strengthening and Project Management.** The output of this component is efficient project management and coordination. This component will finance the costs of project management at national, provincial and district levels and support the development of the staff

capacity of key participating agencies to provide the services required by the rural community in the target villages.

8. **Gender Strategy:** The project will: (i) enhance the value of production and processing activities dominated by women through skills training and introduction of new technology; (ii) use a group approach (women only or mixed groups) for improving quality standards and marketing; (iii) promote women entrepreneurs to provide business development services and to venture into value chain activities often dominated by men, e.g. primary marketing; (iv) build women's leadership skills to participate in the governance of groups and their unions; (v) sensitise men to support women's enhanced role in the value chain development; (vi) build the capacity of groups and their unions and those of the local government institutions to ensure gender responsive service delivery; (vii) sensitise and train planners and sector staff and key project staff at district and sub-district levels to institutionalise gender mainstreaming into district and local level development planning and management practices; (viii) conduct gender analysis of district level planning, monitoring and evaluation frameworks and developing guidelines and checklists in community development and poverty reduction, agriculture and infrastructure.

### **C. Background and Rationale**

9. The rationale for IFAD to help the government to finance SOLID include: First, the project will target rural sub-districts in the provinces of Maluku and North Maluku with higher than average levels of poverty and/or large numbers of poor people. By focussing on improving the livelihoods of the poorer sections of these rural communities, the competitiveness of smallholder agriculture and growth of the agricultural sector, the project can contribute to the achievement of the Government's poverty reduction objectives in line with the government's Medium Term Development Plan and the IFAD COSOP 2009-2013, while simultaneously improving the low returns from agricultural production and leading to higher farm incomes and improved household food security, which are sustainable. Secondly, the project will need to address key marketing, production, natural resource management and infrastructure constraints that have prevented the growth in the productivity of food and estate crops in the target areas over the last decade, with a focus on: (i) improving the access to productive assets, appropriate technology and production support services for on-farm productivity improvement; (ii) value chain development, including building market links with the private sector, post harvest management, agro-processing and supporting small rural enterprises; (iii) providing access to, and improved management of, natural resources; (iv) improving productive small-scale rural infrastructure at the village level e.g. to improve access to the crop production areas, micro-scale irrigation and rehabilitation of previously cultivated areas; and (v) establishing group revolving funds to help build up the members' financial assets for investment or emergency purposes and subsequently help link these groups to micro-finance institutions (MFIs) and formal banking sector institutions. Thirdly, adopting a community empowerment and participatory development approach, that provides assistance to village and community organisations can help ensure the sustainability of the improvements in the livelihoods of the smallholders in the targeted villages initiated with project assistance and enable the rural poor and other marginalised groups, to make their own decisions in managing their resources, establishing their development priorities and negotiating services from various sources.

### **D. Rural Context, Geographic Area of Intervention and Target Groups**

10. Conflicts in Maluku and North Maluku during the period 1999-2003 have had a major effect on the economic prosperity and livelihoods of people in these areas and the combined economy of Maluku and North Maluku contracted by approximately 30% in real terms. 28% of the population in Maluku was living below the poverty line in 2009 and 10% in North Maluku with high level of unemployment and cereal deficit, due to a lack of access to various forms of human, physical, financial, natural, and social capital.

11. The project will target a total of 11 districts, five in Maluku and six in north Maluku. The target group of the project will include a total of around 49,500 farm households as direct beneficiaries belonging to the SHGs and Federations and additional poor or very poor households will benefit from the projects investments in productive rural infrastructure and natural resource management.

12. The targeting strategy is that the project will use a participatory approach in the selection of an estimated 49,500 households in the target villages using a gender-sensitive poverty and livelihood analysis e.g. participatory wealth ranking, identification of common interests etc. The criteria for selecting the sub-districts and villages for participation in the project include: (i) exclusion of all urban villages and urban sub-districts; (ii) incidence of poverty >20%; (iii) potential for agricultural productivity and livelihoods improvement and rural poverty reduction; (iv) commitment from the local government to participate in the project; (v) availability of providers of rural services (public, private and/or NGOs) with the capacity to deliver the services to the target groups; (vi) accessibility with a maximum journey time from the district or sub-district HQ of around four hours; and (vii) availability of a district agricultural office and/or office of food security at the sub-district level. Within the sub-districts, the project will target about 330 villages with: (i) a large number of poor households, where there is a potential for increased agricultural productivity, improved food security, higher household incomes and improved natural resource management; (ii) a large number of households from the poor and poorest socio-economic groups, including female headed households; (iii) where people express a need for assistance and guidance; and (iv) people are willing to work together in a participatory way. The project will target poor indigenous and immigrant communities (including where appropriate transmigrant communities).

### **E. Benefits**

13. The main direct benefits will come from: (i) improved prices for commodities that are exported from the islands due to the improvements in quality and some value addition (post harvest management and primary processing); (ii) higher crop yields following the use of improved low cost cropping, enrichment planting and pest management techniques; (iii) rehabilitation of productive rural infrastructure, mainly farm access roads, micro-irrigation systems and previously cropped agricultural areas; and (iv) improved management of natural resources. In addition, the project will enhance community empowerment and help create better links between central government, sub-national administrations and rural communities

### **F. Implementation Arrangements**

14. The project will be a “central government project”, with the Agency for Food Security (AFS) of the Ministry of Agriculture (MOA) as the Lead Project Agency, delegating the responsibilities to the local governments for project implementation. The National Project Management Office (NPMO) in AFS, headed by a National Project Coordinator, will manage the coordination and implementation of the project. For policy guidance, advice and overall coordination, the SOLID Project will use the existing National Steering Committee (NSC) established for all IFAD-supported projects under the responsibility of MOA which was established by decree of the Minister of MOA in February 2008. In each province, a Provincial Project Coordinating Office (PPCO), headed by a Provincial Project Coordinator, will be established in the Provincial Lead Coordinating Agency. In each district, a District Project Implementation Office (DPIO), headed by a District Project Manager (DPM), will be established in the District Lead Implementing Agency, responsible for overall project management at the district and sub-district levels. The project will work with other government agencies, NGOs, donor-supported projects, universities, private sector and/or other development partners to strengthen the capacity of provincial, district and sub-district institutions and their staff for effective service delivery.

### **G. Costs and financing**

15. Total project costs including contingencies, duties and taxes are estimated at USD 65.00 million. The proposed project financing is: (i) an IFAD loan of about USD 49.1 million (76%); (ii) an IFAD grant of USD 1.08 million (2%); and (iii) Government contribution equivalent to USD 14.81million (23%). The project period will be seven and half years (July 2011-end of 2018).

### **H. Risks**

16. Under-performing institutions at all levels will have a negative impact on project outcomes, which will be addressed by providing resources to finance additional staff to assist the SHGs and the

federations to strengthen the capacity of the line agencies' provincial and district administrations to perform their respective support functions effectively. The quality of construction of small-scale rural infrastructure implemented at village level is frequently poor and subsequently poorly maintained, which will be addressed by focusing on simple infrastructure directly related to improving agricultural productivity within the capacity of the groups and federations to implement and maintain rather than the more general types of rural infrastructure. Close supervision and monitoring using strong project implementation teams, establishing and training the groups and federations on the maintenance of infrastructure investments are all ways of ensuring the sustainability of the infrastructure. The assumed rate of technology uptake and adoption of processing and marketing initiatives that add value to the production of food and estate crops may not materialise, and so prevent the achievement of the project's objectives. This will be addressed by providing support from experienced NGO(s) to ensure that the SHGs and federations can become sustainable organisations for both social and economic development. The risk that the procurement of the inputs and other materials required by the farmer organisations and self-help groups financed with project assistance will be delayed will be countered by the use of Community Participation in Procurement procedures with the SHGs and federations purchasing their own requirements. To overcome the risk of the SHGs and federations being hindered by a lack of access to credit and financial services provided by the formal banking sector and MFIs, the project will assist the SHGs and federations establish and build up groups revolving funds (GRFs) so that the members have access to funds for input purchases. In addition, the project will establish partnerships between the federations and MFIs and the formal banking sector to enable the SHGs and federations obtain funds for investment over and above the level that their GRFs can provide.

## **I. Environment**

17. The project is classified as Category "B".

## **J. Knowledge Management, Innovation and Scaling Up**

18. Knowledge management and communications will be in line with the IFAD Strategy for Knowledge Management, including: (i) annual assessments of service providers by local communities to feed into the annual project planning process; (ii) the policy analysis outputs and other specific studies focusing on rural poverty to inform the government policy making machinery; (iii) annual meetings to review the project performance and the country programme to share lessons learned and best practices among project staff and government counterpart agencies and the co-financiers; (iv) support for the costs of publication and dissemination of studies carried out; (v) the proposed Project Coordination and Consolidation Meetings to solve technical problems and implementation issues; and (vi) a project website for disseminating studies, output and selected outcome data to a wider audience. At the regional level, the stakeholders in the IFAD country programme, including those participating in this project, will receive newsletters on different focused themes from IFAD Headquarters, regular analysis and documentation of lessons and experience learned from the project operations to communicate country-level knowledge from Indonesia, including that from SOLID, to others.

19. The design of the SOLID project has three innovative features. First, the project will introduce as part of the project's value chain approach village federations to handle larger volumes of agricultural products as required by the market with drying, grading, primary processing, etc. Secondly, the project will introduce quarterly Project Coordination and Consolidation Meetings in which project staff and consultants will identify constraints and recommend improvements in operational arrangements, procedures and policies. Thirdly, the project will adopt a more organised approach to capacity building, which is a major project investment, than in the past. This approach includes first conducting a Training Needs Assessment covering staff involved with project activities as well as carrying out an evaluation of the impact and effectiveness of the training provided.

**REPUBLIC OF INDONESIA**  
**SMALLHOLDER LIVELIHOOD DEVELOPMENT PROJECT IN EASTERN INDONESIA**  
**PROJECT DESIGN REPORT**

**II. INTRODUCTION**

1. The mission<sup>1</sup> worked in Indonesia with the government from 18-30<sup>th</sup> October 2010 to complete the design of the proposed Smallholder Livelihood Development Project in Eastern Indonesia (SOLID) (IFAD/PPMS No.1509). The mission's Aide-Mémoire describes the work of the mission and summarises the proposed changes made to the design included in the Draft Project Design Report (PDR) dated 17<sup>th</sup> August 2010. The mission's work was guided by the government, Ministry of Agriculture (MOA) and the National Development Planning Agency (*Bappenas*), and IFAD Quality Enhancement Review of the Draft PDR.

**III. STRATEGIC CONTEXT AND RATIONALE FOR IFAD INVOLVEMENT, COMMITMENT AND PARTNERSHIP**

**A. Rural and Agricultural Development Context<sup>2</sup>**

2. With growing rural-urban migration, nearly half of the Indonesian population of 227.3 million now lives in the urban areas. Agriculture accounts for about 14% of Gross Domestic Product (GDP), while the industry and services sectors account for 47% and 37% of GDP respectively. Growth in the agricultural sector was 3.5% in 2007 which was slightly higher than the average of 3.2% p.a. during the period of 2003-2007. There has been a significant shift in the composition of sector GDP between 1970 and 2007 with a reduction of the contribution of food crops from 61% to 49% (a 19% decrease), an increase in fisheries from 9% to 16% (a 79% increase) and in livestock from 6% to 13% in 2007 (a 112% increase). Indonesia used to be self-sufficient in rice but now has become a major rice importer.

3. Agriculture's share of GDP has declined significantly since 1970 (41% of GDP), with the growth of the industry and services sectors. However, agriculture continues to play an important economic role as it remains the major employer accounting for 43% of the total work force in 2006, a reflection of the relatively low productivity of small-holder production of annual food crop and estate (tree)<sup>3</sup> crops, particularly in Eastern Indonesia. The causes of the low agricultural productivity include inadequate management and marketing systems, use of shifting cultivation systems in some areas, limited knowledge of appropriate and modern improved agricultural practices, lack of effective extension and research outreach, poor rural infrastructure and a lack of supply of production inputs and appropriate sources of finance. The above factors have resulted in the production of poor quality produce with a low market value, despite the cultivation of potentially high value crops e.g. cocoa, nutmeg, cloves etc., without local value addition through processing and marketing. Meanwhile food crop production has focussed on meeting subsistence needs. Market outlets are limited and there is a lack of market information systems. Other factors which have often prevented improved agricultural productivity include multiple, overlapping, uncoordinated and short-term government programmes leading to confusion, apathy, conflict, dependency and a lack of sustainability.

**B. Policy, Governance and Institutional Political and Economic Issues**

4. Indonesia has made a strong economic recovery from the 1997 financial crisis with both political and macroeconomic stability, higher levels of economic growth, and has achieved the status

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<sup>1</sup> Michael Rayner, Mission Leader; Iketut Budastra, Community Development and Small and Medium-Scale Enterprise Specialist; Sumaryo Soemardjo, Financial Management and Procurement; and Constanza Di Nucci, GEF Specialist, IFAD Environment and Climate Division. During the provincial visits the mission was accompanied by two of the SOLID national preparation team from FSA: Djadi Purnomo and Yukoningsih Suciandari, while Reninta Fitrianti from BAPPENAS joined the mission in Maluku. Youqiong Wang, IFAD Country Programme Manager for Indonesia joined the mission for the meetings in Jakarta from 25-29<sup>th</sup> October 2010, while Ms Anissa Lucky Rinaldi, IFAD Country Programme Facilitator for Indonesia attended the meetings on 18<sup>th</sup> and 29<sup>th</sup> October 2010.

<sup>2</sup> Data is for 2008 unless stated and comes from the World Development Indicators database (April 2010).

<sup>3</sup> Estate crops is the term used hereafter for tree crops to accord with the Indonesian convention.

of a middle-income country. Indonesia has graduated from the IMF programme and has terminated the Consultative Group for Indonesia.

5. The economy is well-diversified and the annual growth rate was 6.1% p.a. in 2008 (with forecasts for 5.5% in 2010 and 6% in 2011). GNI per capita (Atlas Method) was USD 1,880 in 2008. In 2005 the real per capita GDP exceeded the level in 1997 for the first time since the crisis. Despite the global economic downturn, the economy is growing steadily. However, Indonesia's growth rate during the last five years has been significantly lower than those of other emerging economies of Asia (China, India, and Vietnam), but Employment growth has been slower than population growth (1.2% p.a.). Public services remain inadequate by the standards of middle income countries and Indonesia is also doing poorly in a number of health and infrastructure related indicators and may fail to reach several of the Millennium Development Goal (MDG) targets<sup>4</sup>.

6. The transition to democratic governance continues as does the decentralisation of service provision. Nearly 500 provincial, district and city governments now play an important role in local administration, social and economic development and in the delivery of public services. Together these sub-national governments are responsible for 40% of public spending. The technical and management capacity of the staff of the decentralised governments remains a constraint to development and especially rural development, as does their dependence on central government funds. The role of the central government agencies has therefore shifted from implementation to that of creating the enabling legal and policy environment for the local governments to take the lead implementing their own development agenda. Decentralisation has also helped contribute to the peaceful resolution of regional and social conflicts, e.g. in Aceh, Papua and Maluku and North Maluku.

7. Since the start of IFAD support for poverty reduction, community empowerment and development in Indonesia in 1978, MOA has implemented most of the IFAD financed projects and programmes through its own specialised agencies. The proposed project executing agency for SOLID at the national level is the Agency for Food Security (AFS) of MOA which implemented the recently completed Post-Crisis Programme for Participatory Integrated Development in Rainfed Areas, IFAD Loan No. 539-ID or PIDRA. The project design and implementation arrangements takes into account the lessons learned from PIDRA and other IFAD and donor supported projects in Indonesia.

8. Other national institutions with an involvement in rural development include: (i) *Bappenas*; (ii) Ministry of Finance (MOF); (iii) State Finance and Development Supervisory Board (*BPKP*), a government audit agency; (iv) Indonesian Agency for Agricultural Research and Development (IAARD); (v) Directorate General for Community and Village Empowerment (*PMD*) of the Ministry of Home Affairs (MOHA) which has the mandate for community empowerment; its Community and Village Empowerment Boards were decentralised to the provinces and districts in 1999, weakening its coordination functions; and (vi) the Ministry of Disadvantaged Regions (MODR).

9. The aspiration of the Government's Medium-Term Development Plan (MTDP) for 2010-2014 is build a nation that is "more advanced and prosperous, more self-reliant, more secure and peaceful, and more democratic and just." The MTDP has 11 national priorities: (i) governance reform; (ii) education; (iii) health; (iv) poverty alleviation; (v) food security; (vi) infrastructure; (vii) investment climate; (viii) energy; (ix) environment and disaster management; (x) outer islands and conflict areas; and (xi) culture, creativity and technology innovations.

10. The 2010-2014 National Medium-Term Priority Framework for Agriculture<sup>5</sup> focuses on the revitalisation of the agricultural sector to increase competitiveness in the national and global economies. The priority strategies include: (i) ensuring food security, producer profitability, and consumer safety and nutritious diet; (ii) developing sustainable agriculture in a climate-changing environment and using green technology and best practices; and (iii) facilitating decent and "green" employment.

11. The following priority areas were proposed for external assistance: (i) food crops, especially rice, corn and soybean; and (ii) institutional and staff capacity for developing and adopting "green" technology in sustainable food crops practices. For cash crops, assistance for small-scale horticulture

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<sup>4</sup> Indonesia still suffers 307 maternal deaths for every 100,000 live births, while the MDG target is 105 by 2015. Despite recent progress 68% of the population has access to improved sanitation, while the MDG target is 86% by 2015.

<sup>5</sup> A joint effort of *Bappenas*, MOA, Ministry of Forestry, and the Ministry of Marine Affairs and Fisheries with FAO.



producers will promote agribusiness and trade, value-added processing, and entrepreneurship. In livestock, the focus is on improved animal breeding and feeding methods and technologies, to allow small-scale livestock owners to increase their competitiveness of local livestock production and processing.

12. The strategy for forestry is to optimise the functions and benefits of forest resources by careful management of natural forest resources in a sustainable manner. The conservation and rehabilitation of forest resources is highlighted as is securing the existing forest cover in 282 watersheds.

13. The focus in fisheries is to increase fisheries productivity and profitability through improving post-capture handling, storing, value-added processing technologies, and marketing. This includes both capture fisheries and aquaculture and the full range of products within each.

### **C. IFAD Country Programme**

14. As of 7<sup>th</sup> January 2011, IFAD has provided loans of the equivalent of SDR 207.76 million or USD 316.82 million for 13 projects to the government of Indonesia, of which 11 are closed and two ongoing. By 7<sup>th</sup> January 2011, the total disbursement of these IFAD loans was SDR 157.76 million, equivalent to USD 240.57 million (76% of the total commitment). IFAD has also funded a number of country and regional grants of about USD 1.59 million in Indonesia to support investment projects in the country.

15. In December 2008, the IFAD Executive Board approved the Country Strategic Opportunities Programme (COSOP) for Indonesia for 2009-2013. The country strategy will continue to support the government in achieving its long-term vision for rural poverty reduction, the MDG targets and the medium-term development targets. SOLID is the first project to be designed under the COSOP for Indonesia 2009-2013.

### **D. Opportunities for Rural Development and Poverty Reduction**

16. There are opportunities for SOLID to contribute to the following national priorities namely: governance reform; poverty alleviation and improving food security; infrastructure development; environment, climate change adaptation and disaster management. By including the provinces of Maluku and North Maluku the project has a focus on the outer islands and areas of conflict a decade ago.

## **IV. POVERTY, SOCIAL CAPITAL AND TARGETING**

### **A. Rural Poverty Information and Analysis**

#### **National Situation**

17. Globally in terms of the Human Development Index (HDI), Indonesia is ranked 108<sup>th</sup> out of 169 countries for which data is available in the 2010 Human Development Report. The value of 0.600 is above the average for countries of medium human development but two places lower than their GNI per capita rank. Over the decade 2000-2010 the average annual HDI growth rate has been 1.82%. The percentage of people living on less than USD 1.0 a day was already below the MDG target in 2006.

18. The recent economic growth has benefited the poor with a decline in the incidence of poverty from 16.7% in 2004 to 13.3% in March 2010, which is equivalent to 31.02 million people. Yet despite these achievements, approximately 50% of the total households remain clustered around the national poverty line<sup>6</sup>. These households are vulnerable to shocks such as food price increases or ill health that can drive them into poverty. The gap between the poor and non-poor is also widening. The Gini Coefficient has increased from 32 in 1999 to approximately 35 in 2009. Regional disparities also persist, with eastern Indonesia lagging behind other parts of the country, notably Java.

<sup>6</sup> The poverty line in Indonesia is IDR 211,726 per capita a month as defined by the Central Bureau of Statistics (CBS) as the amount of expenditure for food calculated on the basis of a daily requirement of 2,100 calories plus minimum expenses for non-food items in housing, clothing, education, transportation and other basic needs.

19. Furthermore, 16.6% of rural people are poor, compared to 9.9% of urban people and 70% of the poor live in rural areas and the rural poor usually lack access to social, productive and infrastructure services. Poor agricultural extension services, geographic isolation and difficult access to markets and financial institutions have limited development opportunities in these areas.

20. The poverty gap index indicates that although the proportion of people living in poverty has fallen to almost the pre-1997 crisis level, those who are poor now are worse off than before. Maluku is among the provinces recording the greatest severity of poverty in 2008 (Working Paper 1).

21. **Gender Inequality Index.** The 2010 UNDP Human Development Report ranked Indonesia 100<sup>th</sup> out of 138 countries in 2008 using the Gender Inequality Index. The value of 0.680 is worse than the average for countries with a medium level of human development (0.591) and much worse than the average for developing countries in East Asia and the Pacific (0.467).

### Maluku and North Maluku

22. Conflicts in Maluku and North Maluku during the period 1999-2003 have had a major effect on the economic prosperity and livelihoods of people in these areas and the combined economy of Maluku and North Maluku contracted by approximately 30% in real terms. Virtually no sector or sub-sector of the economy was unaffected and the economic impacts of the conflicts are still being felt, more strongly so in some areas than others.

23. In 2008, both provinces had higher HDI than the Gross Regional Development Product (GRDP) rankings: 12 points for Maluku and 5 points for North Maluku. The GRDP per capita for the two provinces are the equivalent of USD 510 for Maluku and USD 425 for North Maluku using the current USD:IDR exchange rate. Despite these figures, according to the Central Bureau of Statistics (CBS), 28% of the population in Maluku was living below the poverty line in 2009 and 10% in North Maluku. This apparent anomaly may be partly explained by the fact that Ambon, the provincial capital of Maluku, accounts for 40% of the Maluku economy. The unemployment rate in Maluku in February 2009 was 10%, among the highest level nationally and higher than the national average of 8%. In comparison, the unemployment rate in North Maluku was less than 7%.

24. The Bureau of Statistics poverty data for 2009 shows that ten<sup>7</sup> of the eleven target districts have an incidence of poverty of 18% or more, the target rate<sup>8</sup> for participating districts, while the poverty incidence in Halmahera Selatan, the eleventh district, is below this threshold at around 11%. Overall 70 of the 127 sub-districts in the eleven provinces have poverty rates greater than 20%. The justification for including Halmahera Selatan as part of the project area is based on the fact that eight of the 30 sub-districts have poverty rates of close to 20%, (the target poverty rate for participating sub-districts), which account for 5% of the poor in North Maluku, or 8,000 people. A further four sub-districts have relatively large numbers of poor (nearly 5,000), even though the poverty rate ranges from 8-14%. This analysis highlights the fact that the absolute numbers of poor households should be considered as well as the incidence of poverty when using poverty as a targeting tool.

25. **Food Security.** Both Maluku and North Maluku are provinces that include areas with a cereal deficit. In North Maluku, Kepulauan Sula has a high deficit and Halmahera Selatan a moderate deficit. In Maluku Seram Bagian Barat, Maluku Tengah, Seram Bagian Timur, Maluku Tenggara and Kepulauan Aru all have high deficits.

26. Three of the five districts selected for project activities in Maluku are identified as regions of highest vulnerability under the composite food security index (which takes into account food use, nutritional situation and health aspects): these are Buru, Seram Bagian Timur and Maluku Tengah.

27. The causes of poverty in Maluku and North Maluku can be summarised as: (i) a lack of income, employment and business opportunities and at times a shortage of food; (ii) a lack of access to good quality services: health, education, water and sanitation; (iii) a lack of formalised land rights; and (iv) in some places a deteriorating environment and lack of access to natural resources; (v) the violent conflicts a decade ago; and (vi) a lack of participation by the population in local planning and in

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<sup>7</sup> North Maluku: Halmahera Barat (29%), Halmahera Tengah (27%), Halmahera Timur (22%), Halmahera Utara (18%), and (20%). Maluku: Buru (33%), Buru Selatan (49%), Maluku Tengah (40%), Seram Bagian Barat (47%), and Seram Bagian Timur (41%).

<sup>8</sup> These target poverty rates were agreed with *Bappenas* and AFS during project inception in December 2009.

prioritising development priorities. These causes can be summarised as a lack of access to various forms of human, physical, financial, natural, and social capital.

28. Within Indonesia, North Maluku has the lowest gender empowerment rating primarily because there are no women in the provincial parliament.

## **B. Target Group and Gender Issues**

29. The project target group consists of smallholder farmers, all of whom engage in tree (estate) and food crop production. Great variability exists in the farming systems followed. The tree (estate) crops include coconut/copra, clove, cocoa, coffee, cinnamon, vanilla, cashew nut, and pepper. Major food crops include paddy and upland rice, maize, groundnuts, soybeans, cassava, yams, taro, sago and sweet potatoes. Fruit and intensive vegetable crops are also cultivated e.g. by some Internally Displaced Persons (IDPs) with small plots close to urban centres. Some smallholders also engage in one or more of the following activities: livestock production, fishing or small-scale off-farm income generating activities.

30. The conflicts caused a large number of people - women and men - to lose access to their land. Plantations were destroyed and many people also lost their farm tools and fishing equipment. Today, as a result of improved security, the majority of people have access to their original land. However, due to the damage and intervening neglect (almost four years), incomes initially declined dramatically (by 50-75%), but have now improved to some extent.

31. The socio-economic classification identifies four categories of households: poorest, poor, medium and better off in terms of their livelihood strategies, assets and human capital. The households classified as poorest or poor (with associated characteristics of food shortages and limited assets) account for 13-54% of the total according to the Social Assessment undertaken in the two provinces. Even the households classified as medium are also subject to the risk of food insecurity. This categorisation implies that the difference in socio-economic terms between the three sub-groups is not great. Therefore, the project will include the medium sub-group among the target group, along with the poor and poorest categories. These three sub-groups include the indigenous communities (a majority in both provinces). Major challenges for the target group farmers are the limited access to improved crop husbandry practices, markets and price information. Most depend on traders. The better off households, whose income derives at least in part from trading, are the only socio-economic sub-group which is not engaged in farming activities and while not part of the project target group are likely to be involved in developing value chains.

32. An important target sub-group are women headed households (14% in Maluku<sup>9</sup>) and most belong to the poor or poorest socio-economic categories. The conflicts led to women being widowed or becoming separated and therefore becoming by default the head of a household. These women used to work together with their husbands, but their land may no longer a source of income because it was left unattended for so long. Some women have sold their land, while others have sharecropping arrangements with their neighbours. Others earn money from petty trading, food production and the sale of vegetables. Many live in very small houses, which may be shared with other families.

33. With a low population density and community land available for use, landlessness is not a problem in the project area.

### **Gender Division of Labour**

34. Before the conflict, the roles of men and women were generally divided along traditional lines at both the household and community levels. Men were regarded as the head of the household and their primary role was to provide income for the household and assume the decision-making role regarding family and community matters.

35. Women's primary roles and responsibilities were around the house. In addition to these tasks, women were also engaged in agricultural work and community development activities such as participating in the Family Welfare Programme Movement. As agricultural producers, women's tasks included sowing, watering, weeding, harvesting, drying, storing, selling the products. In addition to

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<sup>9</sup> No data available for North Maluku.

agricultural work, women were also engaged in fish processing both for family consumption and sale.

36. The gender division of labour has changed as a result of the conflict - men are no longer perceived as necessarily the primary income earner. Women and children are also increasingly generating income for the family due to the increase in poverty. Women's role in the community has increased as well as their role in decision-making at the family and community levels. This has brought an increase in women's self-esteem and confidence, but also an increasing workload. Although women's political participation is still limited, it seems to be increasing, especially at the village level as more women participate in village organisations and as members of village councils. Women's organisations and networks such as savings and credit groups, labour sharing groups, and religious based groups linked to income generation have gradually increased. While women play an important role in agriculture and rural development, they are not provided with proper inputs, adequate training and skills. Most extension workers are men.

### **C. Targeting Strategy and Gender Mainstreaming**

37. Based on the incidence of poverty, cereal deficits and as agreed with *Bappenas* and the Agency for Food Security (AFS), the project will target a total of 11 districts, five in Maluku and six in north Maluku. As noted above, there is a wide range of poverty incidence among the sub-districts within the target districts which will be a key determinant in the selection of the sub-districts.

#### **Targeting Strategy**

38. Within the target districts, the following are the criteria for selecting the sub-districts and villages for participation in the project: (i) exclusion of all urban villages and urban sub-districts; (ii) incidence of poverty >20%; (iii) potential for agricultural productivity and livelihoods improvement and rural poverty reduction; (iv) commitment from the local government to participate in the project; (v) availability of providers of rural services (public, private and/or NGOs) with the capacity to deliver the services to the target groups; (vi) accessibility with a maximum journey time from the district or sub-district HQ of around four hours; and (vii) availability of a district agricultural office and/or office of food security at the sub-district level.

39. For reasons of cost effectiveness and management efficiency, the project will target 4-7 sub-districts in a district and a cluster of 5-6 villages in a sub-district, with the exact number to depend on logistics and the capacity of the staff of the districts and sub-districts. Project activities will be phased so that the project would support activities in each target village for four years.

40. Within the sub-districts, the project will target about 330 villages with: (i) a large number of poor households, where there is a potential for increased agricultural productivity, improved food security, higher household incomes and improved natural resource management; (ii) a large number of households from the poor and poorest socio-economic groups, including female headed households; (iii) where people express a need for assistance and guidance; and (iv) people are willing to work together in a participatory way. The project will target poor indigenous and immigrant communities (including where appropriate transmigrant communities).

41. In PY 1 the project will target 44 villages in 31 sub-districts in the 11 districts. The selected villages have a total population of nearly 70,000 belonging to 17,600 households, 10% of which are headed by women, with a high average incidence of poverty, 58% (20-100%). The villages appear to meet the project's poverty targeting criteria. The majority of the population in the target villages (54%) are classified as native speakers (range is 0-100%).

42. The list of target villages and sub-districts is attached to Annex VIII, while the AFS will complete the selection process with the lists of those to be targeted in PY2-5 submitted to IFAD for review and comment after base line survey is completed in 2011<sup>10</sup>. It is important that the AFS complies with all the targeting criteria, including those related to the number of target villages per sub-district and the number of sub-districts per district.

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<sup>10</sup> A complication occurs when using the incidence of poverty for targeting because there are two sources of poverty data at the sub-district level: *BPS* and Social Protection Survey (*PPLS* 2008), with the former the preferred measure, for consistency with provincial, district and national level data. However, only *PPLS* data are available at the village level.

43. The project will use a participatory approach in the selection of an estimated 49,500 households in the target villages using a gender-sensitive poverty and livelihood analysis e.g. participatory wealth ranking, identification of common interests etc.

44. Targeting effectiveness will be assessed by the supervision missions and the mid-term review. Where there are complementary projects in the target villages and sub-districts, the SOLID project activities will be harmonised to enhance its complementarity with other projects.

### **Gender Mainstreaming**

45. Women in Indonesia play a significant role in the country's economic and social development, but their productivity suffers from limited skills, lack of access to appropriate technology, business development services and product and input markets.

46. Mainstreaming gender considerations in all project activities will increase the skills and role of women in production and marketing and their participation in decision-making. Such an approach will bring about a gradual transformation of gender relations in the process of social and economic development. It would also promote gender equality overall and seek to address the needs of the more marginalised groups of women, such as female-heads of households.

47. The project will use the following approach to increase the economic wellbeing and status of women: (i) enhancing the value of production and processing activities dominated by women through skills training and introduction of new technology; (ii) using a group approach (women only or mixed groups) for improving quality standards and marketing; (iii) promoting women entrepreneurs to provide business development services and to venture into value chain activities often dominated by men, e.g. primary marketing; (iv) building women's leadership skills to participate in the governance of groups and their unions; (v) sensitising men to support women's enhanced role in the value chain development; and (v) building the capacity of groups and their unions and those of the local government institutions to ensure gender responsive service delivery.

48. **Strengthening Gender Mainstreaming at the Decentralised Government Structure.** SOLID will sensitise and train planners and sector staff at district and sub-district levels as well as key project staff (coordinators, sector specialists, and monitoring and evaluation staff) to institutionalise gender mainstreaming into district and local level development planning and management practices. The project will conduct gender analysis of district level planning, monitoring and evaluation frameworks and developing guidelines and checklists in four areas (community development and poverty reduction, agriculture and infrastructure).

## **D. Geographic Coverage of the Project**

49. The project districts in North Maluku are: Halmahera Barat, Halmahera Selatan, Halmahera Tengah, Halmahera Timur Halmahera Utara and Kepulauan Sula and five districts in Maluku: Buru, Buru Selatan, Maluku Tengah, Seram Bagian Barat, and Seram Bagian Timur. These districts consist of the two largest islands, Buru and Seram and their adjacent islands, and are the areas closest to North Maluku. Based on the availability of funds, the project will aim to target about 330 villages and 60 sub-districts.

## **E. Main Characteristics of the Project Target Area**

### **Geography, Climate and Natural Resources**

50. The Maluku archipelago consists of 1,208 widely scattered islands in eastern Indonesia and known historically as the Spice Islands. Combined, the two provinces cover over 850,000 km<sup>2</sup>, only 10% of which is land. The provinces of Maluku and North Maluku constitute the north central part of Indonesia, bordered to the North by the Talaud islands and then the Philippines, to the west by Sulawesi, the east by West Papua and the south by the Western Daya islands and East Timor<sup>11</sup>. Located 3° north to 5° south of the equator, the two provinces have a hot humid climate with a daily average temperature of 27° C, with a range from 23° C to 30° C.

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<sup>11</sup> Working Paper 2 provides most of the data in this section of the report.

51. The Maluku Islands comprise some of the most geologically complex and active regions in the world<sup>12</sup>, resulting from their position at the meeting point of four geological plates and two continental blocks. The islands that constitute Maluku and North Maluku are part of the region known as Wallacea, which contains a distinctive fauna representing a mix of Asian and Australasian species, many of which are endemic.

52. The geography is characterised with hundreds of mountainous small islands with narrow low-land areas along the coastal fringe. Most of the islands are mountainous, some with active volcanoes. The vegetation is very luxuriant; including rainforests. A diverse range of soils are present. The high presence of alluvial and volcanic soils and absence of pressure on land resources (except in transmigration and IDP/returnee areas) means that most soils are of moderate to good fertility. The residential areas are scattered in the low-land areas facing the sea while the farms are terraced in the slopes of the main land mountains.

53. Some 34% of the land area of North Maluku is forested, with half this area (17%), some 526,705 hectares designated as conservation forest. Within this area, non-timber forest products may be collected, but no green timber cut. A larger proportion of the land area of Maluku is forested (58%) with a similar proportion designated as conservation forests (17%), or 805,451 hectares.

## Population

54. Together the population of the two provinces is slightly more than two million (less than 1% of Indonesia's total population), with 1.358 million in Maluku and 0.995 million in North Maluku). Overall 59% are Muslims and 40% Christian<sup>13</sup>. Within the provinces, North Maluku has a Muslim majority and Maluku has a Christian majority. Many of the Christians are of ethnic Chinese descent. Since Indonesia's independence, the population has swelled due to immigration mainly from nearby South Sulawesi. Migrants have also come from Sumatra and Java. Some of this migration has been spontaneous, while other migrants have been part of government's transmigration programmes. More recently the population has been augmented by IDPs from other islands. Population density remains low, about 10-42 persons/km<sup>2</sup> in the 11 target districts.

55. The data for the population of Indigenous People (IP) by district shows that the proportion ranges from 47-88% of the total using the *AMAN* (Indonesian Customary Community Alliance) definition that defines the indigenous population as those whose ethnic group considers themselves as indigenous to the two provinces, or *Anak Negeri*. Indigenous People account for the majority of the population in all of the target districts in North Maluku, ranging from 55% to 75%. However in Maluku, Indigenous People accounted for just less than 50% of the population of Buru and Seram Bagian Barat, but 88% and 70% in Seram Bagian Timur and Buru respectively. The Indigenous people are from 44 different ethnic sub-groups with 22 sub-groups found in each province.

56. The project design will include the following specific activities to address the needs of IP: (i) a proposal for an assessment of the IP situation at the start of project activities in any village and training for project and NGO staff on IP issues; (ii) costs have been included in the district and provincial cost tables for these activities; and (iii) improvement of IPs' natural environment, including: biodiversity, dry land agriculture, livestock, forest produce collection, fishing and aqua culture (sea weed).

## Village Organisation

57. The population is clustered around the coastal areas, facing the sea and with sloping agricultural land at the back. Indigenous people traditionally live in customary villages which can be either Moslem or Christian. In Maluku the customary village head (or Raja) is also the formal village head and the traditional hereditary village structure and institutions are integrated into the formal government structure. A customary village, (*Negri*) structure consists of: (a) a Raja (the executive leader); (b) a *Saniri* (the legislative leader); and (c) a *Kemang* (judiciary leader). A *Negri* is sub-divided into a number of *Soa* (sub-clans). The customary village institution remains the social decision making processes, particularly, for marriage arrangements, socio-political orientation, resolving social disputes, and for natural resource management. In North Maluku the governing role of the customary

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<sup>12</sup> Monk, K.A.; Fretes, Y., Reksodiharjo-Lilley, G. (1996). The Ecology of Nusa Tenggara and Maluku. Hong Kong: Periplus Editions Ltd.p.9. [ISBN 962-593-076-0](#).

<sup>13</sup> Other estimates give differing proportions.

village institution has declined and in most places the Rajas and Soas no longer exist.

58. The residents of each island generally have their own (spoken) language. Each group has its own customs and traditions, which the agencies supporting livelihood improvement activities need to take into account when working in the villages. The local culture is typically blood/ethnic based, although modified by religion, and is in harmony with the natural environment. The Addendum to Working Paper 1 provides further information.

### **Land Tenure and Availability**

59. Despite the low population density, the SOLID project database recorded rather small land holdings: 1.36 ha per household for the target districts in Maluku and 0.96 ha per household for the target districts in North Maluku i.e. less than the area received by immigrants under the national transmigration programme. However, the figures from the database do not include customary common land, or forest land cultivated by farmers, which is owned by the Government.

60. The cultivated land in Maluku includes communal land and individual land holdings, while the cultivated land in North Maluku is primarily individual land holdings. In 2008 in Maluku, according to the Government statistics, government land accounts for 44%, communal land 28% and individual and private land 28%. The communal land or traditional land rights were recognised by the 1960 Indonesian agrarian laws as '*Hak Ulayat*'. The communal land belongs to local ethnic sub-groups or clans (Soas). In a village, there may be 5-17 Soas with up to 15 ha of land each.

61. Such communal land is not recognised in North Maluku. The majority of cultivated lands in this province are individual holdings, which are: (i) inherited by the smallholders from the previous generation; or (ii) forest land cleared by the families. Only a small proportion of the individual land holdings have formal certificates.

### **Economy**

62. The islands have for centuries been a major source of cloves, nutmeg and mace. These spices are valuable as exports, along with cocoa and copra. The regional economies of North Maluku and Maluku depend on the export of a range of primary commodities, most without any processing. Very little of the production of the export crops is consumed locally as the absorptive capacity of the local markets is small. In places fishing, including shrimp, crab and tuna is important as is timber production and the mining of manganese, nickel, and oil.

63. Most economic activity, including trade, tourism and education, is centred around the provincial capitals in Ambon and Ternate (the latter has just transferred to Sofifi, on the larger island of Halmahera). Despite these urban sources of revenue, agriculture and fisheries are still the key components of both provinces' economies, and represented by people's primary occupation, 62% in Maluku and 86% in North Maluku.

64. The economic livelihood activities of the IP in Maluku and North Maluku are also closely related to the natural environment, including: dry land agriculture, livestock, forest produce collection, fishing, aqua culture (sea weed) and mining.

### **Communications**

65. Most parts of the project areas are accessible either by sea, road and/or air. However, as there are many scattered small islands access journey times can be long and travel costly. From some locations a day's travel is needed to reach the district centre, while some areas are not connected to the provincial roads. The ports of Ambon and Tual in Maluku and Jailolo in North Maluku serve as export ports. Both Ambon and Ternate have international airports, which there are small airports at district level.

### **Farming Systems**

66. The agriculture system in Maluku and North Maluku is dominated by mixed smallholder farms. The principal cash crops are nutmeg, clove, coconut, and cacao and their relative importance varies from place to place and island to island. Coconuts are the major estate crop in both provinces but

more important in North Maluku than in Maluku, while there is also a greater area of cacao in North Maluku. There is a similar area of nutmeg in both provinces, but Maluku has the larger area of cloves. Small areas of vanilla, pepper and cinnamon are grown in North Maluku.

67. The main food and fruit crops include upland rice, banana, papaya, durian, mango, cassava, sweet potato, *keladi*, other root crops and crops such as maize, groundnuts and soybeans. Sago, which is the traditional basic food, is becoming less popular as people tend to substitute Sago with imported rice. Although paddy rice is grown the area suitable is very limited and most is cultivated by the transmigrants.

68. In Maluku, the cropping pattern is generally mixed involving cacao trees with coconut trees, and some fruit trees and food crops such as banana, cassava, and other root crops. In North Maluku, the cropping pattern is generally intercropping where cacao trees are planted between coconut trees and some fruit trees in plots separate from the food crops. Additionally, the smallholders in North Maluku also generally practice a higher level of farm management in terms of pruning, weeding and pest control. The productivity and quality of the smallholder cacao beans in Indonesia has declined since 1995 due to Cocoa Pod Borer with an estimated yield loss of up to 40%. The Cocoa Pod Borer and Vascular Streak Dieback are regarded as the most important pest and disease currently threatening the productivity and product quality of cacao farms in Indonesia. Similarly, the Aflatoxin problems are regarded as most important issue threatening the product quality of nutmeg farms in Indonesia.

69. Smallholders generally use a minimum of modern production inputs due to limited working capital and price uncertainty. Diversified use of resources is the common livelihood strategy. Only limited amounts of labour are used. In general crop yields reflect the low input systems followed. In general, farmers have limited access to improved cultivation technologies and crop husbandry practices, markets and price information and depend on middlemen. Data availability does not allow a further definition and characterisation of different systems within this model based on an analysis of the agro-ecological situation<sup>14</sup>.

70. In addition to the crops, the smallholders may also keep cows, pigs (in Christian communities), and chickens. Rearing methods are generally extensive leading to uncontrolled breeding. The practice of regular worming and vaccination (other than for zoonosis diseases) is rare and diseases tend to be left untreated. Consequently production under these extensive, low management systems tends to be low and entails high risk. Veterinary services have a low coverage.

71. A traditional law (*Sasi*) governs the harvest from natural resources such as forests, seas and communal lands with 10% of the output going to the village Mosque or Church. Prior to harvest the Mosque/Church will organise a village auction involving the *Soas* as the participants. The winner earns the rights to the harvest. The *Kewang* guards the harvest areas and determines the date for harvest. This traditional law remains effective in most parts of Maluku and according to *AMAN*, there have been some recent initiatives to apply it to the sustainable uses of natural resources.

72. **Forestry.** Community forestry programmes, although planned by government, have yet to be implemented in the two provinces. These programmes are targeted at critical land areas, and indicative targets have been set of some 1,000 ha for North Maluku and 2,035 ha for Maluku.

73. **Fisheries.** The location of North Maluku and Maluku islands within warm tropical waters with adjacent deep sea areas means that the fisheries are very productive and as yet are not being over exploited. Occasionally, farmers catch fish for own consumption using simple equipment and un-motorised boat. In a few of the target villages, there are small scale fishery activities but many are commercially underdeveloped as they use simple equipment, lack market access due to their remoteness and the under developed infrastructure.

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<sup>14</sup> Before the creation of the two provinces, the statistics for the two provinces were collected in combined form until 1998, when the Maluku figures continue, as the smaller province, but agricultural data for North Maluku is only available for 2007. The separation coincided with the social conflict and a decline in the cultivated area from 1999 to 2002 of about 10%. The administrative split and the fact that estimates made when the provinces were combined, were more accurate for some crops than others makes any analysis of the area, production and yield data problematic. In addition, the Social Assessment did not include the same data for both provinces further compounding the difficulties of making a comprehensive assessment of the farming systems including the provision of quantitative estimates for production etc. in both provinces.



## **Off-farm Enterprises**

74. The large size of the rural sector when compared with the urban population, and weak purchasing power in rural towns and villages, creates a difficult commercial environment for non-farm enterprises. There are some home industries processing local agriculture products, such as wet sago flour, sago cakes, copra, coconut oil, and some essential oils. In addition, there is the usual range of micro-enterprises: small shops and restaurants; motorcycle repair, metalwork and carpentry shops; tailors and dressmakers; electrical repair shops; hairdressers; and small trading enterprises. The development of this sector is dependent on the establishment of stronger commercial links with urban businesses (for example in outsourced manufacturing contracts), and on the growth of local purchasing power arising from increased production of export commodities. Dependence on off-farm livelihood sources was markedly higher among the Internally Displaced People and refugee villages, which have less access to land, than members of other communities.

## **Rural Finance**

75. Banks, the state pawnshops, saving and credit cooperatives and the financial management units of social projects provide financial services in the rural areas. In 2009, in Maluku the banking sector consisted of 61 branches of state and local government banks and 2 branches of private bank. The corresponding figures for North Maluku were 39 and 6 branches respectively. However, most of the banks operate in the more developed areas and serve the better off sections of the population, leaving the target villages and smallholders without such services. As elsewhere in Indonesia, there are many saving and credit cooperatives e.g. KSP, USP, BMT, and CUs; and microfinance institutions established by previous and ongoing social projects e.g. P4K, UED-SP, TPSP, KUBE, and UPKs. Statistics and recent performance data for these organisations are unavailable. However, it is thought that only a few are performing well and providing appropriate services to smallholders in terms of loan sizes, repayment schedules, costs, and accessibility. The reasons are the lack of effective technical support and supervision, in-competent and dishonest staff, slow growth and a shortage of capital.

## **Value Chains in Maluku and North Maluku**

76. There are several value chains (Working Paper 3) that are important for the livelihoods of the smallholders in the target villages. These include copra, cacao beans, nutmeg and mace, cloves, fisheries and other marine products, rice and other annual food and cash crops. Two of these value chains, namely nutmeg and mace and cacao beans have been the subject of the analysis included in the Addendum to Working Paper 3.

### **Nutmeg and Mace**

77. The region is an important producer of the world's supply of nutmeg and mace. The analysis shows that only 30% of the nutmeg and mace traded are of a good quality. The decline in quality is due bad farm management, early harvest and inappropriate post harvest handling. Marketing involves a series of traders (rural traders, district/inter-island traders, provincial traders (in Ambon, Ternate, and Manado), exporters (in Surabaya), and multinational importers, processors, and manufactures. The processors and manufacturers are primarily overseas industries. Of the export sale price, the smallholders' price share is 58% for nutmeg seed and 56% for mace, while the net margin received by the traders along the supply chain is 38% for nutmeg seed and 41% for mace. Most of the nutmeg and mace is exported and local nutmeg processing and manufacturing industries are underdeveloped despite favourable policies due to a limited demand, and high costs. The main links in the value chain are the vertical links between some traders along the nutmeg value chain. These links are generally informal, trust base, and long-term and may be formalised in written contracts and also involve information sharing and financial assistance.

78. There is no strategic coordination of the nutmeg value chain to maximise its competitiveness in the market or to ensure an equitable distribution of the resulting added values between the participants, including the smallholders. No one is addressing the aflatoxin problem which has reduced the competitiveness of the Indonesian exports to Europe *vis à vis* Grenada. Traders, but not smallholders are aware of the aflatoxin problem but no action has been taken to solve the problem.

79. The nutmeg value chain is principally governed by the export quality standards and estimated prices. The export quality standards and prices are generally imperfectly disseminated by the

exporters to the smallholders, through the value chain. There is a little interest among the traders in assisting the smallholders to improve their product quality and so gain a larger share of the value addition created by the value chain. In general, the smallholders have little control over the governance of the value chain. Under these circumstances opportunities exist for smallholders to engage in nutmeg seed collection, storage and trading.

### **Cacao Beans**

80. The region is also becoming an increasingly important Indonesian producer of cacao beans. The value chain is similar to that for nutmeg and mace and involves a series of traders (village, district and provincial levels). As with nutmeg and mace quality is similarly poor. Traders offer a uniform low price for ungraded production. Of the export sale price, the smallholders' price share is 59% for cacao, while the net margin received by the traders along the supply chain is 25%. The horizontal and vertical links within the value chain links are similar to those in the value chain for nutmeg and mace.

81. Compared with nutmeg a greater proportion of cacao (20%) is used by domestic processors and manufacturers, but mostly outside Maluku and North Maluku e.g. Makassar which is close to the major cacao production area in South Sulawesi. As with nutmeg processing the business policy environment while favourable lacks implementation. In addition the supportive infrastructure and services required, including transportation, post harvest facilities, power generation and other services required are generally inadequate.

82. The governance of cacao value chain in the two provinces is the same as the nutmeg value chain: (i) there is no strategic coordination to improve competitiveness and/or achieve an equitable added value distribution among the participants, including the smallholders; (ii) the value chain is principally governed by the export quality standards and prices. Under these circumstances opportunities exist for smallholders to gain some additional value added from trading, testing and drying and primary processing of cacao for export to Makassar and Surabaya.

### **Other Value Chains**

83. Other major product value-chains<sup>15</sup> with a possible potential for project investment and associated support, subject to more detailed studies, and which can have an impact on a large number of smallholders are: (i) collection, filleting of fish, storage in ice boxes and transport to cold storage for subsequent export; and (ii) provincial and local (fragmented) market oriented value-chains involving food crops such as paddy, cassava and sago, and other estate crops such as coconuts. The analysis in Working Paper 3 shows that the net value accruals<sup>16</sup> for the proposed target value chains are mostly in the range of 20-35%.

### **Environment for Value Addition**

84. While the provinces have a comparative advantage in several agricultural commodities, conditions for value-addition are rather unfavourable. Examples include: (i) limited availability of skilled-labour; (ii) limited access to capital on affordable terms; (iii) dependence on expensive diesel-oil for power and energy; and (iv) inadequate industrial infrastructure and supporting firms and institutions. The limited availability of cold storage, packaging and printing services is hindering the evolution of a competitive value-adding and employment generating agro-processing sector in the provinces. Value chain and private sector development initiatives will necessarily have to address such constraints. Opportunities exist for enhancing productivity and efficiency in some pre and post-harvest activities and in addressing the above constraints.

85. The development of Micro and Small Enterprises (MSE) is necessary if there is to be a greater value addition within the two provinces. Policy at the provincial level emphasises the development of rural micro enterprises and MSE clusters as instruments for rural poverty reduction. However, the provinces have yet to put in place support policies to foster the Small and Medium Enterprise sector, rural-urban business linkages and to link Government initiatives effectively with

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<sup>15</sup> These are product value-chains where a large number of producers may realise the benefits. Also scope exists for competitively establishing value-added projects targeting either the provincial or export market within a reasonable time-frame.

<sup>16</sup> In general net value accruals are prudently estimated as 30-40% of the difference in price between the processed and unprocessed product with the difference accounting for the costs and losses in processing. Where there is no processing e.g. only grading the percentage will be higher.

those of private sector groups e.g. the Indonesian Chamber of Commerce and Industry (*KADIN*).

86. Re-structuring the value-chains in favour of smallholders may in some cases be possible by smallholders grouping, forming networks and negotiating with traders. In other situations producer groups may adopt the role of traders and eliminate the opportunities for rent seeking. This approach is akin to the IFAD supported PIDRA model where producer networks have assumed the role of traders. A role that could graduate into value-added processing, further enhancing value-addition for the poor.

## Administration

87. **Province.** Maluku province was divided into two provinces in October 1999: North Maluku (capital Sofifi but previously Ternate) and Maluku (capital Ambon). Maluku has one municipality and seven districts with 64 sub-districts and 886 villages. About 85% of the villages are located in the coastal areas. North Maluku province consists of six districts and two municipalities with 78 sub-districts and 919 villages.

88. **Provincial Institutions.** With decentralisation, the provincial governments are now concerned with coordination of regional planning for programme development, implementation, delivery, and monitoring and evaluation. These agencies are directly under the Provincial Governor. The provincial agriculture-related agencies coordinate with the central ministries in the implementation of national or donor-supported development programmes, while *Bappeda*, the provincial planning agency, has a similar role to that of *Bappenas* at the national level.

89. The main agencies that have responsibilities in the rural sector are the following: (i) Agency for Food Security (AFS); (ii) *Dinas* Agriculture – with divisions of Livestock Development, Estate Crops Development; and Horticulture Development; (iii) *Dinas* Marine and Fisheries; (iv) *Dinas* Forestry; (v) *Dinas* Cooperatives; (vi) *Dinas* Industry and Trade; and (vii) *Dinas* Public Works. There are two different institutional models in the two target provinces, based on the presence or absence of an AFS:

- Model 1 is in Maluku province where a Provincial AFS exists and three agriculture-related agencies (*Dinases*): (i) *Dinas* Agriculture (food crops, horticulture, estate crops, and livestock); (ii) *Dinas* Marine Affairs and Fisheries; and (iii) *Dinas* Forestry.
- Model 2 is in North Maluku where the *Dinas* Agriculture has a food security division in addition to food crops, estate crops, and livestock. The *Dinas* Forestry and *Dinas* Marine Affairs and Fisheries are separate agencies.

90. Key agencies include those responsible for extension and research and development. The Extension Coordination Agency (*Bakorluh*) is an integrated extension unit at the provincial level established in 2009 based on Extension Law No. 16/2006. It has responsibility for agriculture, fisheries, and forestry extension. The Assessment Institute for Agricultural Technology or AIAT is a provincial unit of the Indonesian Agency for Agricultural Research and Development (IAARD) that is responsible for assessing, identifying, and disseminating improved technologies (e.g. new crop varieties, good agricultural practices such soil and nutrient management, integrated pest management, integrated crop management, post-harvest and processing, etc. There is one AIAT in each province which is coordinated at the central level by the Indonesian Centre for Agricultural Technology Assessment and Development (ICATAD). These two institutes are important for project implementation because they are the main sources of new and improved technologies and information, technical guidance and training support, and communication materials for extension.

91. The Provincial Technology and Extension Committee (PTEC), an inter-agency committee, provides coordination. Strong research extension linkages are also necessary.

92. Other relevant provincial institutions include universities: (i) University of Pattimura in Ambon, which has a faculty of agriculture and a Community Empowerment Research Institute; and (ii) the smaller Muhammadiyah University in Ternate, which is a private university with a Faculty of Agriculture. In addition, the Provincial Centre for Agriculture and Livestock Production and Seeds/Seedling Certification in Ambon is a government centre that certifies seeds produced by farmer seed producers and sub-district seed centres to ensure the quality of seeds sold to farmers. The Provincial Centre for Seedlings and Protection for Estate Crops in Ambon is under the MOA

Directorate General of Estate Crops and has a research mandate. It identifies improved local clones of nutmeg, cloves, and biological pest and disease control methods. It produces seedlings of new clones of estate crops (e.g. nutmeg and cloves) through private contracts. Finally, the *Pelagandong* Project in Ambon, Maluku is a UNIDO/ILO project with the local government of Maluku. The project is engaged in value chain development e.g. the production and sale of nutmeg juice.

93. **District Institutions.** Since decentralisation, the districts have the major responsibility for development and service delivery and the number and organisational structures of the decentralised district agencies vary widely between districts in line with their specific needs, with a proscribed maximum of 13 agencies. The district agencies report directly to the District Mayor (*Bupati*) but coordinate with the line agencies of the MOA and other ministries in the implementation of national programmes funded by the government or by donors.

94. **Agriculture-Related Government Agencies.** In the 11 target districts in Maluku and North Maluku, there are three different institutional structures for the district agriculture-related agencies, based on the presence or absence of an AFS or a unit responsible for food security.

- In Model 1, the Agency for Food Security and Extension (AFSE) is an AFS integrated with extension and operates as a separate agency. The *Dinas* Agriculture includes food crops, horticulture, estate crops and livestock divisions, while *Dinas* Marine Affairs and Fisheries, and *Dinas* Forestry are separate agencies.
- In Model 2, the *Dinas* Agriculture has a division for food security in addition to food crops, horticulture, estate crops, and livestock. There are separate *Dinas* Marine Affairs and Fisheries, *Dinas* Forestry, and a new integrated Agricultural Extension Agency (*Bapuluh*).
- Model 3 is like Model 2 except that the *Dinas* Agriculture does not have a food security division but has an extension division. The other *Dinases* are separate agencies but the *Dinas* Forestry and Estate Crops is an integrated *Dinas*.

95. These differing situations will necessitate some variations in the implementation arrangements between districts.

96. The district agriculture-related agencies are now developing appropriate programmes that address local issues and problems. Crop and horticulture production, agribusiness improvement and marketing, livestock development, post-harvest and processing, agriculture-related infrastructure development, extension and food security are areas identified for project assistance. The various district agencies would participate in the project as collaborating agencies. Staff numbers and capacities vary widely. Because of limited information, it was not possible to assess the capacities of staff in the key agencies, which will be part of the training needs assessment to be carried out in PY1.

97. A key district agency is *Bapuluh*. The extension workers from three *Dinases*, agriculture (including food crops, horticulture, estate crops, and livestock), marine affairs and fisheries, and forestry have been transferred to this agency. The district *Bapuluhs* are coordinated by the Provincial Extension Coordination Agency (*Bakorluh*). Working Paper 2 has further details.

98. The following district government agencies are also relevant, either directly or indirectly, include: (i) *Bappeda*- the district planning agency; (ii) Industry and Trade; (iii) Cooperatives; (iv) task forces at the sub-district level under the *Dinases* with specific responsibilities for certain themes or locations; (v) Land and Water Division of *Dinas* Agriculture provides technical design and supervision support for the construction of small agriculture-related infrastructure; (vi) Public Works - provides technical support for the design and supervision of infrastructures.

99. **Sub-district Institutions.** At the sub-district level, there is an integrated Agricultural Extension Center (*BPP*), which is the home of the field extension workers assigned to villages within that sub-district. The *BPPs* are under the District *Bapuluh* if a separate extension agency has been established or integrated into the Food Security and Extension Agency (FSEA). Otherwise, they are under the *Dinas* Agriculture. Although the MOA policy is to assign one extension worker (*PPL*) to each village, one extension worker currently covers 3/4 villages due to the limited staff available. With this ratio and where the villages are isolated, or are on separate islands, the provision of extension services is inadequate and ineffective. The contracted extension staff (*THLs*) makes up about 23% of the total extension staff in Maluku and 29% in North Maluku. In practice, the *THLs* are not assigned to

specific villages. Further, the government agencies were not sure whether their contracts will be extended in 2011. Working Paper 5 provides further details on the numbers of extension staff.

**100. Private Sector Service Providers.** There are few private service providers. Sometimes, private input companies (fertilizers, seeds, and pesticide suppliers) provide technical advice to farmers buying these inputs. In Maluku Tengah District, an international NGO (Mercy Corps) provides technical support and training for cacao farmers.

**101. Non-Government Organisations (NGOs).** There are more NGOs with offices in Ternate than in Ambon. The focus of the NGOs is mainly on humanitarian relief and reconstruction following the violence in the two provinces between 1999 and 2003. Most of the NGO activities are driven by the agenda and schedules of their external donor funding agencies. The local NGOs vary in their capacity to implement village-level activities. Some have developed relationships and local knowledge that are essential for successful grassroots development. A few international NGOs, such as CARE and Mercy Corps, also provide support for sustainable agriculture and capacity building for some local NGOs, in addition to providing humanitarian assistance.

**102. Village Institutions.** In each village, there is an elected Village Head and an “elected village representative body” or *BPD*. The village leader, in consultation with the community, appoints the members of a committee for developing community programmes (*LPM*). The administrative Village Head oversees the functioning of these two institutions. As noted above in places in Maluku the traditional hereditary village leader or *Raja* is the Village Head. In villages targeted by *PUAP* there is a federation of village groups (*Gapoktan*) to which the individual groups belong and which acts as a village management unit in respect of agricultural marketing, providing finance etc.

**103.** The roles of the *BPD* and the *LPM* are not clear to the villagers and many committee members have not been trained on how to carry out their responsibilities, hence their capacity for village governance is weak. The governance role of the village institutions was weakened further by the civil strife.

**104.** There are also informal voluntary community groups with no legal status. These groups have been established through local initiatives to serve specific community needs such as participation in the implementation of government programmes. They include farmer groups, religious groups, youth associations, women’s groups, self help groups, etc. In some villages, farmer groups have formed farmers’ federation to access block grants from external programmes to support productive activities.

## V. PROJECT DESCRIPTION

### A. Knowledge Base: Lessons Learned from Previous/Ongoing Projects

**105.** Continued economic growth is fundamental to reducing the incidence of rural poverty and the vulnerability of the majority of the population that lives above the poverty line, but on less than USD 2 per day to falling below the poverty line. Non-income poverty also exists and the provision of rural infrastructure can continue to contribute to reducing poverty.

**106.** A major lesson learned from previous projects in Indonesia is that the design of SOLID should give a major emphasis to raising farm and non-farm productivity. Empowering the poor should not be an end in itself, but a means to help reduce the incidence of rural poverty. The project design should: (i) support the move from subsistence agriculture towards a local market based agricultural economy; (ii) promote value chain development, including agro-processing and improving market access; (iii) treat gender mainstreaming as a cross-cutting issue; and (iv) understand the perspectives of the beneficiaries.

**107.** Among other lessons learned are that: (i) institution building is important as a pre-requisite for the sustainability of community groups and organisations; (ii) savings mobilisation for lending within self-help groups is an important stepping-stone before groups and individuals can access credit from MFIs and the formal banking sector; (iii) the Government and IFAD need to provide adequate implementation support, including financial management, procurement and M&E, for fiduciary risk management and knowledge management and engagement in policy analysis and advocacy; and (iv) project procurement has been a frequent cause of delays which has reduced the effectiveness of the

inputs, including good quality seed and/or planting material due to their late arrival.

108. Some specific lessons from PIDRA are that: (i) building Self-help Groups (SHGs) and their Federations is important in the strategy of a project that aims to improve the livelihoods of the poor; (ii) establishing strong SHGs takes about 2-3 years with a further two years to mentor the federations; (iii) the poor should not be rushed to take up new micro and small scale enterprises when large amounts of finance and risks are involved; (iv) the use of a participative approach and a good quality of NGO facilitation service are critical elements of the success in building the capacity of the target community institutions; (v) Government bureaucracies and NGOs can work together in the successful implementation of a project, but it requires adjustment on both sides and intensive and regular training of staff; (vi) the M&E system should be designed at the beginning of a project; and (vii) community institutions involved in managing infrastructure, marketing, purchase of inputs in bulk should be heterogeneous i.e. not only include the poor.

109. Finally, for operational and procedural reasons related to the transfer of IFAD loans to sub-national governments, IFAD should finance SOLID as “a central government project” through the AFS of the MOA, with AFS delegating responsibility for project implementation to the provinces and districts. The latter will deliver the necessary agriculture and rural development services to the poor as a decentralised poverty reduction programme. The two provinces will provide coordination and technical and management support.

## **B. Ongoing Government and Donor Activities**

110. Donor-supported projects include: (i) National Programme for the Empowerment of Rural Communities (*PNPM-Mandiri-Rural*); (ii) Support for Poor and Disadvantaged Areas (SPADA); and (iii) *Pelagandong Project* (UNIDO and ILO). Some of the relevant national government programmes with donor support include: (i) Programme for Accelerating Development in Disadvantaged Regions (*P2DTK*); (ii) Development Programme in Integrated Production (*P2KPT*); (iii) Village Self Help Food Reliance Programme (*Desa Mandiri Pangan* or *DEMAPAN*); (iv) Village Agribusiness Development Programme (*PUAP*); (v) Cacao Development Programme (*GERNAS Kakao*); (vi) National Programme for Empowering Coastal Communities; (vii) Water Supply and Sanitation for Low Income Communities (WSSLIC). Key File Table 3 provides additional information.

## **C. Project Rationale and Objectives**

### **Project Rationale**

111. There is a strong rationale for IFAD to help the government to finance SOLID. First, the government requested IFAD to take a broad approach to address the major constraints and opportunities of the smallholder farmers in the project area, which have been neglected in the past decades. The design reflects the above based on a social assessment of the livelihoods of the smallholder agricultural producers in the two provinces and considering the post-conflict status. The project will target rural sub-districts in the provinces of Maluku and North Maluku with higher than average levels of poverty and/or large numbers of poor people. By focussing on improving the livelihoods of the poorer sections of these rural communities, the project can contribute to the achievement of the Government's poverty reduction objectives in line with the IFAD COSOP 2009-2013, while simultaneously improving the low returns from agricultural production (food and estate crops). Such an approach will improve the competitiveness of smallholder agriculture and growth of the agricultural sector. The design is in line with the IFAD focus on smallholder agricultural development, to address the main constraints of the smallholders, e.g. their capacity, access to technology, inputs, natural resources, capital and markets and restoration of key community infrastructure. Such an approach will improve the competitiveness of smallholder agriculture and growth of the agricultural sector. The proposed investments should lead to higher farm incomes and improved household food security, which are sustainable.

112. Secondly, for this approach to be successful, the project will need to address key marketing, production, natural resource management and infrastructure constraints that have prevented the growth in the productivity of food and estate crops in the target areas over the last decade. To benefit the poor, such an approach will require a focus on: (i) improving the access to productive assets, appropriate technology and production support services for on-farm productivity improvement; (ii)

value chain development, including building market links with the private sector, post harvest management, agro-processing and supporting small rural enterprises; (iii) providing access to, and improved management of, natural resources; (v) improving productive small-scale rural infrastructure at the village level e.g. to improve access to the crop production areas, micro-scale irrigation and rehabilitation of previously cultivated areas; and (vi) establishing group revolving funds to help build up the members' financial assets for investment or emergency purposes and subsequently help link these groups to micro-finance institutions (MFIs) and formal banking sector institutions identified in Annex VI Key File Table 2.

113. Thirdly, adopting a community empowerment and participatory development approach, that provides assistance to village and community organisations over a period of several years, can help ensure the sustainability of the improvements in the livelihoods of the smallholders in the targeted villages initiated with project assistance. Targeting the poorer sections of the rural population, mostly indigenous people, will enable the rural poor (women and men) and other marginalised groups, to make their own decisions in managing their resources, establishing their development priorities and negotiating services from various sources.

114. To succeed, such an approach will also require project assistance to improve the capacity of the public sector agricultural service providers, the use of NGOs and private sector service providers and take into account opportunities for partnerships and synergies with other rural development initiatives. Service delivery will need a village level focus, including the use of temporary village change agents and embedding agricultural extension expertise and animal health services into the village organisations.

### **Project Design Framework**

115. Three principles underlie the proposed design of the SOLID project, i.e. participation, empowerment and the efficient use of local resources and services. These principles are necessary for improving food security and reducing the incidence of rural poverty amongst the population in the targeted villages. By empowering local communities and improving their livelihoods, project activities can help prevent future community conflicts.

116. Other key elements of the proposed design for the SOLID project are as follows:

- The proposed activities will contribute to implementing the priorities of the local governments for agricultural and rural development and rural poverty reduction. As a result, the project will target the poor including the indigenous people and other marginalised groups.
- The project's focus on smallholder agricultural development will contribute to enhancing the competitiveness of smallholders, growth of the rural economy and addressing the key determinants of rural poverty.
- The value chain analysis has identified two commodities which should provide the basis of the project's initial agricultural and value chain interventions, subject to the results from surveys at project start-up, namely cacao and nutmeg/mace. The rationale for their selection is based on the following criteria: (i) ecological suitability, as demonstrated by the large areas of these two crops that have been under cultivation in both provinces for many years; (ii) familiarity of the local communities with both crops; (iii) availability of markets: the Maluku islands are already a major source for the nutmeg and mace traded internationally and there are opportunities to improve the quality and returns, while there are good markets opportunities internationally for high quality cacao (e.g. using low levels of external inputs); (iii) potential profitability with improved quality from better post harvest handling and some increases in yields; and (iv) the need to use few additional purchased inputs to improve the yields. During implementation other commodities may be identified using the same criteria for providing support for agricultural and value chain development (Working Papers 2 and 3 provide further information). Other possible commodities include copra, cashew and fish and marine products. In the meantime SOLID will also assist farmers to improve the productivity of farmers' food crop production e.g. upland rice, cassava, maize and groundnuts, which meet the above criteria.
- The project will complement and supplement the government's other priority programmes.

Annex VI Key File Table 3 includes details of the relevant projects and programmes.

- Project investments will focus on: (i) improving the skills and empowering local communities, farmers' groups and their organisations; (ii) diversifying the sources of household food supply and adding value to food crops through local processing and marketing; (iii) improving post harvest handling, including local processing of crop and fishery/marine products; (iv) facilitating links between producers and markets; (v) providing small-scale rural infrastructure to improve agricultural productivity with community participation; and (vi) strengthening the coordination and management of project implementation at the national and regional levels.
- The project will be a central government project with the AFS of MOA as the Lead Implementing Agency. However, two factors are important in determining the role of AFS in the provinces and districts. First, at the provincial and district levels, the implementation arrangements will vary because the AFS is not always present as a separate entity and the institutional structure at sub-national level varies from place to place. In addition, while food crops are an important part of the farming systems in the target districts, estate crops are the dominant land use. Therefore, achieving improved productivity and value addition for these crops will be an important element of any approach that seeks to improve the livelihoods of the poor and so help reduce the incidence of rural poverty. The project implementation arrangements will ensure that the technical inputs required from these other departments (e.g. estate crops) can be provided and coordinated by the AFS.
- The project design will take into account the lessons learned from PIDRA and from other Indonesian models and will replicate the successful approaches, modified where necessary.
- The project design also takes into account: (i) the low capacity of the provincial, district, and sub-district staff and village authorities and provide appropriate assistance to develop their capacity to support livelihood improvement among the target communities; and (ii) the *Adat* land systems and culture of the target communities.

### **Project Goal and Development Objective**

117. The objective of the project is to improved the livelihoods (incomes and food security) and reduce and the incidence of poverty for people in the targeted villages in the two provinces.

118. The outcomes are: (i) village institutions and self-help groups and unions functioning effectively; (ii) target group farmers use improved, sustainable production systems and low levels of purchased inputs; (iii) target communities using improved natural resource management systems; (iv) self-help groups and unions/federations operating as successful elements of the value chains for the targeted commodities; (v) improved small-scale infrastructure available in the target villages with the community organisations undertaking their operation and/or maintenance; and (vi) project completion on time and within agreed budget.

119. Annex 2 is the project's logical framework, including verifiable indicators, means of verification and assumptions and risks at the objective, outcome and output levels.

### **D. Project Components, Outputs and Activities**

120. On the basis of the priorities identified by the potential members of the target group during the Social Assessment, by the provincial and district governments and by the villagers during the Design Mission's field work, the project will have the following components: (i) Community Empowerment; (ii) Productivity Improvement and Integrated Farming Systems; (iii) Value Chain Development and Marketing; and (iv) Productive Rural Infrastructure Investment; and (v) Institutional Strengthening and Project Management. Capacity building and gender mainstreaming will be integral parts of all activities.

#### **Component A: Community Empowerment**

121. The output of this component is that communities are mobilised and Self-help Groups (SHGs) and Federations established.



122. The project will adopt a Sustainable Village Development Approach which will include the following elements: establishing and capacity building of the smallholders' institutions (SHGs and Federations), mainstreaming the use of local social capital, improving smallholder competitiveness and farming systems, value chain management, and environmentally sound resource management.

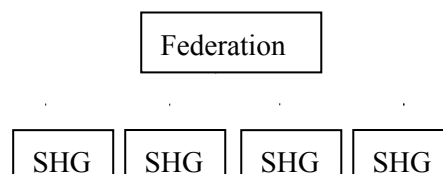
### Integration with the Customary Village Structure

123. In Maluku, there is a scope for integrating the SHGs and Federations into the customary village structure as follows. The members of a SHG should come from the same sub-cultural group (clan or *Soa*) to enable the group to use their membership of a *Soa* to strengthen the group e.g. members would have access to the same communal lands, and have a similar socio-cultural background. The Federation will also benefit from the use of this customary structure since it will be formed by the SHGs within a customary village. This would allow the federation to use the customary village structure such as *Kewang*, *Saniri*, and *Raja*; and, as well as, the formal village structure to support its activities. In Maluku, the customary village organisation structure is integrated into the formal village government structure where the village head is also the *Raja*. This integration should enable the smallholder organisations to effectively use local social capital for the benefits of the smallholders and, as well as, the project outputs and outcomes.

### Self-help Groups

124. The project will support the smallholders in each target village to organise and develop effective SHGs. The SHGs will consist of women and men from the target group involved in on-farm and/or off-farm income generation, while existing groups can become SHGs. The type of the group to be formed by SOLID should be men-group, women-group and mixed-group. However the portion should be in balance, for example, there will be 10 groups formed in every village during three year, so the portion should be formed 4 Men-SHGs, 4 Women-SHGs and 2 Mixed-SHGs. SHGs will start as savings and credit groups, providing a social safety net that reduces members' vulnerability, while also providing opportunities to use savings and loans for productive purposes. Each SHG will have up to 15 members with about 10 new or existing groups belonging to a federation in each village. The group may engage collectively in a productive enterprise or operate individually according to their interest. Project support will include technical and financial assistances. To be effective the SHGs and Federations should generate economic benefits for the members; and have one or more bonding factors (e.g. common goals, socio-economic and cultural assets) to motivate strong group affinity, and participation.

125. The experience of PIDRA approach should be useful in this regard, i.e. Federations were established in year 3 when the SHGs were assessed as mature groups. The PIDRA SHGs sent 2 – 3 of their members as the group representatives on the board of the Federations and also all member groups became members of the Federations. Women representation on the board of the Federations should be 1/3 of the federation members. The federations will have additional members every year from additional SOLID villages when they groups are formed every year during 2011 to 2015. The federation will act as a coordinator of SHGs in improving income generating activities as well as in developing village infrastructure development. The group representatives have responsibilities in providing information to others and facilitate the SHGs members on Federation meetings when the SHG hold their monthly periodic meetings. The structure of Solid beneficiaries would be:



126. SHGs are expected to pursue vertical and horizontal integration in the value chain to gain increased production efficiency and profits. With vertical integration the producers will take on additional activities in the value chain such as processing, grading and packaging, while with horizontal integration the producer organisations will become involved in chain management e.g. buying and selling in bulk to reduce costs and increase returns.

127. Indicators of the maturity of the SHGs are the following: direct election of leaders; a written statute (including roles/responsibilities of leaders and members); criteria for membership and regular financial contributions from members; enforcement of regulations and sanctions; regular group meetings and attendance; accurate recording of the minutes of meetings; written activity plan; regular participatory group self-assessments; maintenance of up to date and accurate records and account books; increase in income and/or income sources of group members; increase in group funds; and membership of the group in a network/apex organisation (Federation).

### **Federations**

128. The influence of SHGs will be expanded, to improve their chances of sustainability, by supporting the formation of a larger group or Federation within a village. These Federations will be capable of linking the growers directly with the vendors to achieve economies of scale through bulk production and sale. Further economies of scale can be expected: (i) when buying inputs and equipment for production and new value adding activities such as post harvest handling and processing; (iii) in coordinating training; and (iv) providing and opportunity for poor people to influence policies and to constitute effective pressure groups. Each target village will have a Federation of SHGs with written bylaws outlining their vision and governance (which should be consistent with project principles and support the project goals). The project will help the Federations become strong producer organisations either by supporting them when they are formed by the SHGs or strengthen them managerially and financially, when the SHGs join an existing *Gapoktan*. The *Gapoktan* is a village federation of farmer groups (one per village) in villages supported by MOA under the ongoing national programme for agribusiness development (*PUAP*). *PUAP* provides each *Gapoktan* with seed capital of USD 10,000. The aim is for Federations to become strong producers' organisations for particular commodities, to increase the smallholders' bargaining power as sellers and to have direct links with buyers<sup>17</sup>.

129. The new Federations (and the *Gapoktans*)<sup>18</sup> will play a key role in coordinating the value chain activities, including: providing links with other players in the value chains, and support institutions such as KADIN, sub-national level, research institutions and other relevant government agencies.

130. The village Federations will also have the following responsibilities: (i) to act as the fund management unit for the village and to receive and manage village grants provided by the SOLID project; (ii) to facilitate access of the SHGs to information, improved technologies, and extension, marketing and other services; (iii) to coordinate closely with the customary village (*Negri*) structure, the formal leadership the *BPD*, the *LPM* in villages where there customary structure does not exist in planning and implementing of project activities and other projects/programmes in the village to maximise synergy and learning and avoid duplication. Each Federation will have a President, Secretary, Treasurer/ Bookkeeper, two Commercial Village Officers (CVOs)<sup>19</sup>, and a Farmer Facilitator<sup>20</sup>, all elected by the membership of all the SHGs.

131. Indicative indicators to monitor the maturity of the Federations supported by SOLID are: written statutes; direct election of leaders, legal status; effective organisation and governance structure; regulation enforcement and sanctions; sound business plan; cost-effective provision of appropriate services to the members; financial viability; proper bookkeeping and reporting; and regular savings and/or timely loan repayments by members (if applicable); effective supervision; and links with private sector enterprises and government programmes.

### **Livelihood Improvement**

132. To improve their livelihoods, the smallholders will most likely opt to increase one of their traditional activities locally by using the project's assistance (finance and expanded marketing links) before opting to add value and take up new activities which require access to markets far away and involves a higher level of risk. At present the smallholders usually finance their activities using high cost loans, which reduces their income and strengthens their dependency on those who not only

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<sup>17</sup> The *PUAP* target villages may in some cases include those that SOLID will target as both projects use the incidence of poverty at village level for targeting.

<sup>18</sup> Referred to hereafter as Federations.

<sup>19</sup> Component D has further details.

<sup>20</sup> Component B has further details.

provide the finance but also buy their products at lower than market prices.

133. The project will provide SHGs with funds to establish their own revolving funds and provide the Federations with funds for investment in value chain development and marketing (Component D). Experience elsewhere in Indonesia <sup>21</sup>indicates that there is a scope to promote a sound community based microfinance institutions at village level. SOLID will assist the successful Federations to become sustainable and registered community based microfinance institutions during the second half of the project period and to make use of the management expertise of the most successful SHGs.

### **Support**

134. Support forums are also necessary at selected sub-district, district/island, and provincial levels. The forums will assist the smallholders and their organisations to attain a better access to technical and financial services, to develop supportive business environment, and to gain larger share of the end market price through vertical and horizontal linkages along the value chains. The forums should involve representatives of smallholders, private sector players, and relevant governments.

### **Implementation**

135. Implementation will start with an assessment of the IP situation in each target village, including their economic and social situation, existing grassroots organisations to identify issues and options and inform the process of capacity development process. The SOLID project will schedule a four year project to build the capacity of the SHGs and Federations. This project will include supervision and monitoring, capacity building for the membership, officials and FFs. These services will be provided by the NGO facilitators and specialist service providers as necessary. At the beginning the members of the SHGs will start saving a fixed amount (to be decided by the group) every month to ensure a small capital base for future economic activities and to provide for emergencies. After six months, groups can start making small loans from their Group Revolving Funds (GRFs) to members with interest for income generating purposes, with the terms and conditions decided by the group. On attaining a certain threshold, the groups will be eligible to receive a first matching grant from the project to expand their lending activities with a second tranche to follow when the groups are assessed as having met criteria that demonstrates their increasing maturity. All funds will be owned and managed by the members of the groups.

136. The contracted NGOs (one in each province) will assist in the process of group formation, provide intensive orientation training and facilitate participatory discussions to arrive at a selection of livelihood improvement activities using the procedures developed by PIDRA. The NGO Village Facilitators will assist in participatory village planning and the preparation of annual village plans and activity proposals for funding under the project. The NGO will also support the strengthening of the groups, monitor progress, and provide the leadership training required and group and fund management. Other service providers, e.g. private sector entrepreneurs or other specialists will also be contracted as needed.

137. The project will establish and support an estimated 10 groups per village in 330 villages each with a membership from about 15 households (total of 49,500 households). Each village Federation will be formed by the groups in a village.

### **Component B: Productivity Improvement and Integrated Farming Systems**

138. The output of this component is that the extension services are improved to facilitate increased agricultural productivity by smallholders.

### **Menu of Options**

139. The project will offer smallholders a menu of options is indicative based on the assessment of local farming systems and will be subject to on market research and a facilitated decision-making process to aid the selection of what crops to take and assessment of sound enterprise opportunities. The focus will be on productivity and quality improvement in the production of agriculture and livestock products in which the provinces enjoy a natural comparative advantage. Within these sectors, there

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<sup>21</sup> Including BKD in Central Java, LPD in Bali, and Bumdes LKM in NTB.

are many opportunities for productivity enhancement, value-adding, quality improvement and better commercial integration. Working Paper 2 provides further details while Component D covers the marketing aspects. The following are examples identified during project design, but these are examples and not intended to exclude other possibilities<sup>22</sup>:

- Increasing cocoa production from an average of 240-350 kg/ha towards a target of 1,000 kg/ha, while improving quality, through improved management techniques, including: (i) regeneration through grafting of new varieties and clones; and (ii) implementing integrated crop management (ICM) and integrated pest management (IPM) practices to reduce pest and disease incidence (e.g. cocoa pod borer) and ensure healthy growth of new grafted materials; techniques include proper pruning to achieve a tree height of 3.5-4 m with good aeration, sanitation, fertilizer use, frequent and regular harvests, biological control using black ants, pod sleeving and insecticide use.
- Increasing nutmeg production from an average of under 0.5 t/ha in Maluku towards a potential of at least 1.1 t/ha over time by: (i) adopting improved varieties introduced by the Estate Crops agency; (ii) pilot marketing for faster propagation of female nutmeg trees; (iii) adopting IPM practices for control of fungal infections associated with young fruit drop and damage by stem borer (*Hana batocera*); and (iv) pruning to increase flower, fruit and seed production;
- Increasing coconut yields from the mixed stands from an average of less than 1.0 t/ha towards 2.0 t/ha over time through improved management of the low input systems practiced and with 100 trees per ha by: (i) promoting the planting of disease free and good yielding local tall varieties (Tenga tall and Mapanget tall); (ii) enrichment planting of existing plantations to ensure optimum plant density; (iii) introducing weeding, leaf trimming and basic pest and disease control to reduce losses, as a phased replanting of areas where trees have become over mature; (iv) encouraging the use of improved roofed, pit smoking house, for copra production; (v) enabling group marketing of copra, through use of revolving funds, transport access and decoupling from credit provision in order to realise better prices for the product.
- Improving the productivity of annual food crops (rice, cassava etc.) within the farming systems by: (i) introducing improved varieties, including varietal testing, evaluation, selection and multiplication of seed by farmers, with a 20-30% production yield increase from the use of improved seed likely under conditions observed; (ii) diversifying the cropping with the introduction of groundnut varieties to improve nutrition and increasing ground cover to reduce erosion: intercropping of legumes with maize can increase the overall production per hectare 40-50% compared to mono-cropping; and (iii) improving IPM and ICM techniques: upland rice yields could increase from 1.0- 2.0 t/ha with effective control measures and the maize yield from 1.5 -3.0 t/ha.
- Improving production of vegetables for villages with access to urban markets by: (i) increasing labour productivity with the introduction of additional wells and manual (STP) or small diesel pumps, to replace current hand irrigation; and (ii) introducing improved rotational practices, soil productivity enhancement and use of IPM methods to reduce pest and disease problems.
- For livestock development there are opportunities to develop small semi-intensive units that make use of the resources available in the villages. Examples of these enterprises are semi-intensive chicken units of 20 birds for egg and meat production targeted at women, small pig fattening units (2 per unit) or goat rearing (2-3 per unit). Improved livestock production techniques include regular vaccination, regular de-worming, housing for better management including the provision of feed supplements and collection of manure, for poultry, ducks or pigs.

## Extension and Demonstrations

140. The government employed Field Extension Workers (*PPLs*) will provide the technical support required by the smallholders in the target villages wishing to adopt one or other of the menu of options and organise the necessary training and demonstration activities. The *PPLs* will be assisted by the Farmer Facilitators (*FFs*) and Animal Health Workers (*AHWs*). There will be one *FF* and one *AHW* in

<sup>22</sup> For example cashew nut tree replanting, simple processing to sell kernels rather than unshelled nuts and processing of cashew waste and cassava production.

each village.

141. The project will support the MOA's policy of designating one *PPL* per village and train them on relevant topics needed for providing crop and livestock extension services to the smallholders and the SHGs in the target villages. The number of extension workers in the target districts is lower than that required to implement this policy (Working Paper 5). Most often, one *PPL* covers 2-3 villages<sup>23</sup>. The use of volunteer Farmer Facilitators (FFs) and VHWs to assist the *PPLs* is an approach to address the lack of *PPLs*.

142. In each village one FF and one AHW selected from among the members of the SHGs, will receive training, act as demonstrators and will assist the *PPL* or *THL* in providing on the job training to the smallholders. The FF and AHW will act as the link between the SHGs and sources of public or private service provision after the end of the project. The FFs and AHWs will be trained to communicate the information through demonstrating best practices on their farms and during farm visits to other smallholders. Over time some of the demonstrations may evolve into nurseries supplying improved planting materials, or become seed production areas.

143. The responsibilities of the FFs and AHWs will include: (i) providing information and transferring technologies; (ii) linking the community with markets, other communities and service providers; (iii) mobilising the community for learning activities; (iv) assist with the training of the members of the SHGs and Federations, including the CVOs; and (v) implementing demonstrations of improved technology and husbandry practices on their own farms. In addition, the AHWs will provide vaccination services on a fee per service basis.

144. Farmer training will include integrated crop management practices that seek to reduce pest and disease incidence, improve regularity in production and increase the quality of the crop(s). Training will either be a demonstration-based training as used by MARS in South Sulawesi and Papua<sup>24</sup>, or use the farmer field schools approach for training at village level. In both cases, following training, selected participants will receive assistance to undertake demonstrations of the techniques learnt. The local governments agreed to ensure that there will be one extension worker per village (either *PPL* or *THL*) or in the case of villages that are close together one per 2-3 villages. The project will provide one motorcycle per target village for use by the facilitators and extension workers.

145. The project will finance the costs of farmer training, inputs for demonstrations, Technical Assistance (TA), training for the FFs and AHWs, transport and operating costs for the government extension workers. The smallholders will use the financial resources (from the GRFs) to help develop their agricultural enterprises.

### **Project's Strategy to Address the Constraint of Production Credit**

146. At present the smallholders usually finance their activities using high cost loans, which reduces their income and strengthens their dependency on those who not only provide the finance but also buy their products at lower than market prices. The project's strategy to address the constraint of production credit and help the various project-assisted organisations subsequently gain access to the financial services provided by the formal banking sector and MFIs includes the following:

- Lessons show that capacity building, training and savings mobilisation for lending within self-help groups is an important stepping-stone before groups and individuals can access credit from MFIs and the formal banking sector. Therefore, the project will focus on increasing the technical and financial capacity of potential microfinance clients, who will be members of the

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<sup>23</sup> There are also contracted extension workers (*THLs*), but they have not been assigned to specific villages and it is not sure whether their contracts will be extended after 2011.

<sup>24</sup> Since 2002, MARS Inc. has developed and refined a successful, farmer centred research and technology transfer approach for smallholder cacao farmers known as the Mars Cocoa Development Centre (MCDC). The MCDC brings together relevant global expertise to demonstrate the impact of improved germplasm, good agricultural practices and pest and disease management, economically feasible farm rehabilitation techniques and appropriate post-harvest technologies as well as linkages to regional and world cocoa markets. The MCDC site functions as a location for training and capacity building of relevant institutes involved in the cacao sector, as well as demonstrating the value of the interventions to farmers, government institutions and donors alike. The IFAD Review Mission in November 2009 found that the MCDC in Papua had achieved impressive results 14 months after its establishment from the training and demonstrations offered by the MCDC to the local farmers (see Assessment of Mars Cocoa Development Centre Extension Approach for Possible Adoption in Papua Province - IFAD Loan No. 755-ID and IFAD Grant No. 1053-ID).

group revolving fund programme to enable the project beneficiaries to exploit the technologies and training made available through the Project.

- On the demand side, the project will work to increase the number of credit worthy clients in rural areas by increasing productivity, improving market links, developing successful revolving fund operations and sensitizing borrowers to credit discipline, savings and effective credit use. When the SHGs and/or federations become credit worthy clients with stronger capacity and credit disciplines, the extension workers and NGO facilitators will assist establishing linkages between the SHGs and federations and MFIs and the formal banking sector to enable the SHGs and federations to obtain funds for investment over and above the level that their GRFs can provide. Subsequently, the MFIs can bring affordable and sustainable microfinance to poor households and groups for farm production and livelihood activities, including trade, processing and storage and marketing.

## **Climate Change**

147. Recent experience seems to indicate that the most likely impact of climate change will be an increased variability in rainfall with longer drought periods but also an increased intensity of rainfall at other times. The implications are that the project should assist in assessing the drought tolerance of varieties of annual crops e.g. upland rice, ground nuts, maize etc. to enable smallholders to mitigate the impact of drought and especially the impact on household food security. An increased reliance of estate crops is a strategy that could help reduce the impact of an increasing incidence of periods of drought, although this would make households less food secure (estate crops are cash crops). Estate crop yields and hence household incomes from estate crops would also be reduced to an extent. Finally, the introduction of conservation farming techniques (Component C) will help minimise the damaging impact of high intensity rainfall due to greatly increased soil erosion.

## **Component C: Value Chain Development and Marketing**

148. The output of this component is the availability of services to improve market returns by the SHGs and Federations.

## **Approach**

149. Prior to the start of any programme of support for a value chain the project will carry out surveys of demand both in the local markets and for export. The Addendum to Working Paper 3 provides some background on the opportunities for developing the value chains for cacao and nutmeg and mace in ways that will benefit poor rural producers while making the value chain more efficient.

150. To provide the detailed information required before supporting the development of a value chain, in a district the project will undertake two activities: (i) assess the local value chains at district level as there will be variations between the districts; and (ii) hold a workshop to agree with the proposed approach, involving representatives of the selected value chain(s) to be developed (smallholders and their institutions, and the private sector), along with representatives from the supporting institutions (regulators, legislators, and providers of technical assistance, and financial services).

## **Integration of Federations into the Value Chains**

151. The project will support the development of Federations and their integration in the value chains through the provision of financial (equity and/or working capital as a grant), technical and management support, based on sound business plans. Assistance could also come from other sources, e.g. government agencies, NGOs and the private sector. Further funding for processing and or marketing, if needed, could come from the banking sector which would require the Federation to be registered as a legal entity, or through contractual arrangements with the private sector. Financing for the individual smallholders could come as loans from the unions, their own GRFs, MFIs or the banking sector.

152. The aim is to integrate the Federations into the value chains and for them to gradually assume the tasks currently carried out by the village collectors and the district traders. Group (bulk) marketing and reducing the length of the value chain can increase the returns to the smallholders. Links will be developed between the Federations and key value chain participants to provide

incentives for farmers to adopt the interventions and produce higher (export) quality products, to grade produce and ensure good primary processing (drying and storage). An additional potential opportunity for cacao is exploring the possibility of linking with the fermented bean market and encouraging farmers to enter this higher value market chain.

153. Partnerships with larger traders may help solving the present problem of provision of appropriate financial services to the smallholder producers by decoupling sales from credit provision at the local level.

154. In addition, where appropriate SOLID will support the development of small scale processing industries to serve local market e.g. nutmeg pulp juice and some snacks, nutmeg powder, and essential oils. The current business environment in the provinces seems to be unable to support the development of large scale industries to serve the market. More importantly, such development needs resources which are beyond the scope of SOLID to provide.

### **Business Plans**

155. Business plan preparation will have four stages: (i) identification of potential opportunities; (ii) an assessment of possible business models for the identified activities; (iii) feasibility study for the selected business activities; and (iv) preparation of a business plan.

156. The first stage will involve group representatives with facilitation by the NGO Village Facilitator, while the Federation management, including the CVOs, with project assistance will be responsible for the remaining three stages. The business plan should be financially, technically, socially and environmentally feasible. The CVOs will provide a direct interface between the SHGs and Federation and the private sector through provision of information and direct contact with traders to help implement the business plan.

### **Financing Value Chain Investments**

157. The project will provide grants to the Federations over a four year period to finance their business plans with the size of the grant depending on the proposed investments. Preliminary assessments included in Working Paper 3 indicate investments in the range of USD 8,000 to USD 90,000. The Federations will submit their proposals to the District Project Implementation Office for approval and disbursement, which will follow agreed project procedures (Section V. D). Opportunities may exist for private sector investment on a cost sharing basis and the AFS will initiate investigations into the opportunities for such partnerships during project start-up.

### **Supporting Interventions**

158. The project will also support and facilitate value chain forums at district level (for value chains targeting district markets), and at provincial level (for a value chain targeting export markets). This support will include: (i) quarterly meetings of a value-chain co-ordination forum for each value-chain; (ii) participation in fairs in Makassar, Surabaya, and Jakarta by processing Federations; (iii) technical assistance comprising a short-term international value chain specialist and national expertise (see below); and (iv) exposure visits and capacity building for staff of government departments and *KADIN* etc.

159. Based on the assessment of value chain related expertise available locally, competent and experienced institutions such as UNIDO could be considered as partners for supporting the implementation of some value chain related activities, including value chain and market analysis and technical assistance support to the Federations. The AFS of MOA, *Bappenas* and MOF should explore ways to partner with UNIDO in this regard, subject to the agreed project procurement processes.

160. Finally, the project will find a Business Development Service Provider to establish a demonstration bio-diesel facility (no cost to the project), to show ways of reducing the current high cost of energy.

## Component D: Productive Rural Infrastructure

161. The output of this component is that small-scale rural infrastructure improved.

162. The project will finance investments in small-scale productive rural infrastructure through the provision of community grants<sup>25</sup>, in response to proposals submitted by the villages. There will be no fixed allocation of funds per village for infrastructure investment. At this stage, there is no fixed budget allocation of funds per village for infrastructure investment, because of the following considerations:

- All sub-projects for productive rural infrastructure will be subject to participatory planning process, eligibility criteria and a negative list.
- All sub-projects will be selected based on the principle that villages will negotiate, collaborate and contribute in labor or kind to infrastructure investment according to the government customary practice.
- The DPIO and Dina Public Works will screen village proposals for rural infrastructure sub-projects in order to avoid overlapping investments provided by other programmes, such as *PNPM-Mandiri* Rural and WSSLIC.

163. During Loan Negotiations, IFAD will discuss with the government on the allocation of a fixed amount of resources to villages under this component.

164. These investments in infrastructure will complement the project's support for agricultural productivity improvement and as well finance the costs associated with preparation of proposals, supervision of implementation and TA. Examples of possible investments include: upgrading access from village to the farmers' fields (estate or food crops), micro-irrigation schemes e.g. shallow wells for vegetable production, small crop drying and storage facilities and rehabilitation of previously cropped areas (clearing, water control structures etc.). Other sources of funds (e.g. *PNPM*, WSSLIC) are available to finance larger-scale rural infrastructure investments, e.g. domestic water supply schemes, village access roads, social infrastructure etc.

165. The following is a negative list of sub-projects that are not eligible for financing under SOLID:

- Large-scale infrastructure (such as big dam, primary and secondary irrigation canals, Ports or harbors, primary roads, and national, provincial and district roads as specified in Bina Marga Decree and other relevant government regulations).
- Construction of new roads or any change to existing road alignments (that will likely trigger safeguards issues).
- Zones marked for ecological protection and conservation such as peat swamp areas, areas of primary forest, length of coasts with coral reefs and notified protected areas.
- Sites identified (or classified) as potential Flooding and Landslide Sensitive Zones generally consisting of secondary forests, slopes greater than 40% and slopes greater than 15% with sensitive soils (backshore, river bank, lake and dam-side and around springs).
- Protected areas or particular areas that is likely to alter land-use or areas that are to be designated as protected zones.

166. The Federations in the target villages will prepare sub-project proposals and submit them to the district, through the District Project Implementation Office (DPIO). For sub-project investments to be eligible, the proposal must demonstrate that the sub-project: (i) is not on the above negative list; (ii) has been identified and budgeted using community participation procedures; (iii) includes the details of those who would oversee implementation and manage the proposed investments; (iv) shows the extent of the proposed community contributions (including community monitoring of the quality of civil works); and (v) details of: (a) any land required; (b) any environmental and social impact; (c) arrangements for O&M; (d) all irrigation development under the project will utilise gravity supplies or shallow wells and take such other steps as may be necessary to avoid adverse impact on groundwater levels; and (e) all rehabilitation of existing roads and upgrading of tracks will include an adequate number of cross drainage structures and the design thereof will be preceded by, and otherwise take account of, a review of local hydrology. As all these projects will use community participation procedures for implementation, the scale of individual projects will be small<sup>26</sup> and as a result will limit

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<sup>25</sup> To be categorised as civil works for rural infrastructure in the cost tables by category of expenditure.

<sup>26</sup> The government regulation for such community executed sub-projects is IDR 5.5 million per sub-project.



the scope for potential negative environmental impacts.

167. The project will give priority to investments that meet most of the following characteristics: can provide immediate benefits and benefit a high proportion of the village population; use simple and low cost technologies; are easy and simple to maintain; attract high levels of beneficiary contributions; and are relatively risk free.

168. The DPIO will review each proposal (both desk reviews and field verifications) before approval. If the DPIO's review indicates any anomaly, the sub-project proposal will be returned to the Federation for appropriate revision and resubmission. The MOA at the national level and the *Dinas* at the province and district levels are responsible for the above type of investments. Funds will flow from DPIO to the Federation following the agreed disbursement procedures included in the Project Implementation Manual (Annex IV).

169. The local communities will undertake civil works under the Component of Productive Rural Infrastructure through procurement involving community participation, when each of such contracts costs less than IDR 55 million equivalent, which is in line with the government procurement regulations for community participation in procurement of civil works. All such civil works executed by communities will be clearly defined in the approved procurement plan. The project will use the technical staff of the district Public Works and/or agricultural office to support the community in the design and supervision of infrastructure construction (from identification to implementation and handover, including arrangements for O&M). At the start of the project, the National Project Management Office (NPMO) will request the Ministry of Public Works to prepare an Infrastructure Investment Manual, including a menu of possible investments, procedures for fund disbursement, standard formats for monitoring and reporting etc. for implementing the infrastructure proposals submitted by the villages, which may be updated as required.

170. The mitigation measures to prevent programme abuse, favouritism or graft in the allocation of funds include:

- Enhanced disclosure provisions: (i) making publicly available all key documents, (ii) all bidders promptly of contract awards and bid evaluation summaries; (iii) allowing representatives of end-users of the goods or works being procured to attend the public bid openings; (iv) making available the details of all contracts awarded; and (v) making available the date of request for all contract payments and the date of each payment, with an explanation of the reason for any delays.
- Standardization of certain items e.g. (i) use of standard wording in advertisements; (ii) agreement on the list of newspapers of nation-wide circulation in which specific advertisements will be placed; (iii) use of standard bidding and contract documents and request for proposals (for consultancy service), with no further changes to be made without IFAD's prior approval; and (iv) publication of prices paid for items in different locations.
- Establishing a complaints handling mechanism (and the use of sanctions), whereby community members and the general public can channel complaints or inquiries e.g. through the use of mobile phone text messaging. Complaints and inquiries will be systematically recorded and answered. The project will also post complaints on the project's website so that case processing will be more transparent. Designated staff at the DPIOs, PPCOs, and NPMO will handle complaints and respond in a timely manner.

## **Component E: Institutional Strengthening and Project Management**

171. The output of this component is efficient project management and coordination.

172. This component will finance the costs of project management at national, provincial and district levels and support the development of the staff capacity of key participating agencies to provide the services required by the rural community in the target villages.

173. **National Level:** At national level, the project will have a NPMO in AFS with at least 15 staff working full time for the project, including a National Project Director; a Deputy; four officers for planning, M&E and reporting; two staff for financial management and book keeping; one staff for procurement and contract management; three technical staff (e.g. food crops, estate crops, value chains); and support staff (computer operators, translator, secretary, etc.).

174. IFAD will finance the costs of office furniture, equipment (computers, printers, projector, digital camera, accessories, etc.), transport (cars and motorcycles); staff training, including a training needs assessment and preparation of a Human Resource Development Plan in PY1; technical assistance; design and production of communication and information materials and dissemination activities; studies and workshops. In addition, IFAD will finance the costs associated with the existing NSC when the members are involved with SOLID Project-related activities and the costs of a SOLID Technical Working Committee, comprising representatives of the technical agencies involved in the project implementation. This committee will report to the National Steering Committee in MOA which oversees all IFAD projects in the Ministry.

175. The government will finance all staff costs (seconded and contract staff) and other recurrent costs (office operating costs, travel costs, vehicle O&M costs etc.).

176. **Provincial Level.** The Lead Coordinating Agencies will be: (i) the Provincial AFS in Maluku Province, and (ii) the *Dinas* Agriculture in North Maluku Province. These agencies will provide the overall supervision and implementation support for the project and will establish the Provincial Project Coordination Office (PPCO) and provide the staff needed from their existing staff to work for the project full time.

177. Each PPCO will have about 15 staff, headed by a Provincial Project Coordinator. The PPCOs will have the same types of professional expertise as the NPMO, while other technical expertise needed in project implementation will be contributed by the collaborating agencies in the province and by the TA (short and long-term consultants and NGOs). The PPCO staff will be trained in project management and technical topics to ensure that they can carry out their new responsibilities in an efficient and effective manner.

178. Each PPCO will be staffed with at least 15 staff to work full time for the project, including a Provincial Project Coordinator; a Deputy; four officers for planning, M&E and reporting; two staff for financial management and book keeping; one staff for procurement and contract management; three technical staff contributed by the collaborating agencies in the province (e.g. food crops, estate crops, value chains); and support staff (computer operators, translator, secretary, etc.).

179. IFAD will finance the costs of office rehabilitation/extension, office furniture, equipment (computers, printers, projector, digital camera, accessories, etc.), transport (cars and motorcycles), staff training (PPCO and AIAT staff); design and production of communication and information materials and dissemination activities; technical assistance and NGO costs, studies and workshops. As part of the project costs, the provincial governments will also provide support for parallel activities, including the operating costs for the PTEC, although these costs are not included in the project's detailed or summary costs tables.

180. The government will finance all staff costs (seconded and contract staff) and other recurrent costs (office operating costs, travel costs, vehicle O&M costs etc.).

181. **District Level.** The Lead Implementing Agency will be Agency for Food Security and Extension (AFSE) (Model 1) in five districts and *Dinas* Agriculture (Model 2) in six districts, based on their existing organisational structures. In each district, a District Project Implementation Office (DPIO) will be established by the District Lead Implementing Agency. This office will be responsible for the overall management and implementation of the project at the district, sub-district and village levels.

182. Each of the 11 DPIOs will have at least 15 staff to work full time for the project, to be selected from existing staff of the Lead Implementing Agency with expertise covering the same disciplines as at the provincial and national levels. The DPIO staff will be trained on project management (participatory planning and M&E, financial management, procurement, etc.) and technical topics to ensure that they can carry out their new responsibilities in an efficient and effective manner. Each DPIO will be staffed with a District Project Manager (DPM); a Deputy; four officers for planning, M&E and reporting; two staff for financial management and book keeping; one staff for procurement and contract management; three technical staff contributed by the collaborating agencies in the district (e.g. food crops, estate crops, value chains, infrastructure); and support staff (computer operators, translator, secretary, etc.).

183. IFAD will finance the costs of office rehabilitation/extension, office furniture, equipment

(computers, printers, projector, digital camera, accessories, etc.), transport (car and motorcycles), staff training (DPIO staff and DTEC members); technical assistance and NGO costs, design and production of communication and information materials and dissemination activities; studies and workshops. As part of the project costs, the district governments will also provide support for parallel activities including the operating costs for the District Technology and Extension Committee (DTEC), although these costs are not included in the project's detailed or summary costs tables.

184. The government will finance all staff costs (seconded and contract staff) and other recurrent costs (office operating costs, travel costs, vehicle O&M costs etc.).

185. **M&E.** The project will finance: (i) the conduct of annual participatory planning and preparation of the project Annual Work Plans and Budgets (AWBPs); (ii) design, preparation and distribution of project management manuals, financial and procurement management; (iii) all participatory M&E activities, the project's baseline studies (including village surveys and village database development), periodic household surveys, mid-term impact survey and mid-term review, and final impact survey and project completion review; (iv) preparation and printing of project reports (semi-annual, annual reports and Results and Impact Management System (RIMS) reports; and (v) management and coordination meetings, workshops and seminars.

### **Technical Assistance**

186. In view of the limited institutional capacity in the two provinces and 11 target districts, the project will finance the provision of the following project management and technical consultants and other service providers: (i) a short-term international expert on value-chain, marketing and agribusiness; (ii) a consultancy company to provide the following staff: one long-term national management adviser, two provincial management and technical advisers, 11 district community development and management advisers and short-term and long-term consultants, at national and provincial levels in key areas, e.g. value chain and enterprise development, gender, seeds, financial management, procurement, human resource development and training, communications etc.; (iii) consulting firm(s) to carry out a baseline survey, and the impact evaluation surveys (periodic longitudinal household surveys, Mid-Term and Project Completion); (iv) two NGO contracts, one for each province, to include a provincial supervisor, one district facilitator in each target district and village facilitators for each of the 330 target villages. The contracted NGOs will be required to hire and train local staff as part of its teams of village facilitators who understand local culture and social and economic issues in order to improve the delivery of quality services and support; and (v) short-term individual consultants at district level i.e. infrastructure design and development engineers and food security nutritionists. The NGOs and the consultancy companies will be recruited on performance-based contracts. Working Paper 6 lists the expertise required, the proposed duration of their assignments and Draft TOR. Additional specialist services may be required with the proposed TOR included in the Annual Work Plan and Budget (AWPB).

### **Policy Support**

187. IFAD support for policy analysis in the agricultural and rural development sector, including rural poverty, is being provided through the Rural Empowerment and Agricultural Development Programme (READ) in Central Sulawesi. READ is assisting the MOA Bureau of International Cooperation to undertake relevant policy studies and analyses and no additional assistance is necessary.

### **Project Support for Capacity Development**

188. The project will support the government's effort to improve the capacity of staff of the local government agencies. The activities to be financed include: (i) a training needs assessment (TNA) in key government agencies at the national, provincial and district levels, preparation of a HRD plan; (ii) training on project management for staff of the DPIOs, PPCOs, and NPMO; (iii) development of training curricula, guidelines, and training modules for training of trainers and staff training; (iv) relevant technical training of staff (including extension workers) in key government agencies involved in the project; (v) monitoring and evaluation of staff training; (vi) training contracts for non-government training centres/units; and (viii) operations cost for key training centres that will collaborate in the development of training curricula/modules and training of trainers and staff. The design recognizes that project assistance is required to improve the capacity of the public sector agricultural service

providers, the use of NGOs and private sector service providers and take into account opportunities for partnerships and synergies with other rural development initiatives. Specific measures to address the constraints of weak institutional capacity include:

- Providing resources to finance extensive training and capacity building programme for the farmers' groups and the project staff.
- Providing support from experienced NGO(s) in community development to ensure that the SHGs and federations can become sustainable organizations for both social and economic development.
- Providing extension services through village-based extension workers and farmer facilitators.
- Providing support to assist the SHGs and the federations to strengthen the capacity of the line agencies' provincial and district administrations to perform their respective support functions effectively.
- In recognizing the risks associated with institutional capacity, the project will adopt a more organized approach to capacity building, which is a major project investment than in the past. This approach includes first conducting a Training Needs Assessment covering SHGs and other community based organizations and the project staff involved with project activities as well as carrying out an assessment of the expected impact and effectiveness of the training provided. This will enable the project to better sequence capacity building activities to ensure it is appropriate and timely to support implementation of the project activities.
- In addition to strengthening the capacity of the line agencies' provincial and district administrations to mitigate the risk of under-performing institutions and improve the weak implementation capacity, the design includes such measures as, an extensive training and capacity building programme for the farmers' groups and the project staff; recruitment of NGOs to provide support to community organizations in community empowerment; providing extension services through village-based extension workers and farmer facilitators; and putting in place arrangements to improve coordination and management of the project implementation.

189. Project design and implementation arrangements are aligned with the Government's decentralization processes. The project will work with and strengthen the existing government institutions rather than creating parallel structures. The project will be a central government project with implementation responsibilities delegated to the provincial and district governments with the provinces providing a coordination and oversight role and district governments an implementation role. Rather than adding complexity, the project's institutional arrangements support the effective implementation of Government policy for revitalizing agriculture and improving the provision of service delivery at various institutional levels. Furthermore, in assisting government in implementing its decentralization policies, the project will also facilitate through partnership with other agencies, NGOs, the private sectors and other development partners to strengthen the capacity of provincial, district and sub-district institutions.

190. The variation of institutional arrangements at the province and district levels is necessary to ensure the project's organizational and management are appropriate and context specific rather than taking a generalized approach to project management arrangements.

191. The staff in the institutions responsible for the project implementation are not seconded to the project. They are part of the existing government system and institutions with a mandate for management and coordination of agricultural and rural development in their own regions.

192. Though there is not yet a separate division for Food Security in North Maluku, but the *Dinas* Agriculture in North Maluku has the mandate for food security as well as other mandates under the Ministry of Agriculture (MOA).

193. Both the division of Food Security in Maluku and the *Dinas* Agriculture in North Maluku are part of the MOA with a direct line of technical reporting and authorities delegated by the MOA for the project implementation, while all provincial technical agencies will report to the governors and the district-level agencies will report directly to the *Bupati* (District Mayor).

194. The Provincial Project Coordinating Office (PPCO) at the Food Security Agency in Maluku and at the *Dinas* Agricultural in North Maluku will be responsible for the management and

coordination of the project implementation at the provincial level, while a District Project Implementation Office (DPIO) within the district-level agencies will be responsible for the management and coordination of the project implementation at the district level.

195. One additional feature introduced to promote more effective management and coordination is that the project will introduce quarterly Project Coordination and Consolidation Meetings in which project staff and consultants from the 11 districts, the two provinces and national level will identify constraints and recommend improvements in operational arrangements, procedures and policies.

196. To support the development and integration of the village organisations into the value chains, the project design includes:

- Capacity building from extension workers, farmer facilitators and NGOs.
- Provision of technical support and training from the Field Extension Workers (*PPLs*), the Farmer Facilitators (FFs) and Animal Health Workers (AHWs).
- Provision of financial (equity and/or working capital as a grant), technical and management support, based on sound business plans.
- Assistance from other sources, e.g. government agencies, NGOs, through contractual arrangements with the private sector and the banking sector which would require the mature Federations to be registered as a legal entity.
- Support to group (bulk) marketing for them to gradually assume the tasks currently carried out by the village collectors and the district traders and reduce the length of the value chain can increase the returns to the smallholders.
- Developing links with key value chain participants to provide incentives for farmers to produce higher (export) quality products, to grade produce and ensure good primary processing (drying and storage).
- Linking with the fermented cocoa bean market and encouraging farmers to enter this higher value market chain.
- Development of small scale processing industries to serve local markets, e.g. nutmeg pulp juice and some snacks, nutmeg powder, and essential oils.

197. The NPMO will prepare a Manual and Guidelines for the TNA and the project can benefit from the experience of the Farmer Empowerment through Agricultural Technology and Information Project that carried out a similar TNA exercise in 2009, including the use of a TNA manual that was developed by the Indonesian Centre Agricultural Technology Assessment and Development (ICATAD).

198. The staff information collected through the TNA exercise will be used for preparing a five-year HRD Plan for the key agencies involved in the project. A training schedule will be prepared to include: (i) priority topics (project management, including all aspects of M&E, and technical aspects related to the project); and (ii) proposed participants, time frame, potential training service providers, funding sources, and procedures for the evaluation of the training provided.

199. The following staff will receive priority for training: (i) managers and other project staff; (ii) extension workers and members of extension teams at the district and sub-district levels including *PPLs*, NGO Facilitators, Federation officials and FFs; (iv) technical staff involved in the project; and (v) trainers. The NPMO will provide guidance and coordination for this activity at all levels.

#### **E. Alignment with Country Rural Development Policies and IFAD Strategies**

200. The project design is in alignment with the policies and priorities of the government for agricultural and rural development and rural poverty reduction included in the MTDP 2010 – 2014. In addition, the project will contribute to implementing the priorities of the local governments for agricultural and rural development and rural poverty reduction. The project will complement and supplement the government supported priority programmes e.g. *PNPM-Mandiri*, SPADA etc. in the same sector and/or in the same geographical area.

201. The project design is also entirely consistent with the IFAD COSOP for 2009-2013. The COSOP states that “*IFAD future assistance to Indonesia will focus on smallholder agricultural development for rural poverty reduction, to contribute to the enhancement of the competitiveness of*

*agricultural smallholders and producers, growth of rural economy and addressing the key determinants of rural poverty in local context, taking into account opportunities for partnerships and synergies”.*

202. The goal of the COSOP is to empower the rural women and man in the target areas of the IFAD operations to achieve enhanced food security and increased incomes by: (i) improving their access to productive assets, support services for on-farm and off-farm productivity improvement, infrastructure, markets and financial services; (ii) building up their social capital and bargaining power; and (iii) supporting the Government's efforts in pro-poor, evidence-based policy making.

203. The project's investments will improve the access of the target group of poor or very poor households to support services for farm and off-farm production, markets for these products and rural infrastructure, and therefore supports the COSOP's first Strategic Objective. Similarly the projects support for SHGs and their Unions, and value chain development will help build the up the social capital and increase the bargaining power of the target group households in line with the COSOP's second Strategic Objective. By contributing to these two Strategic Objectives, SOLID can help improve the livelihoods of the target group, 115,700 poor and very poor households, of whom 49,500 are expected to be direct beneficiaries.

204. SOLID's contribution to policy making (Strategic Objective 3) will come from the experiences gained from implementation e.g. lessons learned, best practices etc. which the project will feed into the country portfolio review process rather than from financing any specific policy studies (which the READ project is financing).

205. SOLID's investment in restructuring selected value chains, initially two, is innovative but has the potential for scaling up if the initial results are positive.

## **VI. IMPLEMENTATION AND INSTITUTIONAL ARRANGEMENTS**

### **A. Project Management and Oversight**

#### **Executing Agency and Oversight Committee**

206. With Government institutions at national and sub-national levels implementing the project, the institutional arrangements are of necessity complex due to the absence of uniformity in the structure of the government agencies at sub-national levels. Therefore, strong coordinating and reporting mechanisms, and a strong commitment by all concerned agencies will be necessary for a successful project implementation.

207. SOLID will be a “central government project”, with the AFS of the MOA as the Lead Project Agency<sup>27</sup>, delegating the responsibilities to the local governments for project implementation. The NPMO in AFS, headed by a National Project Coordinator, will manage the coordination and implementation of the project.

208. For policy guidance, advice and overall coordination, the SOLID Project will use the existing National Steering Committee (NSC) established for all IFAD-supported projects under the responsibility of MOA which was established by decree of the Minister of MOA in February 2008. The NSC is chaired by the Secretary General of MOA with a small Secretariat at the Bureau of International Cooperation in the Secretary General's Office. Membership includes representatives of the Ministry of Finance, *Bappenas*; the Ministry of Forestry; and other relevant agencies. The NSC provides advice and policy guidance to the IFAD-supported projects executed by MOA and provides feedback and recommendations on the progress of project implementation. If needed other agencies could join the committee for cross-cutting policy issues to complement the expertise of the membership. A SOLID Technical Committee with a membership from the same agencies as the Steering Committee will prepare technical and management documents for presentation to the NSC

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<sup>27</sup> The main concern of AFS is food supplies and security, food distribution and consumption hence, their focus is on food crop production and distribution. However, most farmers in the target areas rely on estate crops (cacao, coconut, nutmeg, cloves, etc.) for their incomes, while for some fisheries and forestry are also important. The AFS will need inputs from collaborating agencies e.g. *Dinas* Forestry and *Dinas* Marine Affairs and Fisheries and strong coordinating mechanisms for the DPIOs and PPCOs to access the expertise from these government agencies to support project activities at the district and village levels.

for their review and serve as a channel for technical and managerial assistance from the collaborating agencies to the NPMO.

209. During the project start up, consultations will be held with all stakeholders on how to improve synergies between the implementation of various project elements and activities and to strengthen the sustainability issues through addressing the key constraints to promote sustainable agricultural development.

### **Main Implementing Agencies and their Roles**

210. **National Level.** The NPMO in the AFS will provide overall supervision, implementation guidance and management support to the sub-national levels, including planning, financial management, procurement and M&E. The NPMO will prepare the consolidated documents combining provincial level documents with those for national level activities: AWPBs, semi-annual and annual Progress Reports, annual Financial Reports, M&E reports, including the Results Impact Management System (RIMS) reports, Withdrawal Applications (WAs), annual financial statements, audit reports and other reports/ documents needed by IFAD and the government.

211. The NPMO will organise the Training Needs Assessment and preparation of a Human Resources Development Plan in PY1, manage the bulk procurement, including the consultancy company, establish and supervise the M&E system, RIMS reporting, and evaluate the performance of the consultants and NGOs. Other tasks will be to ensure effective inter-agency coordination during project implementation, coordinate the IFAD implementation support and supervision missions, prepare and disseminate project media materials. Finally, the NPMO will provide information on policy issues identified at the various levels and share the successful experiences, strategies, and lessons learned from SOLID implementation through the Country Portfolio Review process.

212. Some qualified and experienced staff from the PIDRA National Programme Office in the AFS will be reassigned to work full time for the SOLID Project. AFS will ensure that project staff selected from the AFS staff will have qualification and experience that match their job description and will work full time for the project. Women professionals will be encouraged to apply for the project positions and, with equal qualifications, priority will be given to women professional staff. The staff will work full time for the project for at least four years to ensure stability of project implementation. The staff of the NPMO will be designated by a Ministerial (MOA) decree before the start of the project.

213. **Provincial Level.** In each province, a Provincial Project Coordinating Office (PPCO), headed by a Provincial Project Coordinator, will be established in the Provincial Lead Coordinating Agency (AFS in Maluku and Provincial Agriculture Services in North Maluku).

214. The responsibilities of the PPCOs are to: (i) consolidate the district annual work plan and budget (D-AWPB), prepare the provincial AWPB (P-AWPB), and submit P-AWPB to the AFS/NPMO in a timely manner; (ii) supervise, monitor and evaluate the district and provincial project activities and manage the M&E/RIMS; (iii) manage the recruitment of the NGO to undertake the community mobilisation/facilitation activities with assistance from the NPMO; (iv) consolidate the district reports and prepare the provincial semi-annual and annual progress reports for submission to the AFS/NPMO in a timely manner; (v) consolidate the district financial reports, records and accounts for provincial expenditures and prepare the quarterly financial reports for submission to the AFS/NPMO; (vi) prepare training curricula and manuals, organise TOT courses and train provincial and district staff on project management and technical topics; (vii) produce appropriate multi-media materials for extension workers and farmers in collaboration with the AIAT staff; (viii) establish linkages with research and training institutions and support the identified activities; (ix) assist in organising meetings of the PTEC and keep accurate records of the minutes of meetings; and (x) organise provincial *fora* (seminars, conference and workshops) for sharing of project experiences with participation from all the districts in the province.

215. The project staff will work on full time arrangement for the project for at least four years to ensure stability of project implementation. Staff will be selected from among those working for the Lead Coordinating Agency using a transparent selection process, with selection committees established by the lead coordinating agencies, from their current staff. Selected staff will have qualification and experience that would match their job description. Women professionals will be encouraged to apply for the project positions and, with equal qualifications, priority will be given to

women professional staff.

216. In each province, the existing Provincial Technical Committee of AIAT will be strengthened by integrating extension in its mandate to become the Provincial Technology and Extension Committee (PTEC) for SOLID with the members designated by a Governor's Decree. This committee will provide advice, recommendations, and feedback on the implementation of the project at the provincial level. The membership will be across sectors with representatives from public agencies (50%) and non-government institutions (50%), including private entrepreneurs, NGOs, *KADIN*, producers/farmers' organisations, civil society, etc. (about 30% women).

217. **District Level.** In each district, a DPIO, headed by a District Project Manager (DPM), will be established in the District Lead Implementing Agency<sup>28</sup>. As a multi-sector extension team already exists at the district level under the Agency of Agriculture Extension, the project will request them as team members in DTEC for the provision of project supported services and activities when needed. Therefore, the DPIO and DTEC will be responsible for overall project management at the district and sub-district levels and to: (i) select target villages based on the agreed phasing of villages and the selection criteria; (ii) manage all project activities implemented at the village, sub-district, and district levels; (iii) receive village plans and activity proposals from target villages and forward these to the DTEC for technical evaluation and approval/rejection for funding; (iv) consolidate approved proposals and include them in the district annual work plan and budget (D-AWPB) for submission to the PPCO; (v) ensure that the financial management is efficient, prepare quarterly financial reports for submission to the PPCO on a timely manner; (vi) procure the services of individual consultants required and ensure that procurement staff comply with IFAD procurement procedures and guidelines; (vii) operate the M&E/RIMS systems, and prepare semi-annual and annual progress reports for submission to the PPCO; (viii) ensure that technical guidance and implementation support are provided to all target villages; (ix) coordinate all the activities of the service providers; (x) organise the training of relevant in collaboration with the PPCO and carry out annual evaluation of staff; and (xi) assist in organising meetings of the DTEC and keep accurate records of the minutes of meetings.

218. Staff selection from those working for the lead agency will follow a transparent process. Women professionals will be encouraged to apply for the project positions and, with equal qualifications, priority will be given to women professional staff. The DPIO staff will work on full time basis for the Project for at least four years to ensure stability of project implementation. Staff will be designated through a *Bupati* decree before the start of the project.

219. **DTEC (District technical and Extension Committee).** In each district, the Lead Implementing Agency will establish a multi-sectoral DTEC (District technical and Extension Committee - *Bakorluh/Bapeluhs*) to provide policy advice and overall coordination during project implementation. The DTEC will be established through a decree of the *Bupati* before the start of the Project. The membership of the committee will consist of representatives from public agencies (50%) and non-government institutions (50%), including private entrepreneurs, NGOs, producer/farmer groups, civil society organisations, etc. (about 30% women). The DTEC will have extension staff with expertise in agriculture, livestock, forestry, fisheries, post-harvest and processing, natural resource management, etc. Staff from collaborating and other institutions may be invited to become members of DTEC, if such expertise is not available within the Lead Implementing Agency. The skills and knowledge of the DTEC members will be strengthened through training, etc. Guidelines and a manual for the DTEC operation will be prepared by the Project. The responsibility of the DTEC will be to: (i) receive and verify the technical feasibility of proposals from the target villages and recommend the qualifying proposals for funding; (ii) provide technical guidance to the FFs and CVOs; (iii) prepare training modules and train field extension workers, FFs, and CVOs; (iv) prepare appropriate communication materials, in collaboration with the PPCO, for distribution to community groups in the target villages; (v) periodically monitor and evaluate the project activities at the village level; and (vi) strengthen linkages of the DPIO with other technical staff in collaborating and other institutions in the district to enhance project implementation.

220. **Sub-district Level.** Project implementation at the sub-district level will be through the existing integrated Sub-District Extension Offices (*BPP*) consisting of extension staff with expertise and experience in agriculture, forestry, and fishery as technical and extension team when needed. The extension team in each sub-district will provide technical guidance and facilitation to the various

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<sup>28</sup> As noted earlier the lead agency will depend on the structure of the agricultural service provision in the district.



village/community groups in the target villages, based on their specific needs and will advise and facilitate the technical aspects of village planning and the preparation of village proposals for funding by the Project. They will ensure that these proposals are technically feasible and of good quality. Additional experts from other government agencies and from non-government agencies will be considered for membership in the *BPP* extension team if needed. The Project will provide technical and facilitation skills training for the *BPP* extension team members based on their specific needs and provide them with operational budget to travel to the target villages. In each target village, the *PPLs* will work closely with the village service providers such as the FFs, VCOs, and NGO village facilitators.

### Technical Partners in Implementation

221. The project will work with other government agencies, NGOs, universities, private sector and/or other development partners to strengthen the capacity of provincial, district and sub-district institutions and their staff for effective service delivery. The project will collaborate with government and donor-supported projects such as the Village Agribusiness Development Programme or *PUAP*, *PNPM-Mandiri* Rural and *PNPM-SPADA* and the UNIDO-ILO Maluku *Pelagandong* Project, etc. The MARS Inc. is identified as a potential partner for public and private partnership, which will help tackle cocoa pod borer through a Mars Cocoa Development Center in one of the two provinces. Knowledge exchanges and experience sharing will be conducted with other relevant programmes/projects/partners through annual performance review meetings and value chain support forums. Annual planning processes would also be coordinated with other relevant programmes/projects/partners operating in the same area or in the same sector, in order to ensure alignment and/or harmonization. In order to prevent overlaps of SOLID funding with that of other on-going programs in both provinces, the National Project Management Office (NPMO) and District Project Implementation Office (DPIO) of SOLID will maintain regular coordination and communication with *PUAP*, *WSSLIC*, *PNPM* and *SPADA* programs. The project will build on the lessons and experience learned from the government and donor-supported projects in productivity improvement, provision of services and capital to farmers' groups, linkage with markets, and use of standard designs, close supervision and operation and maintenance for the productive rural infrastructure investments.

222. **District Collaborating Agencies.** The key district agencies that will participate to provide technical support and guidance include: (i) *Dinas* Agriculture Services (if the Lead Agency is AFSE), (ii) *Dinas* Forestry, (iii) *Dinas* Marine and Fishery, (iv) *Dinas* Industry and Trade, (v) agencies under *Dinas* Agriculture responsible for seed certification, pest and disease control, and for land and water management, and (vi) the Community and Village Empowerment Boards for community development. All the district-level agencies report directly to the *Bupati* (District Mayor).

223. **Technical Assistance.** As already noted SOLID will require technical assistance from long and short-term consultants, and NGOs in a variety of disciplines. During PY1, the NPMO will recruit the technical and project management consultants and other specialists to support the DPIOs, PPCO, and NMPO through one national technical assistance support package. The two PPCOs will each recruit a qualified and experienced NGO to provide the facilitation and mobilisation services through national bidding process. Recruitment will be open to qualified national and provincial NGOs, who may sub-contract qualified and experienced NGOs at the provincial and/or district levels. The DPIOs will recruit the district based individual consultants. The recruitment of consultants and NGOs will follow the IFAD guidelines for procurement of services. At the end of each year, all consultants, NGO facilitators and the overall performance of the consulting firm and NGO will be evaluated as part of the annual project review. The annual evaluation and the actions taken on the recommendations will be part of the Project's Annual Progress Report. The project will benefit from the lessons learned by PIDRA from the evaluation of NGOs and NGO facilitators.

## B. Project Coordination

### Links with Complementary Projects

224. The SOLID Project will be harmonised with other ongoing projects and programmes to enhance its complementarity with other projects being implemented in the target locations. During the initial village assessment, the existing government and other programmes will be identified to

maximise synergy with the Project and avoid situations where duplication could occur.

225. An example of a project with which close coordination will be essential is *PUAP* which may be supporting *Gapoktans* in some target villages. Another example is the Rural *PNPM-Mandiri*, which supports community identified investments in rural infrastructure, mainly access roads, bridges, drinking water supply schemes and irrigation. However, *PNPM* tends not to finance minor or “light” rural infrastructure that targets agricultural productivity improvement e.g. access to crop production areas, micro irrigation improvements etc. that would be the focus of SOLID. Other projects where close coordination is necessary are: WSSLIC which finances drinking water supply and sanitation schemes in low income communities, the Village Self Help Food Reliance Programme (*DEMAPAN*); and the Cacao Development Programme (*GERNAS Kakao*).

226. **Provincial Collaborating Agencies.** The Project will access the services of specialists from the technical service agencies through collaborative activities to support project implementation. The collaborating agencies may include: (i) *Dinas* Agriculture where an AFS is the Lead Implementing Agency, (ii) *Dinas* Marine and Fisheries, (iii) *Dinas* Forestry, (iv) *Dinas* Public Works, (v) Provincial Extension Coordination Agency, and (vi) Assessment Institute for Agricultural Technology. The role of the collaborating agencies, especially *Dinas* Agriculture, and *Dinas* Forestry, is critical in project implementation.

227. **Research and Extension Linkages.** The links between research (AIATs) and extension (*Bakorluh/Bapeluh*s) need to be strengthened significantly to improve agricultural productivity. Currently, the AIAT in Maluku has designated one researcher as AIAT regional coordinator to carry out this task. The coordinator is responsible for identifying the constraints in the farming systems and identifying possible solutions. In collaboration with selected farmer co-operators and the field extension workers, they establish assessment trials and demonstration plots. One AIAT coordinator will be supported by the Project in each target district. The AIAT coordinator can represent research in the DTEC (District technical and Extension Committee) and can also represent the AIAT in the DTEC. The World Bank-assisted Farmer Empowerment through Technology and Information Project is following a similar approach in 18 provinces.

### Integration within the IFAD Country Programme

228. The IFAD portfolio has two agricultural and rural development projects, both of which are located in Eastern Indonesia and operating in environments similar to that in which the SOLID Project will operate, namely: (i) READ in Central Sulawesi; and (ii) National Programme for Community Empowerment (*PNPM*)-Strategic Plan for Human-Centred Village Development (Papua) or *RESPEK*-Agriculture in Papua and West Papua.

229. Implementation experiences and lessons learned from the IFAD country programme in Indonesia could help the SOLID Project implementers through the transfer of knowledge and sharing of successful experiences and approaches for possible replication and scaling-up during the implementation of the SOLID Project and *visa-versa*. The IFAD Country Portfolio Review Meetings will provide the forum for such exchanges.

## C. Monitoring and Evaluation

230. The NPMO will establish a Monitoring and Evaluation (M&E) system, satisfactory to IFAD, within six months of project effectiveness and manage the system during project implementation. The design will take into account the lessons learned from the M&E activities undertaken during the implementation of PIDRA. The M&E system will be connected and inter-linked at all levels and will consider the effects/impacts of project investments on all project beneficiaries and key stakeholders<sup>29</sup>.

231. The project's M&E activities will include the following: (i) participatory monitoring and evaluation (M&E) by the beneficiaries; (ii) routine reporting by the project to the government and IFAD; and (iii) surveys, impact evaluations and reviews.

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<sup>29</sup> Working Paper 6 contains details of the M&E arrangements.

## Participatory Monitoring and Evaluation

232. The beneficiaries will monitor all project activities and training. This activity has two key elements: (i) monthly meetings of the SHGs during the first two years of their participation in project implementation, and at least quarterly meetings thereafter; and (ii) preparation of quarterly reports including a physical progress and financial statement to be provided to the DPIO following an agreed project format, to be consistent with the government's reporting formats. The officers of the Federation will have responsibility for the periodic PM&E of village activities, assisted by the NGO Village Facilitator and the *PPL* assigned to the village. The *Federation* officers, NGO facilitators, and *PPLs* will receive training in participatory M&E methods and tools and will be provided with formats for data collection and reporting. Using the agreed PM&E formats, the *Federation* officers will collect information on the progress of activity implementation, problems met, and follow-up activity, if needed. The *Federations* will keep the activity progress reports and will discuss them during the monthly village meeting. The *Federations* will keep written minutes of village meetings including decisions and agreed follow-up actions. The monthly meetings will be held at a time when most of the members are able to participate, especially the women. At the completion of each village activity, the *Federations* will prepare an Activity Progress and Completion Reports, following the prescribed format, for submission to the DPIO, through the *PPL*. The National SOLID Project Office will prepare tools of self monitoring of groups performance. The members of SHGs were expected to discuss and agree on common answers to each indicator during their group discussion. The final chart will be displayed on the walls of the meeting hall. The extension worker/*PPL* and NGO Facilitator are responsible for collecting and consolidating such information. The officers of Federation will have responsible to consolidate periodic PME at village level.

## Project Reporting

233. **Government Reporting Requirements.** The government requires that all agencies implementing projects funded by the government or donors submit monthly and quarterly reports. These reports include project expenditure, by project component and category of expenditure, and include comparisons with the AWPB and appraisal targets. The financial and physical information will be reconciled and the data presented on an annual and cumulative basis. The PM&E formats reporting formats and the project databases will be synchronised with the government reporting formats to minimise the time needed to gather information and avoid duplication of effort.

234. **District Reporting.** Each DPIO will develop and maintain a district project database to include information about all project activities in the target villages in the district. Other project databases will be developed, such as a training database covering all the training carried out, topics, participants, schedule, evaluation, etc. The databases will be updated quarterly and the updated data submitted to the PPCO. The district PM&E Team will consolidate and analyse the village and district data when preparing their progress reports in compliance with the Government and IFAD reporting requirements. The DPIO will submit the progress reports to the PPCO, with copy to the NPMO, following the agreed reporting schedule.

235. **Provincial Reporting.** The provincial progress reports consist of consolidated data from the DPIOs plus reports of all provincial project activities. The collated data will be submitted by the PPCO to the NPMO who will maintain the master project database. The PPCO will prepare provincial progress reports that evaluate the progress of project components, identify any major issues and include all activities implemented by any collaborating agencies or other partner institutions. The reports will follow the agreed reporting formats in compliance with Government and IFAD the reporting requirements.

236. **National Reporting.** The NPMO will consolidate the provincial reports and include reports of national level activities, provide an overall assessment of the project and report to the government and IFAD in line with the agreed reporting formats and schedule. The NPMO will submit the six-monthly progress reports to IFAD by 31<sup>st</sup> September each year and the annual progress reports by 31<sup>st</sup> March of the following year. The reports will follow the prescribed formats (based on the PM&E system and consistent with formats of the monthly and quarterly reports required by the government) and will be analytical and evaluative. The data will include an analysis of the appropriate indicators from the logical framework, the RIMS indicators, the village database, and other household studies.

237. The project will prepare financial reports every three months (i.e. in line with the PIDRA

approach). The NPMO will prepare consolidated financial statements of the operations, resources and expenditures related to the project in respect of each Fiscal Year for submission to IFAD within three months of the year end.

238. The overall coordination and management of the PM&E system is the responsibility of the NPMO and the national PM&E Team, which will provide guidance to the provincial and district PM&E Teams to ensure that the PM&E functions effectively. The PM&E Officers from all levels will meet quarterly during the Project Coordination and Consolidation Meetings to report on the progress of their work, to identify constraints and possible solutions.

### **Baseline Survey, Impact Evaluations and Reviews**

239. The NPMO will carry out a baseline survey in PY1, with assistance from an external agency or contracted qualified consulting firm. A mid-term impact survey will be repeated during PY4 prior to the mid-term review (MTR), and a completion impact survey will be undertaken in PY7 before the project completion review (PCR). The study will include two selected villages in each of the 11 target districts. The 22 sample villages will be typical of the selected target villages. The baseline will include the indicators in the logframe in the following four areas: (i) socio-economic conditions; (ii) natural resource base and the environment; (iii) agriculture-related productive infrastructure; and (iv) village institutions.

240. Data from the baseline survey will also include all relevant RIMS indicators, including the anchor indicators, disaggregated by gender and ethnic groups. The results and methodology used in the baseline study will be important reference points for the mid-term impact survey in PY4 prior to the mid-term review (MTR), and the project completion impact survey in PY7 prior to the project completion review (PCR).

241. **Village Profiles and Database.** The outputs of the baseline survey will be village benchmark profiles. In addition to the baseline of 22 sample villages, the DPIO and NPMO will design, establish and maintain a database with information on all 330 target villages. The village database will be updated annually and expanded until it covers all 330 target villages. The project will learn lessons from the experiences of PIDRA in designing and maintaining village databases.

242. **Longitudinal Studies at the Household Level.** To help assess whether the SOLID Project has impact at the household level, the project will undertake (through contracting) periodic longitudinal household studies in PY3, PY5 and PY6 in addition to the baseline and impact studies. The sampling method would ensure that the principal target groups of the project including women-headed households, and marginal farmers are adequately represented in the samples. The topics and specific indicators to be used in the longitudinal household studies may include: (i) perception of groups (now and vision for the future) and role in groups; (ii) participation in meetings etc. and involvement of other household members in the group; (iii) group savings and loan activities; (iv) landholdings and land degradation; (v) changes in cropping pattern, crop production (food and tree crops), crop sales/incomes, own consumption, household food security; (vi) livestock owned, changes in livestock population, sales etc.; (vii) farm technology and changes in technologies used and whether promoted by the project; (viii) other sources of household income, changes in income following project interventions and changes in household assets; (ix) participation in village infrastructure improvement and economic development activities, reasons for involvement or non-involvement, and benefits obtained; and (x) beneficiaries' own (overall) assessment of the impact of the project.

243. **Annual Results, Impact and Monitoring Surveys.** The NPMO will prepare an annual RIMS report for IFAD using the agreed project indicators at output and outcome levels. The measurement of the impact level indicators, (pertaining to the MDGs) will form part of the baseline, mid-term and project completion impact surveys and be undertaken by the AFS/NPMO, as noted above.

244. Data from these three surveys will include the RIMS anchor indicators, disaggregated by gender and indigenous groups, and the project completion review will also include an assessment of the project's costs and benefits. Documented lessons learned, key policy recommendations, and success stories will be shared with stakeholders at all levels as part of the annual portfolio review process.

245. **Mid-term Review (MTR).** IFAD and the government will carry out a MTR in PY4. The MTR

will review the project's achievements, outputs, outcomes, impacts, and constraints in implementation. Based on the findings of the MTR, the implementation plans will be revised. The MTR will assess the following: (i) status of development and performance the project assisted groups, federations etc. (ii) project achievements outputs, outcomes, and initial impact, based on the mid-term impact survey; (iii) performance of NGO facilitators, *PPLs*, and other service providers, including the TA; (iv) performance of the NPMO, PPCO, and DPIO staff and national, provincial, and district government agencies and their staff; (v) changes in the gender relations and achievement of gender-related targets and level of participation of women; (vi) lessons learned from the project and its contribution to poverty reduction and development of agriculture in Maluku and North Maluku; and (vii) recommendations for further improvement and adjustments.

246. **Project Completion Review (PCR).** At the end of PY7 (upon completion of all investment activities), the AFS/NPMO, with assistance from a contracted consulting firm, will carry out a PCR. This review will record the final achievements of the project based on its objective, outcomes and outputs as compared with the project design. The PCR will document the findings from the final impact survey and lessons learned. The AFS and IFAD will agree the contents and format for the PCR Report. The NPMO will submit a draft report to the government and IFAD for discussion. The final PCR Report will reflect the discussions and comments and submitted to IFAD before the Closing Date of the Project.

#### **D. Planning, Budgeting**

247. Preparation of the project's AWPBs will follow a participatory approach involving the local communities and the central, provincial and district level agencies. The planning schedule will predate the Government's budget planning process, so that the project's budget is included in the national budget. The review process at district, province and national levels will ensure that the project's activities are synchronised with, and complement, other development activities. Annex 4 includes the Steps and Schedule in the Annual Budgeting Process.

248. A three-year Village Plan will be prepared in each target village using a participatory planning process led by the officers of the *Federation* with assistance from the Village Facilitator and the *PPL*. The highest priority activities in the plan will be translated into activity proposals for inclusion in the Village AWPB. The village plan will be updated annually. All village activity proposals will be submitted to the DPIO by the *Federation* officers. The DPIO will consolidate all the village activity proposals for review and technical verification, with those accepted recommended for funding by the Project.

249. The DPIO will submit the final activity proposals for review by the DTEC to ensure that the proposed project activities are synchronised with other projects/programmes. Final approval for funding will come from the Head of the District Lead Implementing Agency.

250. Each DPIO will consolidate all the recommended village proposals and will integrate them with the district-level project activity proposals into the District AWPB (D-AWPB) for submission to the PPCO with copy to the NPMO. The PPCO will consolidate all the D-AWPBs from the target districts in the province with the provincial-level project activity proposals and integrate them into the Provincial AWPB (P-AWPB). The PPCO will refer the draft P-AWPB to the PTEC for final review and synchronisation with other government and donor projects/programmes in the project areas to maximise synergy and reduce duplication. Then each PPCO will submit their P-AWPB to the NPMO.

251. The NPMO will consolidate the P-AWPBs from Maluku and North Maluku and integrate them with the national project activity proposals into the National/Project AWPB (N-AWPB). The NPMO will submit the draft N-AWPB to the National Technical Team/Committee for final evaluation and coordination with other government and donor projects/programmes. Then the NPMO will submit the N-AWPB to MOF for inclusion in the budget and to IFAD for review and comments. Working Paper 6 has further details.

### **VII. ARRANGEMENTS FOR FLOW OF FUNDS, FINANCIAL MANAGEMENT, AUDIT AND PROCUREMENT**

## **A. Flow of Funds and Disbursement Arrangements**

### **Flow of Funds**

252. The flow of fund for project financing will follow the Government budget payment mechanisms (*DIPA*). The project budget (IFAD Loan and Grant, and Central Government contributions) will be channelled from the MOF to each of the participating national, provincial and district project implementing agencies using the government budget transfer methods of either *Dekonsentrasi* (*Deconcentration*), or *Tugas Pembantuan* (Tasks for Assistance) to finance the project physical activities as well as non-physical activities (such as capacity building programmes or awareness campaigns), in accordance with the approved project AWPB.

253. In accordance with the approved project AWPBs, the project financing, which includes both government counterpart funds and the IFAD Financing will follow the following proposed flow of funds arrangements:

- (i) The respective Treasurers (*Bendahara*) of the Agency for Food Security of the MOA as the Project Lead Agency and each of the provincial implementing agencies in Maluku and North Maluku and each of the district implementing agencies in the 11 target districts will prepare Payment Orders (*Surat Perintah Membayar* - *SPM*) based on their respective project financing budgets.
- (ii) The Treasurer of the Agency for Food Security of the MOA and each of the provincial and district implementing agencies in Maluku and North Maluku will submit its *SPM* to the Treasury Offices (*KPPN*) of the responsible *KPPN Kanwil* (Regional Office) in their region.
- (iii) Based on the *SPMs*, the *KPPN* (Kanwil XI, Kanwil XXIX, Kanwil XXVIII)<sup>30</sup> will prepare *SP2D* (*Surat Perintah Pencairan Dana* - Disbursement Requests) in 3 copies. The first copy will be submitted to BO.1 (Bank Operational 1) to release payment to third parties/respective treasurer as stated in the *SP2D*. BO.1 is a GOI operational bank which flows the APBN funds to release payment.
- (iv) Upon Disbursement Requests (*Surat Perintah Pencairan Dana*) from each of the AFS of MOA and each of the provincial and district implementing agencies, Bank Operational 1 (BO.1) will disburse the required project funds either to vendors, suppliers or contractors in direct payment or replenishment to the respective Treasurers of the AFS of MOA and each of the provincial and district implementing agencies for payment of non-contract project expenditures.
- (v) The second copy of *SP2D* will be submitted to the DG Cash Management of MoF along with other supporting document. DGCM will then prepare a debit request to BI for replenishment to the BO.1. The third copy of *SP2D* will go to the treasurer of the implementing agencies and will be submitted to Executing Agency (Agency for Food Security of the MoA) along with copy of *SPM* and other supporting document for replenishment and reimbursement.
- (vi) Agency of Food Security of the MoA will then prepare an application for replenishment and reimbursement by submitting all required documents and applications to the DG of Cash Management MoF, which then will be submitted to IFAD along with the Withdrawal Application (WAs) for replenishment to the Special Account in Bank Indonesia.

254. The detailed flow of funds arrangements are provided in Annex IV and will be confirmed at Loan Negotiations and recorded in the Minutes of the Negotiations.

255. Once the annual budget (*DIPA/APBN*) is approved, the Directorate General of Treasury will assign the respective local *KPPN* offices for each of the implementing unit (AFS, provincial and district implementing agencies) for processing project expenditures. The APBN funds will flow from the Directorate General of Treasury to the Treasurers of the implementing agencies at the national,

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<sup>30</sup> Kanwil XI : *KPPN* Jakarta; Kanwil XXIX: Maluku (which covers *KPPN* Ambon, *KPPN* Tual, *KPPN* Saumlaki and *KPPN* Masohi); Kanwil XXVIII : North Maluku (which covers *KPPN* Ternate and *KPPN* Tobelo)

provincial and district levels, through Bank Operational 1 (BO.1). The funds will finance project activities and make payments to suppliers/contractors/consultants and other service providers, using standard Government procedures and forms for withdrawal of funds from *KPPN*. Approvals for payments from *KPPN* offices will be based on duly approved Disbursement Requests (*SP2D*) and contracts and Payment Orders (*SPMs*) will be sent to project offices for accounting purposes. Actual payments will be through the Bank Operational 1 (BO.1) in the region to the respective suppliers/contractors/consultants and other service providers' bank accounts or for replenishment of funds to the Treasurers of the each of the implementing unit (AFS, provincial and district implementing agencies) for non-contract project expenditures according to the approved AWPB.

256. Under the *Tugas Pembantuan* mechanism when a project is considered as a central government project, the use of a local government budget (*APBD*) to provide counterpart funds (*Dana Pendamping*) is forbidden. However, to show commitment by the participating local governments to supporting a central government project, it is expected that local governments will also use their local government budgets, i.e. *APBD I* (provinces) or *APBD II* (districts) as a support budget (*Dana Pendukung*) to support parallel activities through *Dana Pendukung* budget in the region. Examples of such expenditures are routine budget items for the operation of the provincial/district project management units and M&E activities and other agreed activities. The budgeting process and flow of funds for the *APBD* budgets usually starts later than for *APBN* funds and withdrawal of funds is through the respective regional development bank (*Bank Pembangunan Daerah* or *BPD*). It is recommended that these *Dana Pendukung* budgets be monitored and included in the periodic project progress reports.

257. The flow of funds to the farmer groups, e.g. Federations and SHGs will come from the *APBN* fund through the respective regional *KPPN* based on recommendation by or request from the district implementing agencies, using the current procedures for transferring funds to communities as for *PNPM-Mandiri* and other similar programmes. In short, the steps will be as follow: (i) the SHGs and Federations with the assistance of the village facilitators will prepare and submit proposals, in line with the AWPB, to the DPIOs for review and technical verification by the DTEC (District technical and Extension Committee); (ii) if acceptable, the SHGs and Federation with the DPIOs will sign an agreement on the activities to be financed; (iii) then the DPIO will request the nearest *KPPN* to transfer the funds directly to Federation's bank account; and (iv) *KPPN* will transfer the funds to the Federation's and SHGs' bank accounts.

## Accounts

258. A Designated Account (DA) also previously known as Special Account (SA) or *Rekening Khusus (RK)* for the IFAD Loan will be opened and maintained in a bank acceptable to IFAD (usually at the Bank Indonesia) in the currency of United States of America to assist the Borrower in financing eligible expenditures with one or several instalments made by IFAD to the DA, equal to approximately six month's worth of IFAD share of the eligible project expenditures in accordance with the approved AWPB. The DA will be replenished, as necessary, based on withdrawal applications submitted by the government to IFAD as project implementation progresses. Once the annual budget (*DIPA*) is approved or released, funds will be made available through the provincial and district State Treasury Service Offices (*KPPN*) of each of the implementing agencies at the national and regional levels.

259. A Grant Bank Account for the IFAD Grant will be opened and maintained in a bank acceptable to IFAD (usually at the Bank Indonesia) in the currency of United States of America to finance the agreed technical assistance to value chain development and other services under Component D, in accordance with the approval AWPBs. The disbursement of the IFAD Grant into the Grant Bank Account will follow the approval AWPBs.

260. A separate account for the project financing will be set up in the Bank Indonesia. The Treasurer of Implementing Agencies (National, Provincial and Districts) will receive the project *APBN* funds, through the agencies' account, from the Directorate General of Treasury of MOF to finance project activities and make payments to suppliers/contractors/consultants and other service providers, using standard Government procedures. These treasury office accounts will be maintained to adequately identify the project expenditures by component/sub-component, by expenditure category, by year and by source of financing. Payments will be based on duly approved payment requests and contracts, and payment vouchers will be sent to project offices for accounting purposes.

## Disbursement Methods

261. The project will use the following disbursement methods under the transaction based (traditional) disbursement procedure:

- **Reimbursement:** IFAD may reimburse the GOI for expenditures eligible for financing pursuant to the Financing Agreement (eligible expenditures) that the borrower has pre-financed from its own resources.
- **Advance:** IFAD may advance loan proceeds into a Designated Account (DA) operated by the GOI to finance eligible expenditures as they are incurred and for which supporting documents will be provided at a later date. Replenishment of the DA will be by way of withdrawal applications (WA) submitted regularly by the government. The NPMO will prepare the WAs, subject to approval of the MOF (Director General of the Treasury), for submission to IFAD. Annex 4 shows the simplified flow of funds and reimbursement procedures to be used.
- **Direct Payment:** IFAD may make payments at the borrower's request, directly to a third party e.g. supplier, contractor and consultant for eligible expenditures.
- **Special commitment:** This modality is used for eligible project expenditures related to items imported by project implementing agencies under a letter of credit requiring the issuance of guarantees for reimbursement to negotiating banks by IFAD.

## Initial Withdrawal upon Effective Date and Prior to Fulfilling Conditions Precedent to Withdrawals

262. It is proposed that the Financing Agreement should include a provision to allow the project to request an initial withdrawal amount of up to USD 500 000 from the Loan Account to cover the eventual start up cost (at the request of the Borrower), upon the Effective Date and prior to fulfilling the conditions precedent to withdrawals.

## B. Financial Management Arrangements

263. The NPMO, DPIOs and PPCOs will maintain all Project records and accounts adequate to identify the goods, works and services by source of financing. All Project accounts will be set up, operated, and reported using government accounting standards acceptable to the Financiers.

264. For efficient financial management, there will be: (i) designated staff responsible for government financial management and for reporting requirements at all levels and for IFAD's reporting requirements; (ii) the use of a standard software that is user friendly for preparing the government and IFAD financial reports; and (iii) provision of adequate training prior to the start of project implementation.

265. Given that most of the finance staff at the national and regional levels has limited experience with externally financed projects, the NPMO will hire qualified consultants to review the software capabilities at each of the implementing agencies at the national and regional levels. The consultant will recommend a suitable software and chart of accounts for the Project, which will be able to report on the different sources of funds and integrate with systems from various locations/sub implementation units/offices. The consultant will also recommend suitable contract management database to be used to capture the investment contracts at the national and regional levels, which will include clear identification for the source of funds. Staff training in using the identified software, chart of accounts, financial management and financial reporting will be undertaken regularly.

## Liquidation of Accounts and Reporting

266. All the accounts, including the Designated Account for the IFAD financing and Government Counterpart Funds and accounts of the local treasury offices will be established, managed, replenished, and liquidated in accordance with Loan and Grant Disbursement Handbook of IFAD and the financial regulations of the Government.

267. **Withdrawal Applications (WA).** The Borrower/Recipient should apply for replenishment of the DA on a quarterly basis or once the amount withdrawn reaches one third of the amount advanced, if this occurs sooner. The WAs should be submitted promptly once the monthly and quarterly statements from the bank in which the DA is held is received and reconciled. The replenishment



applications documenting the expenditures from the DA must be submitted regularly and any ineligible amounts must be promptly refunded to the DA or otherwise justified through the submission of evidence that other eligible expenditures have been financed from the Borrower/Recipient's own resources. The NPMO will prepare WAs for replenishment of the DA, subject to approval of the MOF (Director General of the Treasury), and then submit WAs to IFAD for review and reimbursement. Annex IV of the Main Report shows the reimbursement procedures to be used in the Project.

268. The Designated Account shall be replenished from time to time through Withdrawal Applications (WAs) through MOF to IFAD. Each WA for the replenishment of the Designated Account will have the minimum amount of USD 200 000. Each individual payment reimbursed or liquidated using the statement of expenditures procedures will not exceed USD 100,000 equivalent. Each WA will be supported by copies of supporting documents or Statement of Expenditures (SOEs) and Designated Account Reconciliation Statement.

269. For SOEs, the original supporting documents for each transaction should be kept respectively at the NPMO, DPIOs and PPCOs for fiduciary review and auditing purposes.

270. In the operation of the Designated Account for the IFAD financing and the Government Counterpart Funds and the accounts of the local treasury offices, the NPMO, DPIOs and PPCOs will:

- Make payment from their respective accounts for all eligible Project expenditures according to the approved Project AWPBs.
- Request the NPMO to transfer funds from the Designated Account to the accounts of each of the local treasury offices for agriculture related investment.
- Obtain and keep receipts for all Project expenditures.
- Prepare and maintain accounts and records of all Project expenditures, reflecting all Project expenditures by Project component/activity and disbursement categories.
- Consolidate and process, on a timely basis, records of eligible Project expenditures and withdrawal applications for submission through NPMO and MOF for forwarding to IFAD for reimbursement or replenishment of the Designated Account and the accounts of each of the local treasury offices.
- Record properly and keep in safe condition details of all transactions relating to the Project to be made available to the supervision missions, independent auditors and MOF for review and inspection at any time.

271. The project expenditures in Treasurers' accounts of the implementing agencies at the national, provincial and district levels will be reported monthly. At provincial level, the PPCOs will consolidate the financial reports from all DPIOs on a monthly basis prior to their submission to NPMO for consolidation at the national level. The NPMO will prepare consolidated monthly financial reports for the expenditures of all implementing agencies at the national and regional levels to include all project expenditures at the national and sub-national levels for submission to MOF monthly and quarterly to IFAD.

272. For reporting eligible expenditures paid from the designated account and requesting for reimbursement, the following Supporting Documents for Disbursement will be required:

- **Statements of Expenditures (SOEs)** will be accepted for eligible project expenditures less than USD 30,000 equivalent.
- **Full documentation** including records evidencing eligible expenditures (e.g. signed contract, invoices) are required for any expenditure exceeding the above limit.
- **Withdrawal applications for direct payments.** Purchase records evidencing eligible expenditures (such as copies of contracts, purchase orders, supplier's invoice and receipts, etc.) will be submitted together with withdrawal applications setting out clear payment instructions.
- **Withdrawal applications.** Based on the disbursement reports prepared and submitted by the Finance staff of each of NPMO, DPIOs and PPCOs, withdrawal application will be prepared and consolidated by the finance staff of NPMO and submitted to MOF for approval and signature before submission to IFAD.
- The **related documents** shall be retained by each Implementing Agency during the life of the Project and until at least the later of: (i) one (1) year after the Borrower/Recipient and IFAD

have received the audited financial statements covering the period during which the last withdrawal from the Loan and Grant Accounts was made; and (ii) two (2) years after the Closing Date. These documents will be made available for required audits, as well as to IFAD supervision missions upon request.

- Should the auditors or IFAD's supervision missions find that disbursements have been made that are not justified by the supporting documentation, or are ineligible, IFAD will have the right to withhold further advances to the DA. IFAD may exercise this right until the Borrower/Recipient has refunded the amount involved or (if IFAD agrees) has submitted evidence of other eligible expenditures that offset the ineligible amounts.

### **Control of Soft Expenditures**

273. The control of soft expenditures is related to how controls of fuel, training, per diems etc. should operate. The purpose is to ensure that all such expenses are properly authorized and that appropriate documentary evidence is available to support the expenditures. The controls related to soft expenditures shall include but not be limited to:

- Procedures and controls for Budgeting and Acquitting of Expenditures for Workshops. This will include, for example, selection criteria for participants, controls on attendance, controls against budgeted expenditures, and the Finance Section undertaking verification (including where applicable spot checks).
- Procedures for controls of fuel and vehicle log books.
- Maintenance and monitoring of Advance records.

### **Financial Reporting and Monitoring**

274. The quarterly Interim Financial Report (IFRs) will be prepared by each Implementing Agency using the cash basis of accounting. As the IFRs will be used as a monitoring tool, they will summarize the project progress and provide budget versus actual variance analysis; financial statements on sources and uses of funds; project financial position; expenditures and physical progress compared with plans; procurement and contract monitoring reports. Such reports will be prepared on a timely basis and to be submitted to IFAD by each Implementing Agency within 45 days after the end of each quarter starting from the first quarter after the first disbursement is made. They will not be subject to audit. The format of the IFRs will be agreed during the project start up.

275. Annual consolidated financial statements will be prepared individually by each Implementing Agency and consolidated by NPMO. The consolidated annual financial statements for the Project are subject to annual audit by an external auditor to be appointed by the NPMO.

### **Financial Management Supervision Plan**

276. The project will be aligned with risks based supervision for financial management arrangements. This will require an in-depth and intensive supervision in the initial years to ensure the successful implementation of the financial management arrangements. At least one on-site financial management visit either as part of the annual supervision mission or through a separate mission/consultant complemented by desk-based review of IFRs and audit reports will be done per year. The financial management risks will be reassessed and the supervision plan will be revised accordingly, after each supervision visit.

## **C. Audit**

### **Internal Audit**

277. Internal audits for government agencies are usually conducted at several levels, starting from the verifications of the goods/works/services received before payments are made, up to audits by the respective Inspectorate General of the Ministries for APBN expenditures, or by the Regional Inspectorate Office (*Inspektorat Daerah or Bawasda*) for all project expenditures.

### **External Audit**

278. The Financial and Development Supervisory Board (*Badan Pengawasan Keuangan dan*

*Pembangunan or BPKP*) is proposed as the independent external auditor for the project and should participate in the start-up workshops so that *BPKP* has a good understanding of the project's financial and procurement systems.

279. The audit will be performed in accordance with International Standards on Auditing complemented by terms of reference (TOR) acceptable to IFAD and in line with IFAD Guidelines on Project Audits. The financial statements will be prepared in accordance with the cash basis of accounting in accordance with International Public Sector Accounting Standards (IPSAS) published by the International Public Sector Accounting Board (IPSASB) that reflect receipts, payments (by disbursement category) and fund balance for the current reporting period and the cumulative period from the commencement of the Project. The annual audit will be carried out with greater emphasis on internal controls, according to the TOR acceptable to IFAD.

280. Terms of reference for the annual audits will be submitted by the NPMO for IFAD's review and concurrence on an annual basis. The TOR will require *BPKP* to produce an audit opinion on the project's consolidated annual financial statements. In addition, the auditor will provide a separate audit opinion covering the financial statements, statements of expenditures and on: (i) an opinion on the operations of the SOEs, the DA and the borrowers' counterpart fund; (ii) an opinion on the operations of the project expenditures in the treasury office accounts of each of the implementing agencies at the national and regional levels; (iii) an opinion on the compliance with the agreed procurement procedures; and (iv) a separate management letter addressing the adequacy of the project accounting and internal control system.

281. The Audit Management Letter should:

- Identifies deficiencies in project accounting records, financial management systems and procedures and internal controls.
- Makes appropriate recommendations for improvement.
- Includes any other significant matter that might have material impact on project implementation.

282. The NPMO will submit the reply to the management letter of the auditors to IFAD within one month of receipt of the report. The implementation status of the audit recommendations will be provided by each Implementing Agency in the separate section of quarterly IFRs to be submitted to MOF and IFAD within one month of the receipt of the audit report.

283. The audit reports are required to be submitted to IFAD within six months after the end of each fiscal year.

## **D. Procurement**

284. Procurement will maintain the principles of: (i) economy and efficiency; (ii) enabling all eligible bidders an opportunity to compete in the provision of goods, works and consulting services; (iii) highlighting the importance of fairness, integrity, transparency and good governance in the procurement process; and (iv) ensuring that competition is the basis for efficient public procurement.

285. Procurement of goods, works and services financed by the IFAD Financing shall be carried out in accordance with the provisions of the Borrower/Recipient's procurement regulations, to the extent such are consistent with the IFAD Procurement Guidelines (September 2010) and the Procurement Handbook of IFAD (September 2010). However, the government has proposed to follow the new national procurement regulation (*Perpres* No. 54/2010) for the project procurement. IFAD has identified a number of areas where the new *Perpres* No 54/2010 is not consistent with the IFAD Procurement Guidelines, which are detailed below. These specific items will be discussed with an agreement require prior to proceeding to the loan negotiations.

### **Initial Assessment of the National System for Public Procurement**

286. In August 2010, the Government of Indonesia issued a new procurement regulation (*Perpres* No. 54/2010) to replace the *Keppres* No. 80/2003 with the main objective of increasing the efficiency and effectiveness on the use of government funds by simplifying some of the procurement procedures. The appraisal mission reviewed the *Perpres* No. 54/2010 and noted the following main

changes; (i) in general the new guideline/regulation is clearer compared with the previous and similar guidelines; (ii) the clause on procurement which is partly or wholly financed by donors, in principle follows the *Perpres* No. 54/2010; where there are substantial differences, the procurement arrangements to be followed will be negotiated with the donors and stipulated in the financing agreements; (iii) more transparent with a requirement to announce the procurement plans and awards of contracts on websites and public notification boards; (iv) increased authority of the *PA/KPA* (Budget User/Proxy) to announce the tender winners; (v) in an institution/agency, there can be more than one *KPA* which will reduce complexity in the financial management; (vi) use of standard bidding documents (SBDs); (vii) the use of direct appointment for procurement of vehicles is allowed using the Government Service Operation; and (viii) ministry/institution/agency will implement e-Procurement partly or for all procurement starting in 2012.

287. Despite these positive changes, there are still restrictions that will limit competition, for example: (i) the short tender notification period which is only a minimum of seven days; (ii) foreign companies are allowed to participate for procurement of construction works, goods/other services, and consultant services only when the values are more than IDR 100 billion (USD 11 million), IDR 20 billion (USD 2.2 million) and IDR 10 billion (USD 1.1 million) respectively; (iii) a mandatory requirement that any foreign company has to cooperate with national companies; and (iv) the requirement to submit appeal/complaint guarantee amounting to 0.2% of the owner estimates with the maximum of IDR 50 million (USD 5,500) which will discourage bidders to submit appeal/complaints in case there are irregularities in the procurement process.

288. The initial findings of an assessment undertaken during appraisal of the new national system for public procurement, as provided in the government procurement regulations (*Perpres* No. 54/2010) proposed the following major exceptions from the government *Perpres* No. 54/2010, to order to be consistent with the IFAD Procurement Guidelines:

- For National Competitive Bidding (NCB) (General Tender), the minimum period for tender announcement will be 30 (thirty days) to allow time for more participants to bid, unless prior concurrence is obtained from IFAD.
- There will be no restriction on the participation of interested foreign companies in any bidding under the project. If foreign companies are awarded contracts, there will be no mandatory requirement that they have to cooperate with national companies. Foreign companies will be free to choose whether they want to cooperate with national companies or not.
- Shortlists for consultant services selection will be 3-6 firms with a wide geographic spread, i.e. no more than two firms from any one country and at least one company from a developing country, unless qualified firms from developing countries cannot be identified. IFAD may ask the Borrower to expand or reduce a short list. However, once IFAD has issued a “no objection” to a short list, the Borrower may not add or delete names without IFAD’s prior concurrence. The shortlist may comprise entirely national firms, if the ceiling of the assignment is less than USD 400,000 equivalent.

289. For procurement of motor vehicles which under *Perpres* No. 54/2010 can use the “Direct Appointment” method, IFAD must be satisfied that the Government Service Operations (GSO) prices offered by vehicle distributors are substantially cheaper than the market price. For this, the government will provide the official current and updated GSO and the publicly available market prices that are published for IFAD review for each procurement package for motor vehicles.

290. IFAD should review the arrangements for procurement of goods, works and consulting services proposed by the Borrower, including contract packaging, applicable procedures and the planning and scheduling of the procurement process to ensure their conformity with the above guidelines and the proposed implementation and disbursement schedule.

291. Working Paper 6 includes an initial review of the new government procurement regulation issued in August 2010 (Presidential Regulation/*Perpres* No 54/2010), in relation to the IFAD Procurement Guidelines (September 2010), an assessment of implementing agency’s procurement capacity and suggested procurement arrangements of major contracts.

292. **Conclusion of the initial assessment.** According to the IFAD Procurement Guidelines

(September 2010) and Handbook, before IFAD makes a final decision on if the project procurement should in the future follow the government *Perpres* No. 54/2010, it will require a more in-depth review of the new national system for public procurement, as provided in the government procurement guidelines (*Perpres* No. 54/2010), to assess whether the national procurement system and regulations are consistent with the procurement policies, principles and standards laid down in the IFAD Procurement Guidelines and Handbook.

### IFAD Financed Procurement of Goods, Works and Services

293. The IFAD financed procurement of goods, works and services will include the following:

- Goods. A total amount estimated at around USD 14.0 million), including *inter alia*: vehicles, equipment and materials.
- Works. A total amount estimated at around USD 8.314 million), including *inter alia*: civil works for office renovations in the provinces and districts and for the productive rural infrastructure.
- Services. A total amount estimated at around USD 20.02 million), including *inter alia*: Capacity Building, Studies and Workshops, International TA and National TA and NGO Services.
- In addition, IFAD will finance Matching Grants for the group revolving funds at about USD 7.86 million.

### Procurement Methods and Thresholds

294. **Goods.** Procurement of goods will follow the following procurement methods and thresholds, in accordance with the IFAD Procurement Guidelines and Handbook.

- Each contract for goods estimated to cost more than USD 100,000 equivalent shall be procured through the **International Competitive Bidding (ICB)** or Limited International Bidding (LIB) methods using IFAD's applicable Standard Bidding Documents (SBDs). Domestic preference will be allowed for eligible nationally manufactured goods.
- Each contract for goods estimated to cost less than USD 100,000 but more than USD20,000 equivalent may be procured through the **National Competitive Bidding (NCB)**.
- Each contract for goods estimated to cost less than USD 20,000 equivalent may be procured through **International or National Shopping method**.
- **Direct Contracting** will be limited to the following scenarios and will require IFAD's concurrence for each case:
  - a) Where an extension to an existing contract for goods or works is required under 25% of the original contract in value.
  - b) Where the equipment required is proprietary and there is only one source and no alternative exists.
  - c) Where there is a need to standardise upon existing equipment and to achieve compatibility in spare parts.
  - d) In cases of emergency, where urgent delivery is required.

295. **Vehicles.** The procurement of motor vehicles and motorcycles will follow the "**Direct Appointment**" method as provided by the government procurement regulations (*Perpres* No. 54/2010), on the understanding that: (i) the association of motor manufacturers/importers (*GAIKINDO*) has special program called "**Government Sales Operation** or GSO) where the association offers special prices for government procurement of vehicles, which should be lower than prevailing market prices; (ii) the association will provide information on GSO prices periodically in the internet which should be transparent and the government agencies can also compare them with the current market price. However, IFAD must be satisfied that the GSO prices offered by the association of motor

manufacturers/importers (*GAIKINDO*) are substantially cheaper than prevailing market prices. In this regard, the government will provide the official current and updated GSO prices and the publicly available market prices that are published for IFAD review for each procurement package for motor vehicles and motorcycles. The procurement method which will apply upon IFAD's concurrence for the procurement of motor vehicles and motorcycles will be National Shopping by inviting eligible distributors to provide written quotations of the make's, model's and specification's outlined in the Letter of Invitation (LOI). An evaluation panel should review and evaluate the technical and price quotations and other information received and provide its recommendation to IFAD, along with a draft contract for review. The award of the contract will be subject to IFAD No Objection.

296. **Works.** Procurement of works will follow the following procurement methods and thresholds, in accordance with the IFAD Procurement Guidelines and Handbook.

- Each contract for works estimated to cost more than USD 100,000 equivalent shall be procured through the **International Competitive Bidding (ICB)** method using IFAD's applicable Standard Bidding Documents (SBDs). Domestic preference will be allowed for eligible nationally executed works.
- Each contract for works estimated to cost less than USD 100,000 but more than USD 20,000 equivalent may be procured through the **National Competitive Bidding (NCB) method**.
- Each contract for works estimated to cost less than USD 20,000 but more than USD 6 000 equivalent may be procured through **National Shopping method**.
- **Direct Contracting** will be limited to the following scenarios and will require IFAD's concurrence for each case:
  - a) Where an extension to an existing contract for goods or works is required under 25% of the existing contract in value.
  - b) Where the equipment required is proprietary, there is only one source and no alternative exists.
  - c) Where there is a need to standardise upon existing equipment and to achieve compatibility in spare parts.
  - d) In cases of emergency, where urgent delivery is required.

297. **Services.** Procurement of services and technical assistance will follow the following selection methods and thresholds through Request for Proposals or Request for Quotations, in accordance with the IFAD Procurement Guidelines and Handbook.

- Each contract for the selection of consultancy services estimated to cost USD 100,000 equivalent or above, shall follow any one of the selection methods<sup>31</sup> as listed below:
  - a) Quality and Cost Based Selection.
  - b) Quality Based Selection.
  - c) Fixed Budget Selection.
  - d) Least Cost Selection.
- Each contract for the selection of consultancy services estimated to cost less than USD 100,000 but more than USD20,000 equivalent, shall follow any one of the selection methods as listed below:
  - a) Quality and Cost Based Selection.
  - b) Fixed Budget Selection.

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<sup>31</sup> The preferred method for the selection of services from consultant firms only without NGOs competing in the same procurement package or from NGOs only without consulting firms competing in the same procurement package will be through Quality and Cost-Based Selection (QCBS). The preferred method for the selection of services from consultant firms and NGOs competing in the same procurement package will be through Quality Based Selection (QBS).

- c) Least Cost Selection.
- d) Selection Based on Consultants Qualification.
- Each contract for the selection of consultancy services estimated to cost USD 20,000 equivalent or below, shall follow Selection Based on Consultants Qualification method.
- Each contract for the selection of individual consultants shall follow Selection Based on Consultants Qualification method.
- Sole Source Selection will be limited to the following scenarios and will require IFAD's concurrence for each case:
  - a) For tasks that are a natural continuation of previous work carried out by the consultant.
  - b) Where rapid selection is essential (for example, in an emergency situation).
  - c) For very low value assignments costing less than USD 2,000.
  - d) When only one firm is qualified or has the necessary experience for the assignment.
- Selection of services from an UN agency may also be awarded through Sole Source Selection, with the express agreement of IFAD and with a detailed justification which will be examined carefully to ensure that IFAD is content there are no other alternative selection methods which can be used. This would include the proposed selection of UNIDO to provide technical assistance to support the implementation of the value chain development under the project.

**298. Procurement involving community participation.** In accordance with the IFAD Procurement Guidelines, procurement with community participation is not a distinct method of procurement and it therefore requires the same adherence to all principles and standards set out in the IFAD Procurement Guidelines. In order to follow procurement involving community participation in the this project, the NPMO will ensure the following:

- (ii) Translate documents and records from the Borrower's/Recipient's official language(s) to English as may be required for purposes of audit and review.
- (iii) Provide appropriate procedures for regular monitoring and audit of community procurement activities, including the retention of relevant records by the DPIOs, PPCOs and NPMO.
- (iv) Define the relationships, roles and responsibilities between the DPIOs, PPCOs and NPMO and the community, including a clear exit strategy for the completion of the project interventions.
- (v) Ensure proper handover of assets to the community.

**299.** Under the term "community participation", the community may play one or more of the following roles during project implementation:

**As a provider of goods, works or services directly to the project**

**300.** Communities are permitted to undertake works or provide goods or services to the project where:

- (i) It is an implementation modality within the framework of the project design document; or
- (ii) It is not an implementation modality, but it is agreed with IFAD that this represents a cost-effective and practical alternative to procuring externally. IFAD will also consider factors such as fostering ownership, the sustainability of project activities, effective operation and maintenance of a project facility, and the overall risk/reward equation.

**301.** Generally, agreement will only be granted where it can be demonstrated that such goods, works or services have been or could be successfully provided or produced by the community. As a provider, a community may act either:

- (i) On a commercial basis under contract; or

- (ii) As part or all of the beneficiary community's contribution to the project.

### **As the implementing agency undertaking procurement for the project**

302. Communities or informal groups may be brought together to act as implementing agencies to undertake project procurement. Where this is the case, their role will include:

- a) Competitive contracting using any of the agreed procurement methods; and
- b) Supervision of a contracted provider of works, goods or services.

303. **Conclusion.** In accordance with the IFAD Procurement Guidelines and the Handbook, it is proposed that through procurement involving community participation, the local communities will undertake civil works under the Component of Productive Rural Infrastructure, when each of such contracts costs less than IDR 55 million equivalent, which is in line with the government procurement regulations for community participation in procurement of civil works. All such civil works executed by communities under the Component of Productive Rural Infrastructure will be clearly defined in the approved procurement plan. In undertaking the civil works, the community may have to purchase materials and tools, and these should be procured using national shopping method (comparison of at least three quotations).

### **Review of Procurement Decisions**

304. The award of any contract for goods or civil works estimated to cost USD 100 000 equivalent or more shall be subject to prior review by IFAD in accordance with the provisions of the IFAD Procurement Guidelines.

305. The award of any contract for services estimated to cost USD 50 000 equivalent or more shall be subject to prior review by IFAD in accordance with the provisions of the Procurement Guidelines. The award of any contract using direct contracting and/or single source selection method shall be subject to prior review by IFAD in accordance with the provisions of the IFAD Procurement Guidelines.

306. With respect to any other contract for goods, civil works or consulting services, the Borrower/Recipient shall furnish two certified or conformed copies of such contract to IFAD, together with the analysis of the respective bids and the recommendations for award, promptly after its signature and before the submission to IFAD of the first application for withdrawal of funds from the Loan and Grant Accounts in respect of such contract.

307. Before agreeing to any material modification or waiver of the terms and conditions of any contract for goods, works and services or granting an extension of the stipulated time for performance of such contract, or issuing any change order under such contract (except in cases of extreme urgency) that would increase the cost of the contract by more than 10% of the original price, the Borrower/Recipient shall inform IFAD of the proposed modifications, waiver, extension or change order and the reasons therefor. IFAD, if it determines that the proposal would be inconsistent with the provisions of the above, shall promptly inform the Borrower/Recipient and state the reasons for its determination.

### **Procurement Plan**

308. Working Paper 6 includes the agreed procurement plan for all major procurements of goods, works and consulting services for the first 18 months of project implementation, which will be part of the first approved AWPB but will extend for six months beyond the end of the AWPB. The procurement plan includes each contract to be financed by IFAD proceeds, proposed procurement packages (types, sizes and locations), the types of procurement methods, the procurement procedures, the thresholds for pre or post-qualification, estimated cost, prior review requirements and time-frame.

309. The NPMO will update the procurement plan after effectiveness and submit it for IFAD approval. The procurement plan is to be updated annually (or as and when needed) to cover every subsequent 18-month period of the project's duration as part of the AWPB preparation and review



process. The Borrower will promptly inform IFAD of any delays in funding or other revisions to the procurement plan that could significantly affect the timely and successful implementation of project contracts, and agree with IFAD on timely corrective measures.

310. The procurement assessment found that the DPIO and PPCO procurement staff have no prior experience with IFAD or other international donors financed procurement. Therefore, the procurement staff will require training during project start-up. Procurement management will be part of project management training for project staff at all levels in PY1. Refresher training will also be provided during project implementation as needed, especially when new procurement officers are designated. To assist the NPMO, a procurement specialist will be contracted for 12 months (6 months in PY1 and intermittently in PY2). The trained staff should not be transferred for a minimum of 3-4 years.

### **Procurement Management**

311. Procurement management is a very important and integral part of project management as a whole because procurement expenditures provide a large portion of project expenditures. Hence, it must be managed properly. Good procurement management includes, *inter alia*, good planning, timely procurement processes as per the schedule, proper documentations, and supervision or monitoring during contract execution (including evaluation of the performance of contractors, suppliers, and service providers). IFAD requires the use of standard bidding documents (SBD). The procurement staff should have adequate knowledge of IFAD's Procurement Guidelines, the Procurement Handbook and the provisions of the financing agreement. Since the DPIO and PPCO staff have no prior experience with IFAD financed procurement, training will be provided during the start-up workshops prior to project implementation. To assist with initial procurement the NPMO will contract a procurement specialist for 12 months (6 months in PY1 and intermittent in PY2). Procurement management will be included in the project management training for project staff at all levels in PY1. Refresher training will also be conducted during project implementation as needed, especially when new procurement officers are designated.

### **Contract Management**

312. Contract management activities can be broadly grouped into three areas: (1) service delivery management to ensure that services are being delivered as agreed, to the required level of performance and quality; (2) relationship management keeps the relationship between the two parties open and constructive, aiming to resolve or ease tensions and identify problems early; and (3) contract administration handles the formal governance of the contract and changes to the contract documentation. All three areas must be managed in a satisfactory manner by all project units (DPIOs, PPCOs, and NPMO) to ensure that the process is successful. In addition, good preparation and the right contract are essential foundations for good contract management. The arrangement must also be flexible enough to accommodate changes as needed.

### **Procurement Risk Mitigation Measures**

313. The project includes a number of actions to strengthen procurement capacity of implementing agencies (IAs) and mitigate procurement risks. In terms of capacity, each of the NPMO, PPCOs and DPIOs will be required to assign qualified procurement staff to be in charge of procurement related tasks. Other risk mitigation measures include: (i) training workshop for the IAs' staff during the project start up period and during project implementation; and (ii) higher level and expanded scope of ex-post reviews by IFAD to include checks for indicators of collusion, end-use deliveries, and procedural compliance, among other measures.

## **E. Governance and Anti Corruption**

### **Fraud and Corruption Practices**

314. Fraud and corruption can undermine the effectiveness of the IFAD's operations in different ways. IFAD shall apply a zero-tolerance policy where it has determined, through an investigation performed by IFAD, the borrower or another competent entity, that fraudulent, corrupt, collusive or coercive actions have occurred in projects financed through its loans and grants, and it shall enforce a range of sanctions in accordance with the provisions of applicable IFAD rules and regulations and

legal instruments. 'Zero tolerance' means that IFAD will pursue all allegations falling under the scope of this policy and that appropriate sanctions will be applied where the allegations are substantiated. This policy applies to IFAD-funded activities. IFAD ensures that it is effective in preventing, detecting and investigating fraudulent, corrupt, collusive and coercive practices. The Fund shall take all possible actions to protect from reprisals individuals who help reveal corrupt practices in its project or grant activities and individuals or entities subject to unfair or malicious allegations. This policy is in line with the policies adopted by the other international financial institutions.

315. Many transactions in the Project will be vulnerable to corruption. Apart from the corruption from procurement, including overcharges for honorariums and costs, the Project will also be vulnerable to corruption from government employees who expect "thanksgiving money" (bribes) from beneficiaries, suppliers, and contractors.

### **Mitigation Measures**

316. To address the concerns about the potential for corruption in the project, the design incorporates the following measures.

#### **Transparency of Information:**

- Enhanced disclosure provisions: (i) making publicly available all key documents, (ii) informing all bidders promptly of contract awards and bid evaluation summaries; (iii) allowing representatives of end-users of the goods or works being procured to attend the public bid openings; (iv) making available the details of all contracts awarded; and (v) making available the date of request for all contract payments and the date of each payment, with an explanation of the reason for any delays.
- Standardization of certain communication items/materials e.g. (i) use of standard wording in advertisements; (ii) agreement on the list of newspapers of nation-wide circulation in which specific advertisements will be placed; (iii) use of standard bidding and contract documents and request for proposals (for consultancy service), with no further changes to be made without IFAD's prior approval; and (iv) publication of prices paid for items in different locations.

#### **Participation and Consultation:**

- Establishing a complaints handling mechanism (and the use of sanctions), whereby community members and the general public can channel complaints or inquiries e.g. through the use of mobile phone text messaging. Complaints and inquiries will be systematically recorded and answered. The project will also post complaints on the project's website so that case processing will be more transparent. Designated staff at the DPIOs, PPCOs, and NPMO will handle complaints and respond in a timely manner.
- Public Audit Groups: The project would set up public audit groups, one in each province and or district, to facilitate 'more transparent, accountable and locally manageable' project implementation. They would be composed of representatives of civil society, media and other concerned stakeholders, with the members selected by the NPMO, reporting to the National Steering Committee..
- Annual Assessments of Service Providers will be undertaken by local communities with the results contributing to improvement of performance of the service providers and annual project planning process.

#### **Monitoring and Oversight:**

- Direct supervision. The project will be directly supervised by IFAD. One full supervision mission, with the participation of relevant project partners, will be undertaken per annum.
- M&E: the project will establish an operational M&E system from the village to the national level to proactively monitor and report on project activities and performance across the results chain (including financial and physical progress).
- For financial management, there will be an in-depth and intensive supervision in the initial years to ensure the successful implementation of the financial management arrangements and at least one on-site financial management visit either as part of the annual supervision

mission or through a separate mission/consultant complemented by desk-based review of Interim Financial Report (IFRs) and audit reports will be done per year. The project will also prepare financial reports every three months (i.e. in line with the PIDRA approach).

- Procurement: the project will be subject to a higher level and expanded scope of ex-post reviews by IFAD to include checks for indicators of collusion, end-use deliveries, and procedural compliance, among other measures.
- Annual performance review meetings. Annual meetings will be held to review the project performance as well as the country programme to share lessons learned and best practices among project staff and government counterpart agencies and the co-financiers.
- Annual assessments of service providers by local communities to feed into the annual project planning process.
- Independent Audit: The project will be subject to independent and external auditing in line with IFAD procedures and requirements.
- Support forums. Under Component 1, Support forums will be held at selected sub-district, district/island, and provincial levels. The forums will assist the smallholders and their organizations to attain a better access to technical and financial services, to develop supportive business environment, and to gain larger share of the end market price through vertical and horizontal linkages along the value chains. The forums should involve representatives of smallholders, private sector players, and relevant governments.

#### **Enhancing Capabilities:**

- The project has an explicit focus on strengthening the capacity of the line agencies' provincial and district administrations to mitigate the risk of under-performing institutions and improve the weak implementation capacity and accountability. The project also provides important technical assistance to enhance capacities in all critical fiduciary areas.
- For procurement management, (i) each of the NPMO, PPCOs and DPIOs will be required to assign qualified procurement staff to be in charge of procurement related tasks; (ii) training workshop for the IAs' staff during the project start up period and during project implementation.

### **F. Supervision and Implementation Support Plan**

317. It is planned that one full supervision/review mission will take place per year, which will coincide with the time when the project will prepare its AWPB. The supervision/review mission will focus on:

- Achieving development impact based on assessment of progress against agreed indicators embedded in an effective monitoring and evaluation (M&E) system, joint identification of problems and solutions with recipients and implementers, and agreement on suitable actions to achieve the project's development objectives. Where needed, this is supported by project-specific technical support, policy dialogue, innovations and programme and/or design adjustments to improve effectiveness. Implementation support pays special attention to social and environmental dimensions, including improved targeting and mainstreaming of gender issues.
- Ensuring compliance with loan covenants, procurement, disbursement and the end-use of funds, and is an effective tool for promoting economy, efficiency and good governance.

318. The operationalization of the concept of supervision and implementation support will adhere to the following main guiding principles:

- Recognition of loan and grant recipients, who are owners and implementers of development programmes, as key partners with shared accountability for outcomes;
- Enhancing impact and development effectiveness of the individual country programme and, therefore anchored in and responsive to concrete country and programme realities.
- Primary role of IFAD to assist and facilitate project/programme implementation;

- Supervision and implementation support activities set within the context of results-based country programmes, seeking to maximize synergies, opportunities and learning, and to make efficient use of resources;
- Building of partnerships with the private sector, civil society and other development partners, for enhanced coverage and reach of supervision and implementation support, and, where appropriate, improved practices for greater development impact;
- Encouragement of innovation during project implementation;
- Ongoing learning and sharing of knowledge with all stakeholders; and
- Adherence to effective management systems, quality standards and accurate reporting, guided by good practices and policies to improve management effectiveness, and monitoring and evaluation.

319. The supervision/review mission will comprise different “blends” of headquarters staff and contracted service providers and consultants, including reputable international/regional/national institutions and local partners. At least one on-site financial management visit either as part of the annual supervision mission or through a separate mission/consultant complemented by desk-based review of IFRs and audit reports will be done per year.

320. The Implementation Support Plan (ISP) describes how IFAD will support the implementation of the risk mitigation measures and provide the technical advice necessary to facilitate achieving the project development objective (PDO - linked to results/outcomes identified in the result framework). The ISP also identifies the minimum requirements to meet IFAD’s fiduciary obligations.

## **VIII. PROJECT COSTS, FINANCING AND BENEFITS**

### **A. Project Costs**

321. Total project costs including contingencies, duties and taxes are estimated at USD 65 million. Costs have been estimated using October 2010 prices. Price contingencies add about 4% to the base costs. Taxes and duties have been calculated at prevailing rates and amount to USD 5.59 million, about 8% of total project costs.

322. With an estimated 115,700 poor or very poor households in the target villages and about 578,000 people, the cost per household is about USD 605 or USD 105 per capita. If the project directly benefits 49,500 households (group members), or 43% of these households as planned, the actual cost per household will be USD 1,414 per household or USD 282 per capita. The cost of the direct assistance to the SHGs and federations is USD 28.8 million, 44% of project costs, and an average of nearly USD 87,200 per village. The cost of local capacity building (SHGs and federations) is USD 9.52 million or an average of USD 2,885 per group.

**Table 1: Project Cost Summary (USD'000)**

	(USD '000)			% Foreign Exchange	% Total Base Costs
	Local	Foreign	Total		
Community Empowerment	12,809.8	-	12,809.8	-	20%
Productivity Improvement & Integrated Farming Systems	5,965.8	164.2	6,130.0	3	9%
Value Chain Development and Marketing	16,657.6	1,331.8	17,989.4	7	28%
Productive Infrastructure Investment	8310.3	870.3	9,180.6	9	14%
Institutional Strengthening and Project Management	15,132.9	802.4	15,935.3	5	25%
<b>Total BASELINE COSTS</b>	<b>58,876.3</b>	<b>3,168.8</b>	<b>62,045.1</b>	<b>5</b>	<b>95%</b>
Physical Contingencies	-	-	-	-	
Price Contingencies	2,892.0	64.7	2,956.7	2	5%
<b>Total PROJECT COSTS</b>	<b>61,768.3</b>	<b>3,233.4</b>	<b>65,001.7</b>	<b>5</b>	<b>100%</b>

323. Annex III includes the summary cost tables, while Working Paper 8 includes more detailed tables.

## B. Project Financing

324. The proposed project financing is as follows with the percentages in brackets: (i) an IFAD loan of about USD 49.11 million (76%); (ii) an IFAD grant of USD 1.08 million (2%); and (iii) Government contribution equivalent to USD 14.81million (23%).

325. The IFAD loan will finance the project's investment costs, except for the costs of critical value chain TA which the IFAD grant will finance. The central Government will finance all the project's operating costs. In addition, the Government contribution will finance a payment or waiver of any duties and taxes, including value added tax on all project expenditure including equipment, vehicles, supplies, operating costs and technical services.

326. The contributions of the beneficiaries to the costs of the productive infrastructure investments have not been quantified. The communities will decide which investments are to be financed and the community contributions will reflect the contributions made under other projects e.g. *PNPM* etc. for various infrastructure investments.

**Table 2: Financing Plan (USD'000)**

Category	IFAD Grant		IFAD Loan		Govern.		Total		Foreign Ex.	Local (Ex. Taxes)	Duties & Taxes
	Total	%	Total	%	Total	%	Total	%			
Civil Works	-	-	8,313.6	90.9	831.3	9.1	9,144.9	13.1	914.7	7,399.1	831.3
Vehicles	-	-	925.0	75	308.3	25.0	1,233.4	1.8	616.7	308.3	308.3
Equipment & Materials	-	-	13,076.4	90.9	1,307.5	9.1	14,383.9	20.5	1,438.4	11,638.0	1,307.5
Capacity Building, studies and Workshops	310.8	1.8	15,357.1	89.3	1,535.5	8.9	17,203.4	24.6	-	15,639.6	1,563.8
Matching Grants	-	-	7,857.1	100.0	-	-	7,857.1	11.2	-	7,857.1	-
International TA	107.8	100.0	-	-	-	-	107.8	0.2	107.8	-	-
National TA and NGO Services	659.6	14.3	3,582.9	77.9	358.2	7.8	4,600.7	6.6	-	4,182.5	418.2
Staff Costs	-	-	-	-	2,699.4	100.0	2,699.4	3.9	-	2,699.4	-
O&M Vehicles	-	-	-	-	1,560.3	100.0	1,560.3	2.2	156.0	1,262.4	141.8
Office Operating	-	-	-	-	6,210.9	100.0	6,210.9	8.9	-	5,646.3	564.6

Category	IFAD Grant		IFAD Loan		Govern.		Total		Foreign	Local	Duties
Costs									Ex.	(Ex.)	& Taxes
<b>Total PROJECT COSTS</b>	<b>1,078.2</b>	<b>1.5</b>	<b>49,112.1</b>	<b>70.2</b>	<b>14,811.4</b>	<b>21.2</b>	<b>65,001.7</b>	<b>100.0</b>	<b>3,233.4</b>	<b>56,632.8</b>	<b>5,135.5</b>

327. In addition to the above, the provincial and district governments are expected to provide support for project supervision, monitoring and evaluation, office operating costs and other key parallel activities. However, the costs financed by the provincial and district governments are not included in the project cost tables and financing plan.

328. The project period will be seven and half years (July 2011-end of 2018), with intensive project assistance provided to each cluster of villages for four years (matching grants to SHGs provided over three years). As a result implementation of project activities in the last clusters of villages to be targeted will start in 2015.

329. The IFAD loan will be on intermediate terms. Government will use funds from the IFAD loan to insure project vehicles and equipment financed by the loan. The insurance for the project staff will follow the government's customary arrangements.

330. The project budget will come from the national budget (*APBN*) for both the IFAD loan and the central government counterpart budget. *Bappenas* has confirmed that the proposed SOLID project and the proposed IFAD financing has been included in the government's draft "Blue Book" for 2010-2014 pending the issuance of a decree by the Minister of National Planning. The AFS has included a budget for project activities in the draft 2011 budget amounting to IDR 28 billion (USD 3.1 million).

### C. Expected Benefits, Outcomes and Impact

331. It is expected that the project will directly benefit a total of around 49,500 farm households belonging to the SHGs and Federations/*Gaoktans* that the project will support out of a target group of around 115,700 poor or very poor households. The 115,700 poor or very poor households include those households, who are not members of SHGs but who would benefit from some of the projects investments in productive rural infrastructure and natural resource management.

332. The main direct economic benefits will come from: (i) improved prices for commodities that are exported from the islands due to the improvements in quality and some value addition (post harvest management and primary processing); (ii) higher crop yields following the use of improved low cost cropping, enrichment planting and pest management techniques; (iii) rehabilitation of productive rural infrastructure, mainly farm access roads, micro-irrigation systems and previously cropped agricultural areas; and (iv) improved management of natural resources.

333. The community empowerment activities will help create the organisations needed (SHGs and Federations) to realise the production and marketing benefits. The provision of funds to enable the SHGs to establish GRFs will help finance the costs of new technology, the value addition and marketing activities. Similarly, the support for the Federations will help them to operate as village financial institutions and ultimately to act as a link between the SHGs and the MFI and formal banking sectors. Finally, the project's support for gender mainstreaming as a cross cutting issue will be a further un-quantified benefit. Working Paper 1 Attachment 4 includes a Gender Action Plan Matrix.

334. By working through decentralised government systems SOLID, as a central government project with implementation delegated to the districts, can help create better links between central government, sub-national administrations and rural communities in two ways. First, by building institutional capacity and secondly by supporting participatory decision and implementation mechanisms at the community level. Such an approach should strengthen the districts' service provision capacity and contribute to better implementation of future rural development projects in the two provinces, while leading to gains in the social capital of the communities.

### D. Financial and Economic Analysis

#### Introduction

335. The design of this project does not lend itself to a conventional cost/benefit analysis because the location of all the 330<sup>32</sup> target villages has not been finalised and the activities to be financed will be determined by the various SHGs and federations themselves through participatory processes and therefore cannot be known in advance.

336. To address this situation, the economic rate of return (ERR) analysis is based on an expanded analysis of the costs and returns from the major food, cash and tree crops and a sensitivity analysis. The analysis draws on three sources of information to assess the viability of the investments that the project could finance: (i) gross margin, cost benefit ratios and internal rate of return (IRR) calculations for various food and estate crops for both the “without” and “with project” situations; (ii) an analysis of the potential for value addition to key products in the major value chains in the 11 districts; and (iii) the costs and benefits from various infrastructure investments similar to those likely to be financed by SOLID that other programmes have financed. Working Paper 7 provides further details of the three types of analysis.

### **Food, Cash and Estate Crops**

337. For the food and cash crops analysed the potential returns from the introduction of simple improved management techniques, involving the use of some additional inputs and labour, are high with substantial increases in gross margin per ha and in the benefit cost ratios. These calculations are based on the following increases in crop yields (per ha): upland rice 1,000 to 2,000; maize 800 to 2,200 kg; groundnuts 600 to 1,200 kg and soybeans 750 to 1,250 kg. Using lower with project crop yields (per ha) e.g. upland rice 1,500 kg; maize 1,500 kg; and groundnuts 1,000 kg still provides substantial increases in the gross margin per ha and attractive benefit cost ratios, although a reduced soybean yield of 1,000 kg/ha does not.

338. A similar analysis of two estate crops, coconuts and cacao shows the potential for the introduction of improved management techniques as well as for enrichment planting in the case of coconuts and the use of improved planting material through grafting for cacao. Although low at IDR 1.25 million per ha the introduction of simple improved management techniques increases the gross margin of coconuts by 25%. Enrichment planting is potentially highly profitable, with an IRR of 30% under the most unfavourable assumptions tested. However, the incremental return is still relatively low compared to that from some other crops, namely IDR 2.0 million per ha by PY11.

339. For cacao simple, low cost improvements can yield incremental gross margins of IDR 1.50 to IDR 5.50 million per ha respectively for low and high productive areas with attractive benefit cost ratios. Introducing new plant material to low productive areas has the potential to add a further IDR 10.75 million per ha starting from Year 8 with an IRR of 31%. The IRRs are not particularly sensitive to changes in costs and benefits and even under the most unfavourable assumptions tested the IRR exceeds 20%.

340. No uptake rates were assumed. It is expected that the assumed project change in technology uptake and adoption of processing and marketing initiatives will be addressed by providing support from extension workers, farmer facilitators and experienced NGO(s).

### **Value Addition**

341. The analysis of the potential for value addition in the two provinces (Working Paper 3) shows that there are significant potential gains in terms of smallholder incomes from adding value to the major commodities produced in the two provinces with potential net returns of 30-40% of the incremental gross value-accruals. This figure allows for the reduced volume of production that will be sold following processing etc. as well as the costs incurred.

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<sup>32</sup> Project activities will start in 44 villages in 31 sub-districts.

## **Infrastructure Investment**

342. An analysis of the costs and returns for small-scale infrastructure investments undertaken by communities in the past under a similar programme show high rates of return and costs that are approximately 40% less than for the same type of investment undertaken using government contracting procedures.

## **Un-quantified benefits**

343. In addition to these direct sources of benefits the project will have additional un-quantified benefits in terms of community empowerment and institutional capacity building both at the village and service provider levels.

## **Overall Economic Viability**

344. The assumptions made in the economic analysis and calculation of the ERR include the following:

- The economic analysis looked at four possible situations where the project could have an impact based on activities that the project would support. These are examples and exclude other activities e.g. improvements for nutmeg and mace that the project is likely to support, but for which there was insufficient data.
- The analysis showed the incremental production needed if all 49,500 direct beneficiaries adopted each of the four technologies and calculated the area per household required to produce that benefit.
- For each of the improvements, the areas of production are within the area cultivated by a household.
- If the project supported these four activities alone and there was equal uptake of each improvement by the 49,500 beneficiaries, then the uptake rate would be 25% for each technology.
- However, the benefits from other technologies were not quantified, nor were the benefits from the infrastructure (for which the returns are likely to be high), so the uptake rates implied by the economic analysis can be conservatively assumed to be less than 20%.

345. To provide an overall analysis of the project's economic viability, the level of benefits has been calculated that is required to give an overall internal rate of return of 15% over 20 years. This analysis shows that the project needs to generate USD 14.15 million per year at full development (PY12), to provide a 15% return, equal to an annual increase in income of about USD 286 for each of the 49,500 households that are expected to be the project's direct beneficiaries. This modest annual increase in household income could come, for example, from any of the following situations: (i) an increase in the yield of upland rice from 1.0 to 1.5t/p.a. from 1.1 ha; or (ii) improved management of 0.47 ha of high potential cocoa; or (iii) improved management of 1.30 ha of coconuts with enrichment planting; or (iv) improved management and enrichment planting of 0.24 ha of low productive cacao. These improvements do not involve the use of high levels of inputs or significant increase in the use of labour.

346. Sensitivity analysis shows that 10% adverse changes to costs and benefits still yield internal rates of return in excess of the assumed opportunity cost of capital. The switching values for both costs and benefits are 15%. Combined adverse changes in costs and benefits of 20% will reduce the IRR to 9%, while the corresponding changes of 10% still yield an IRR of 12%. Working Paper 7 provides further details of the analysis of the project's overall economic viability.

## **E. Environmental Impact**

347. The project's main emphasis will be on capacity building in poor village and on improved livelihoods and increased incomes by improving product quality and market links and agricultural productivity. The latter will involve the use of improved management techniques (e.g. IPM, green manuring, weeding, pruning, use of new varieties through grafting, enrichment planting etc.), but do not involve the extensive use of purchased inputs either fertilizers, or agricultural chemicals for the



control of pests and diseases. None of proposed activities directly impinge upon the environment. The project's awareness raising activities will increase community consciousness of the need to follow sustainable practises.

348. The agricultural production and marketing activities will have beneficial environmental impacts e.g. green manuring, composting and the proposed NRM activities. The construction of scattered, small-scale village post harvest facilities will have no negative environment impact due to their small-scale while construction will avoid negative environmental impacts e.g. erosion, pollution of water resources etc.

349. Introducing more intensive methods of animal rearing will reduce the numbers of animals running free in and around the villages, will improve productivity of the grazing areas, make more efficient use of feed resources and help the return of nutrients to cultivated land through collection and use of manure. Similarly, encouragement of intercropping and mixed cropping, together with conservation agriculture techniques will improve soil conservation and reduce erosion.

350. Limiting possible support for marine fisheries to obtaining greater value from the existing catch is designed to improve livelihoods without encouraging increased fish capture.

351. The design provides for investment in small-scale rural infrastructure identified by community empowerment and facilitation processes; and will very likely include funding for improvements of access tracks, micro-irrigation development and rehabilitation of previously cultivated areas. The first activity will not include the construction of any new alignments, but will upgrade existing tracks and paths to facilitate crop collection at harvest and transport to collection points for subsequent processing/ marketing<sup>33</sup>. Micro-irrigation will include an assessment of any possible downstream impacts to avoid investments that will disadvantage other communities.

352. In all cases pertinent laws and regulations for environmental impact assessments and relevant IFAD guidelines would be applied during the course of investment planning, scheme design and implementation to ensure incorporation of any necessary environmental mitigation measures. The Project Implementation manual will include the necessary details.

353. Based on the foregoing analysis, the project is classified as Category "B".

## **IX. PROJECT RISKS AND SUSTAINABILITY**

### **A. Risk Analysis and Management with Assumptions**

354. IFAD will monitor the enabling environment during project implementation and through the annual portfolio review process, and if necessary, IFAD will assist the Government to address priority policy and institutional reforms to ensure continued support for poverty reduction and development of small-holder-based farming systems in Maluku and North Maluku. This approach is in line with the six national priorities of the MTDP 2010-2014 to which the project can contribute (governance reform; poverty alleviation and improving food security; infrastructure development; environment and disaster management and with a focus on the outer islands and conflict areas).

355. Project design and implementation arrangements are aligned with the Government's decentralisation processes. The project will be a central government project with implementation delegated to the district governments with the provinces providing a coordination and oversight role. The decentralisation process is seen as irreversible and recentralisation is not seen as a risk to the project's implementation arrangements.

356. Under-performing institutions at all levels will have a negative impact on project outcomes. Therefore, the project design provides resources to finance additional staff to assist the SHGs and the federations to strengthen the capacity of the line agencies' provincial and district administrations to perform their respective support functions effectively. The approach is designed to counter the potential problem of under-performing institutions.

357. The quality of construction of small-scale rural infrastructure implemented at village level is

<sup>33</sup> Other programmes (e.g. *PNPM-Mandiri*) are providing finance to improve market access and other rural roads and other rural infrastructure such as village drinking water supply schemes, school improvements, health centres etc.

frequently poor and subsequently poorly maintained. The project design addresses this risk by focusing on simple infrastructure directly related to improving agricultural productivity which is within the capacity of the groups and federations to implement and maintain rather than the more general types of rural infrastructure e.g. those financed by *PNPM-Mandiri*. Close supervision and monitoring using strong project implementation teams, establishing and training the groups and federations on the maintenance of infrastructure investments are all ways of ensuring the sustainability of the infrastructure.

358. Farming communities in Maluku and North Maluku are traditionally risk averse and cautious about change. There is a risk that the assumed rate of technology uptake and adoption of processing and marketing initiatives that add value to the production of food and estate crops may not materialise, and so prevent the achievement of the project's objectives. The ability to form sustainable SHGs and village federations for marketing and processing and an access to finance underlie the rate of development assumed in the project's financial and economic analysis and the targets included in the project's logical framework. Component A, to be implemented with the support of extension workers and suitably experienced NGO(s), will seek to ensure that the SHGs and federations that the project will help establish can become sustainable organisations. The project implementers will have access to the experience, lessons learned and best practices from the recently closed IFAD assisted PIDRA project which had a major focus on establishing and supporting sustainable SHGs and associated federations.

359. The risk that the procurement of the inputs and other materials required by the farmer organisations and self-help groups financed with project assistance will be delayed will be countered by the use of Community Participation in Procurement procedures. The SHGs and federations will purchase their own requirements and there will be no project procurement of inputs on behalf of the groups/federations (apart from those needed for demonstrations).

360. A final risk is that the activities of the SHGs and federations will be hindered by a lack of access to credit. To overcome this risk and help the various project-assisted organisations subsequently gain access to the financial services provided by the formal banking sector and MFIs, the project will assist the SHGs and federations establish and build up groups revolving funds (GRFs) so that the members have access to funds for input purchases. In addition, the project will work to establish partnerships between the federations and MFIs and the formal banking sector to enable the SHGs and federations obtain funds for investment over and above the level that their GRFs can provide.

## **B. Exit Strategy and Post Project Sustainability**

361. The project's exit strategy is an essential part of the design. Key elements of that strategy relate to the support to be provided to the SHGs and federations during the project period. Project design focuses on ensuring that these organisations can continue to function profitably and develop further without project assistance following the end of project support. The project aims to achieve this by providing a phased four- year programme of support for all the SHGs and the federation in each of the target villages so that all new SHGs and federations have sufficient time to develop their capacity before the end of project assistance. This level of assistance, combined with developing value chains and market links that provide group members with a greater share of the total end value of the products, and so provide them with greater incentives, enhances the chances that the project benefits will be sustainable.

362. Other elements of the exit strategy are: (i) the establishment and support for GRFs which can continue to help meet the need investment funds for investment etc. after the end of the project period, while also helping the SHGs and federations access funds from the MFI/banking sector hence contributing to the sustainability of the SHGs and federations; (ii) project support for the FFs and the private-sector village animal health workers so they can continue to provide services after the end of the project assistance on a fee for service basis; and (iii) raising the awareness of village administrations to use their budget resources to maintain project financed minor-rural infrastructure.

363. Intensive technical and skills training will be provided to the farmer facilitators who will act as the link between the SHGs and sources of public or private service provision during and after the project. The farmer facilitators will be trained to demonstrate best practices on their farms and during

farm visits to other smallholders and over time some of the demonstrations may evolve into nurseries supplying improved planting materials, or become seed production areas. In accordance with the government policy, the government hired Field Extension Workers (*PPLs*) (one per village) will continue after the end of the project. The value chain change agents are selected based on their entrepreneurship and leadership in starting pilots in selected value chain development, trading or marketing, who can run their own private small scale businesses during and after the project.

## **X. INNOVATIVE FEATURES, LEARNING AND KNOWLEDGE MANAGEMENT**

### **A. Innovative Features**

364. The design of the SOLID project has three innovative features. First, the project will introduce as part of the project's value chain approach village federations to handle larger volumes of agricultural products as required by the market with drying, grading, primary processing, etc.

365. Secondly, the project will introduce quarterly Project Coordination and Consolidation Meetings in which project staff and consultants from the 11 districts, the two provinces and national level identify constraints and recommend improvements in operational arrangements, procedures and policies.

366. Thirdly, the project will adopt a more organised approach to capacity building, which is a major project investment, than in the past. This approach includes first conducting a Training Needs Assessment covering staff involved with project activities as well as carrying out an evaluation of the impact and effectiveness of the training provided.

### **B. Project Knowledge Products and Learning Processes**

367. The project's expected "knowledge products" are the following: (i) the project data bases; and (ii) the impact studies, including the annual RIMS reports. The NPMO M&E unit will lead the dissemination of the findings from the studies to project management staff at all levels. The aim being to ensure timely adjustments to project activities when needed so as to ensure the achievement of the development objectives. The project will fund a number of activities to disseminate the knowledge from the studies to the stakeholders in rural development and a broader audience in Indonesia:

- Support for the costs of publication and dissemination of studies carried out.
- The annual country portfolio review meetings that review the performance of individual projects and the country programme and to share lessons learned and best practices between the various stakeholders.
- The proposed Project Coordination and Consolidation Meetings to solve technical problems and implementation issues.
- A project website for disseminating studies, output and selected outcome data to a wider audience.

### **C. Policy Dialogue and Expected Institutional Outcomes**

368. As already noted policy dialogue will occur as part of the country portfolio review process and thereafter feed into the policy making processes of the AFS and MOA as well as other external development agencies. During this process the experiences and lessons learned from the field experience of the IFAD supported projects will be discussed and recommendations made for changes in approaches to rural poverty reduction, improving household food security etc. for consideration by the AFS/MOA.

### **D. Knowledge Management and Regional Knowledge Networking**

369. Knowledge management and communications will be in line with the IFAD Strategy for Knowledge Management. The following activities will aim to improve the arrangements in place for knowledge management and communication during the project implementation: (i) annual assessments of service providers by local communities will feed into the annual project planning

process; (ii) the policy analysis outputs and other specific studies focusing on rural poverty will inform the government policy making machinery; and (iii) annual meetings will be held to review the project performance as well as the country programme to share lessons learned and best practices among project staff and government counterpart agencies and the co-financiers.

370. At the regional level, the stakeholders in the IFAD country programme, including those participating in this project, will receive newsletters on different focused themes from IFAD Headquarters, regular analysis and documentation of lessons and experience learned from the project operations to communicate country-level knowledge from Indonesia, including that from SOLID, to others.

## **XI. KEY FINANCING CONDITIONS AND COVENANTS**

### **A. Key Financing Conditions**

371. Among others, the following is a list of key financing conditions to be discussed with the Government of Indonesia during the Negotiations:

- (1) The Borrower/Recipient will ensure that the project will be implemented within the framework of the agreed project objectives, approaches and strategy.
- (2) The Borrower/Recipient will ensure that the project activities financed by the IFAD Financing are in accordance with the agreed financing plan.
- (3) The Borrower/Recipient will ensure that the proposed eligibility criteria and targeting criteria for different project activities provided in the Design Documents will be strictly adhered to during project implementation.
- (4) The Borrower/Recipient will ensure that all procurement will follow the IFAD Procurement Guidelines (September 2010) and the Procurement Handbook of IFAD (September 2010).
- (5) The Borrower/Recipient will ensure that all productive rural infrastructure projects will be: (ii) selected and designed using participatory approaches; (iii) requested in writing by the communities who will make written application to the responsible district technical agency; and (iii) designed by the district public works agencies with supervision of construction undertaken by consultants or district technical agencies, with community participation.
- (6) The Borrower/Recipient will ensure that prior to letting contracts for productive rural infrastructure sub-projects financed by the project, the sub-project proposals must meet the following eligibility criteria: (i) is not on the negative list<sup>34</sup>; (i) is not on the above negative list; (ii) has been identified and budgeted using community participation procedures; (iii) includes the details of those who would oversee implementation and manage the proposed investments; (iv) shows the extent of the proposed community contributions (including community monitoring of the quality of civil works); and (v) details of: (a) any land required; (b) any environmental and social impact; (c) arrangements for O&M; and (d) all irrigation development under the project will utilise gravity supplies or shallow wells and take such other steps as may be necessary to avoid adverse impact on groundwater levels.
- (7) The Borrower/Recipient will ensure that no contracts will be approved until the first year's annual work plan and budget had been prepared and approved by IFAD and all contracts for productive rural infrastructure construction in the first and second Project Years will be submitted to IFAD for review together with the relevant Withdrawal Application.
- (8) The Borrower/Recipient will ensure that due consideration is given to gender issues in project implementation, both with respect to project beneficiaries and to recruitment of project staff and ensure, among other things, that:

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<sup>34</sup> (i) Large-scale infrastructure (such as big dam, primary and secondary irrigation canals, Ports or harbors, primary roads, and national, provincial and district roads as specified in Bina Marga Decree and other relevant government regulations). (ii) Construction of new roads or any change to existing road alignments (that will likely trigger safeguards issues). (iii) Zones marked for ecological protection and conservation such as peat swamp areas, areas of primary forest, length of coasts with coral reefs and notified protected areas. (iv) Sites identified (or classified) as potential Flooding and Landslide Sensitive Zones generally consisting of secondary forests, slopes greater than 40% and slopes greater than 15% with sensitive soils (backshore, river bank, lake and dam-side and around springs). (v) Protected areas or particular areas that is likely to alter land-use or areas that are to be designated as protected zones.

- (a) 50% of the community facilitators and agricultural extension staff are women;
  - (b) Women are encouraged to apply for project posts and equally-qualified women candidates are given preference in the recruitment and selection of project staff; and
  - (c) Approximately 50% of participants in the village annual planning and beneficiary impact workshops are women.
- (9) The Borrower/Recipient will ensure that the MOA will establish and maintain until completion of the project a National Project Management Office (NPMO) in the Agency for Food Security (AFS) of the Ministry of Agriculture (MOA) staffed with 15 staff working full time for the project, including a National Project Director; 5 professional staff responsible for community development, gender, natural resource management, rural infrastructure development, value chain and integrated farming systems; two staff for planning and M&E; two staff for financial management and book keeping; two staff for procurement; and other supporting staff (operator computer, translator, secretary, etc.).
  - (10) The Borrower/Recipient will ensure that the Provincial AFS in Maluku Province and the *Dinas* Agriculture in North Maluku Province will each establish and maintain a Provincial Project Coordination Office (PPCO) until completion of the project staffed with at least 15 staff working full time for the project, including a Provincial Project Coordinator (PPC); four officers for planning, M&E and reporting; two staff for financial management and book keeping; one staff for procurement and contract management; three technical staff contributed by the collaborating agencies in the province (e.g. food crops, estate crops, value chains); and support staff (computer operators, translator, secretary, etc.).
  - (11) The Borrower/Recipient will ensure that the Agency for Food Security and Extension (AFSE) in five districts of Maluku Province and *Dinas* Agriculture in six districts of North Maluku Province will each establish and maintain a District Project Implementation Office (DPIO) staffed with at least 15 staff to work full time for the project, including a District Project Manager (DPM); a Deputy; four officers for planning, M&E and reporting; two staff for financial management and book keeping; one staff for procurement and contract management; three technical staff contributed by the collaborating agencies in the district (e.g. food crops, estate crops, value chains, infrastructure); and support staff (computer operators, translator, secretary, etc.).
  - (12) The Borrower/Recipient will ensure that no project assistance will start in the province or any district until all the agreed positions in the PPCO and DPIOs are filled with qualified staff.
  - (13) The Borrower/Recipient will ensure to provide qualified staff in adequate number as specified in the Design Documents or as agreed IFAD from time to time, including agricultural extension staff.
  - (14) The Borrower/Recipient will ensure that the selection of existing staff to be assigned full-time to project activities will follow a transparent selection and/or recruitment process with an agreed timetable. Staff selected will have qualifications and experience that match those of the job descriptions.
  - (15) The Borrower/Recipient will ensure that the key project staff, *inter alia*, the NPMO, PPCs and DPMs responsible for coordination of the project implementation, the staff for Finance, Accounting, Planning M&E of the NPMO, PPCOs and DPIOs will not be transferred until the completion of the Mid-Term Review, except in the case of unsatisfactory job performance. The Borrower/Recipient will ensure that will consult the IFAD three months before any planned transfer.
  - (16) The Borrower/Recipient will ensure to make available the government counterpart contribution as required for project implementation, annually as part of the budget, to MOA, the Provinces of Maluku and North Maluku and the Project Districts, to finance project activities during the entire project period and continue to finance the operation and maintenance of project financed public investments after the end of the project period.
  - (17) The Borrower/Recipient will provide adequate human and financial resources to support the recurrent costs of the project operations both during and after the project period.
  - (18) The Borrower/Recipient will by 15<sup>th</sup> April 2011 and in each of the following years, not later than 15<sup>th</sup> November in each Fiscal Year, commencing 15<sup>th</sup> November 2011 and until completion of

the project, provide IFAD a draft AWPB for project activities for review and approval.

- (19) The Ministry of Finance will ensure that SOLID will be a “central government project”, under which it will make available the required proceeds of the IFAD Financing to the Ministry of Agriculture in the annual national budget to finance the project activities in accordance with the approval AWPBs.
- (20) The Ministry of Finance will open and maintain a Designated Account at Bank Indonesia in the currency of United States of America for the project.
- (21) The Ministry of Finance will open and maintain a Grant Bank Account in the currency of United States of America in a bank acceptable to IFAD to finance all agreed activities, in accordance with the approval AWPBs.
- (22) The Borrower/Recipient will ensure that the NPMO, PPCOs and DPIOs will maintain and consolidate the project accounts in accordance with sound accounting practices and government accounting procedures to reflect the progress of the project and to identify its resources, operations and expenditures. The project accounts will reflect all financial transactions during the project implementation period for the IFAD loan and grant and by project component and by standard expenditure categories. The project accounts will be maintained separately from any routine budget accounts or other externally funded project accounts.
- (23) The Borrower/Recipient will ensure that starting from the Date of Effectiveness, the NPMO, PPCOs and DPIOs will each prepare financial records for the entire project, on an annual basis, ending on 31<sup>st</sup> December of each year, and submit the detailed statement of the project expenditures during the period under review to the Government and IFAD no later than three months after the end of each fiscal year.
- (24) The Borrower/Recipient will ensure that starting from the fiscal year of 2012, the Government Audit Board (BPKP) will audit the project accounts including the IFAD and government counterpart contributions to the project annually in accordance with the International Standards on Auditing. The audited accounts and financial statements, in a format agreed with IFAD, and including a separate opinion on the SOEs, the operations of the Designated Account, the Grant Bank Account and government counterpart contribution and the operations of the project expenditures in the treasury office accounts of each of the implementing agencies at the national and regional levels, will be submitted to IFAD no later than six months after the end of each government fiscal year, until closing of the loan. The audit report will be a Long-Form Audit and will contain a separate management letter. The reply of the Project to the management letter will be submitted to IFAD within one month of the receipt of the audited accounts.
- (25) The Borrower/Recipient will ensure that will ensure that the MOA, the Governments of Maluku and North Maluku and the participating District Governments will establish a project monitoring and evaluation system from the village to the district, provincial and national levels, satisfactory to IFAD and including monitoring of and reporting on the RIMS indicators, not later than six months after the Date of the Effectiveness.
- (26) The Borrower/Recipient will ensure that the project vehicles and equipment financed by the IFAD Financing and the project staff will be adequately insured, against health and accident risks to the extent consistent with its customary practice in respect of its national civil service, during the entire project period.
- (27) The Borrower/Recipient will ensure that the Governments of Maluku and North Maluku will make effective arrangements to coordinate with other international agencies operating in the project area to ensure that: (i) uniform policies are adopted for the same sector or activity, such as extension methodology, staff incentives, beneficiary contribution in labour and local materials to the construction costs of irrigation facilities, drinking water supply schemes, village access roads and responsibility for their operation and maintenance; (ii) project activities financed by different donors in the same province/district are carefully phased to avoid constraints on the available human and financial resources; (iii) activities financed on a parallel basis by other donors are coordinated with those financed by the project.
- (28) The Borrower/Recipient will ensure that the Governments of Maluku and North Maluku and the participating District Governments will take a proactive and lead role in managing and

- coordinating development agencies and their financed projects operating in the project area, take particular care to supervise and coordinate project implementation and take prompt actions to resolve any emerging constraints.
- (29) The Borrower/Recipient will ensure that legislation remains in place to provide the necessary legal basis for allowing user groups, such as irrigation, drinking water supply and rural access roads, to establish themselves and to operate and maintain the relevant infrastructure.
- (30) The Borrower/Recipient will ensure that the extension system will be able to deliver required services to farmers, in the target villages and will ensure that there is one field worker available to work full-time with two target villages for four years.
- (31) As part of maintaining sound environmental practices, the Borrower/Recipient will ensure that, among other things:
- (a) The project parties will maintain appropriate pest management practices under the project and ensure that pesticides procured under the project do not include any pesticide either proscribed by the International Code of Conduct on the Distribution and Use of Pesticides of the Food and Agriculture Organisation of the United Nations (FAO), as amended from time to time, or listed in Tables 1 (Extremely Hazardous) and 2 (Highly Hazardous) of the WHO Recommended Classification of Pesticides by Hazard and Classification 1996-1997, as amended from time to time;
  - (b) Effective policies and measures are enforced to safeguard forest and fishery resources and endangered species in the project area;
  - (c) All irrigation development under the project will utilise gravity supplies or shallow wells and take such other steps as may be necessary to avoid adverse impact on groundwater levels; and
  - (d) All rehabilitation of existing roads and upgrading of tracks will include an adequate number of cross drainage structures and the design thereof will be preceded by, and otherwise take account of, a review of local hydrology.
- (32) The Borrower/Recipient will ensure that the at Project start-up, AFS of MOA will prepare and issue a Project Implementation Manual within 90 days after the Date of Effectiveness that that will specify the project's financial management system, procedures for planning and budgeting, loan and grant disbursement and reimbursement, release of funds, operation of the Designated Account and project accounts and procurement and physical and financial reporting procedures.
- (33) In addition to providing counterpart funds for the project, the Borrower/Recipient will exempt from taxes the importation, procurement and supply of all equipment, vehicle and motorcycles, and exempt from income tax the fees of national and international consultants financed by the IFAD Financing.

## **B. Conditions President to Withdrawals**

372. No withdrawals of the IFAD Financing shall be made from the Loan and Grant Accounts until:
- (a) The MOA, the Provincial Governments of Maluku and North Maluku and each of the participating District Governments shall each have established a NPMO, PPCOs and DPIOs respectively and each shall have staffed the NPMO, PPCOs and DPIOs with the agreed number of qualified staff working full time for the project.
  - (b) The Borrower/Recipient shall have confirmed to the Fund the availability of counterpart funds in the national, budgets for financing the first twelve months of Project implementation.
  - (c) The Borrower/Recipient shall have duly opened the Designated Account and the Grant Bank Account.
  - (d) The Annual Work Plan and Budget for the first Project Year shall have been duly reviewed and given no objection by the Fund.
  - (e) The Procurement Plan for the initial 18 months of the Project shall have been duly reviewed and given no objection by the Fund.
  - (f) The Project Implementation Manual shall have been duly reviewed and given no objection by

the Fund.

## **XII. RECOMMENDATION**

373. On the basis of the above, the project would be suitable for an IFAD loan of USD 49.112 million and a IFAD grant of USD 1.078 million. The proposed total IFAD financing will be USD 50.19 million.