



Investing in Indonesia Institutions for Inclusive and Sustainable Development

The World Bank in Indonesia
Water Sanitation

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FLOW OF FUNDS, FLOW OF WATER

Significant Investments are needed in the water and sanitation sector. Inadequate water supply and sanitation undermines Indonesia's status as a middle income country, weakens the competitiveness of its cities, and seriously affects the lives of ordinary people. Improving sanitation services alone can prevent economic losses of more than US\$6.3 billion per year..

WATER

Access to safe drinking water in Indonesia barely keeps pace with population growth. Only half the urban dwellers have piped water, while 37 million mostly poor rural people still drink from unprotected sources. Water quality and security are under serious threat from pollution, catchment degradation, and over-exploitation, particularly in Java.

Average annual sectoral spending has fallen dramatically in the past decade from US\$400 million in the 1990s to US\$45 million in 2005, about one-tenth of what is needed to achieve Indonesia's Millennium Development Goals (MDGs). Both national- and local governments have been reluctant to invest: only US\$12.4 million or 0.37 percent of reserves was invested in Indonesian regional water utility companies (PDAMs) in 2006.

Operational performance is poor. Regional water utility companies spend heavily on operations and maintenance, but not on investments. For every Rupiah spent on capital investment, 9 Rupiah is spent on operations and maintenance. Half of all the companies are loss-making: one-quarter report water losses in excess of 40 percent and an average service coverage of only 20 percent. By contrast, rural water spending is too focused on infrastructure rather than operations and maintenance. National programs and the special allocation fund (DAK) are the main sources of rural infrastructure spending, but the collection of service fees and responsibility for operations and maintenance are not emphasized. Local governments are the key to the next generation of reforms.

Water-related success stories typically feature local governments that have undertaken reforms, made politically unpopular decisions, invested in PDAM equity, and required performance improvements in return for their support

SANITATION

As a rising middle-income country, Indonesia needs to substantially increase access to sanitation services. Roughly 55 percent of the population has access to at least basic sanitation services; this is well below the 67 percent average for Southeast Asian countries. Open defecation has remained constant at around 40 percent in rural areas and 18 percent in urban areas since 1990. Sewerage coverage is minimal: only 2 percent of urban areas have access to sewerage connections and centralized sewage treatment. The country is losing an estimated US\$6.3 billion annually due to poor sanitation (US\$28.60 per capita), including health care costs, lost productivity, premature deaths, water resource and fishery losses, declining land values, as well as tourism losses. Much of this could be averted: improved sanitation will lead to an estimated annual economic gain of over US\$4.5 billion.



Key Issues

The key challenge is for local governments to undertake the necessary reforms including improved governance - to implement sector programs. The government has announced concrete national water supply and sanitation targets to reach the MDGs. The central government needs to help local governments and local water companies' access financing to meet their investment requirements and encourage and support local planning efforts.

Encourage investment in good water supply and sanitation projects through financing schemes supported at the national level.

WATER SUPPLY

1. Fast-track progress on debt restructuring of local water companies.
2. Develop long-term financing through commercial banks for creditworthy local water utilities using official development assistance finance/ guarantees.
3. Establish competition and transparent criteria- based partial grants and technical assistance for non-creditworthy local water companies whose LGs are willing to invest and institute good governance mechanisms

SANITATION

1. Clarify investment cost-sharing arrangements between the national government and local governments for municipal sewerage and water treatment projects.
2. Initiate a major investment program for municipal sewerage and treatment to be implemented by local governments that incorporates decentralized or connected community systems and improved on-site facilities.

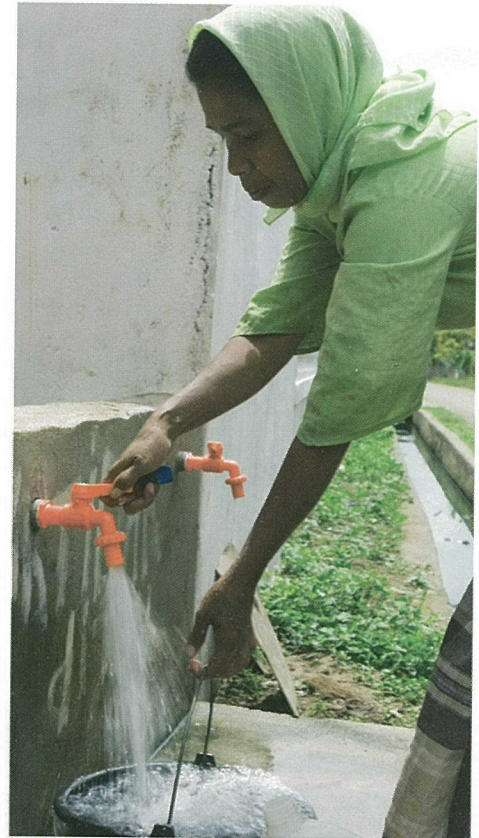
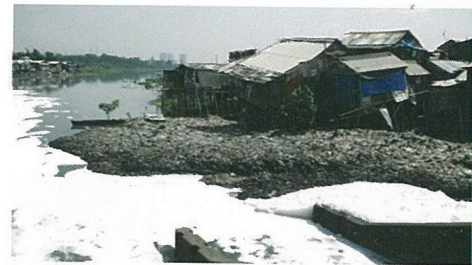
Focus local government's attention on instituting good governance measures and strengthening the implementation capacity of local institutions involved in water supply and sanitation.

WATER SUPPLY

1. Encourage local governments to invest in water utilities supported by an output-based incentive mechanism.
2. Develop and implement sanctions for inefficiency and underperformance such as intercepting inter-governmental transfer payments and instituting temporary management/ receiverships for local governments and utilities that continue to underperform despite receiving bailouts and other support.
3. Build on successful community-based water organizations by promoting accountability and increasing access to financing and technical services.

SANITATION

1. Institute a capacity building program for local governments focusing on planning and development of sanitation services using the city-wide sanitation strategic approach.
2. Realize the national vision for open defecation-free communities by increasing the demand for suitable sanitation services and improving the supply capacity of local sanitation markets.



HOW THE WORLD BANK WORKS IN REAL TERMS

The World Bank offers direct investment and financing, advisory services, capacity building activities, and policy reform assistance to support the government's efforts to develop, realize and deepen its water and sanitation agenda.

The World Bank directly finances infrastructure development in water and sanitation in Indonesia through stand-alone projects such as the recently approved Urban Water Supply and Sanitation Project, rural water and sanitation programs (such as the ongoing Third Water Supply and Sanitation for Low Income Communities Project), water resources management programs, and multi-sectoral programs such as the National Program for

Community Empowerment (PNPM). Looking ahead, and in line with government priorities, the World Bank can support government in the development and implementation of a water supply and sanitation program including through the deployment of an output based implementation/disbursement mechanism.

The World Bank supports the Indonesian government's broader infrastructure policy and institutional reform agenda through the Infrastructure Development Policy Loan (IDPL) series. The IDPL aims to increase the quantity and efficiency of central government spending on infrastructure and improve sub-national infrastructure

services, especially in the water and sanitation sectors. IDPL series will continue to support the implementation of a number of cross cutting reforms vital to these sectors.

The World Bank mobilizes significant development partner support for technical assistance, knowledge management, and institutional development activities with the aim of strengthening national sanitation and water policies, as well as local program implementation capacities. Pilot projects that feed back to national policies, complemented by rigorous analytical work are a central feature of the World Bank's support. The World Bank's trust funded and global partnership programs (e.g.,

Water and Sanitation Program) help local governments plan and implement sanitation, water investment and water resource management programs. It is committed to ensuring that similar support continues over the medium term by convening donors (e.g., AusAID, Netherlands, USAID, JICA) focusing on these key sectors.

The World Bank also provides financing services in support of capitalizing infrastructure-financing facilities, such as the Indonesia Infrastructure Fund Facility, and credit enhancement services through the proposed Indonesia Guarantee Fund for infrastructure investments in water and sanitation.



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