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## INTERNATIONAL DEVELOPMENT ASSOCIATION

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REPORT AND RECOMMENDATION  
OF THE  
PRESIDENT  
TO THE  
EXECUTIVE DIRECTORS  
ON A  
PROPOSED DEVELOPMENT CREDIT  
TO  
THE REPUBLIC OF INDONESIA  
FOR A  
SECOND TECHNICAL ASSISTANCE PROJECT

September 2, 1970

INTERNATIONAL DEVELOPMENT ASSOCIATION

REPORT AND RECOMMENDATION OF THE PRESIDENT TO  
THE EXECUTIVE DIRECTORS ON A PROPOSED DEVELOP-  
MENT CREDIT TO THE REPUBLIC OF INDONESIA FOR A  
SECOND TECHNICAL ASSISTANCE PROJECT

1. I submit the following report and recommendation on a proposed development credit to the Republic of Indonesia in an amount in various currencies equivalent to US\$4 million for a second technical assistance project.

PART I - HISTORICAL

2. On December 27, 1968 the Association made a Development Credit of US\$2 million to Indonesia to help meet the costs of high priority studies and other projects of technical assistance for which finance from other sources would not be readily available. The bulk of these funds has now been committed, or will be committed shortly and the proposed credit is requested to enable the Government, in cooperation with the Bank's Resident Staff, to meet the increasing demand for technical assistance.

3. The provisions of the proposed Development Credit are substantially the same as those of the previous Technical Assistance Credit and were approved by the Government after discussions in Djakarta with the Bank's Resident Staff.

4. If approved, the Second Technical Assistance Credit would be the eleventh Development Credit to Indonesia. The following is a summary statement of Development Credits to Indonesia to date, with disbursements as of July 31, 1970:

<u>Credit No.</u>	<u>Year</u>	<u>Borrower</u>	<u>Purpose</u>	<u>\$million</u>	
				<u>Amount</u>	<u>Undis- bursed</u>
127	1968	Indonesia	Irrigation Rehab.	5.0	2.6
135	1968	Indonesia	Technical Assistance	2.0	1.6
154	1969	Indonesia	Highways	28.0	28.0
155	1969	Indonesia	Agricultural Estates	16.0	15.2
165	1969	Indonesia	Electricity Distrib.	15.0	15.0
193	1970	Indonesia	PUSRI Fertilizer Expansion	30.0	30.0 a/
194	1970	Indonesia	Second Agricultural Estates	17.0	17.0 a/
195	1970	Indonesia	Second Irrigation Rehabili- tation	18.5	18.5 a/
210	1970	Indonesia	Telecommunications Expansion	12.8	12.8 a/
211	1970	Indonesia	Fisheries	3.5	3.5 a/
				<u>147.8</u>	<u>144.2</u>

a/ Not yet effective

5. Under Credit 154-IND, \$61,000 has now been disbursed on consultant services. Bids for workshop equipment, and for highway equipment and spares have been issued; and it is expected that about \$12.8 million of the credit will be disbursed in fiscal 1971. Under Credit 155-IND \$762,200 has been disbursed mostly on procurement of fertilizer. Consultants for management advisory services have now assumed their duties, and disbursements are expected to begin on the other items. Credit 165-IND was declared effective only on June 1, 1970; management consultants are now in the field and disbursements are expected to commence shortly.

6. During the next few months I expect to present to the Executive Directors proposed credits for a technical education project, for a third irrigation rehabilitation project, and later in fiscal 1971, credits for projects for the production and distribution of rice seeds, for tea estates and for a second highway project.

PART II - DESCRIPTION OF THE PROPOSED CREDIT

Borrower: Republic of Indonesia

Beneficiaries: Various Government departments, agencies and enterprises.

Amount: Various currencies equivalent to US\$4 million.

Purpose: The carrying out of high priority studies and other projects of technical assistance (subprojects) to assist the Borrower in the planning and implementation of the rehabilitation and development of its economy. The purpose and scope of each subproject would be determined by agreement between the Borrower and the Association.

Amortization: In 50 years, with a ten year period of grace through semi-annual instalments commencing October 1, 1980 and ending April 1, 2020. Each installment up to and including payment due April 1, 1990, to be 1/2 of 1 per cent, and each instalment thereafter to be 1 1/2 per cent.

Service Charge: 3/4 of 1 per cent per annum.

PART III - THE PROJECT

8. The purpose of the Project is to help provide financing for consulting and engineering services for feasibility, pre-investment and other studies and activities, for which finance from other sources is not readily available to help the Government carry out its program of rehabilitation and economic development. The project would thus continue the assistance provided by the first Technical Assistance Credit. Commitments made so far and expected in the near future under this Credit are described below:

<u>Project</u>	<u>IDA Contribution</u> <u>US\$ equivalent</u>
(i) Detailed engineering of Djatiluhur Irrigation Project	356,000
(ii) Feasibility study of two partially established sugar projects	55,000
(iii) Seeds Industry Project Preparation	67,000
(iv) National Fertilizer Study	530,000
(v) Groundwater Project Preparation	<u>30,000</u>
	<u>\$1,038,000</u>

Up to now \$420,000 has been disbursed.

In addition, commitments are expected to be made soon for an evaluation of the rice intensification program, requiring approximately \$300,000, and for an inventory of irrigation facilities, estimated to cost approximately \$200,000. Furthermore, it has been agreed in principle that if UNDP should decline to finance a planned study of the sugar industry of Indonesia, then Credit 135 would be used for the purpose. The cost of the sugar study is estimated at approximately \$500,000. If, as now appears likely, UNDP should finance that study, the balance left in the present Credit would be applied towards subprojects described in paragraphs 11 and 12 below.

9. The engineering studies for Djatiluhur greatly accelerated the making of the \$18.5 million second Irrigation Rehabilitation Credit (No. 195 IND). The study of two sugar projects has been completed and provides the basis for discussion by the Government with possible lenders with respect to further action on the projects. As mentioned above, I expect to recommend during the current fiscal year a credit for rice seeds production and distribution based in part on the study financed by Credit 135 IND. The National Fertilizer Study is an essential complement to the PUSRI Fertilizer Project (Credit No. 193 IND) and will provide the

Government with a basis for further action with respect to fertilizer production, distribution and use. The groundwater project preparation study will provide the basis for judging whether a groundwater development project should be considered for financing in the near future. The other studies presently contemplated are expected either to prepare specific investment projects or to provide the basis for policy and program formulation.

10. The technical assistance available under the proposed credit, because it can be used for a broad spectrum of activities and can be made available quickly and can draw upon expertise available on an international basis, is particularly valuable to Indonesia. Experience has indicated also that bilateral aid-givers are willing to finance projects identified or prepared under Bank or IDA auspices even though they are often reluctant to finance projects developed under other bilateral auspices.

11. The proposed credit would continue to finance, but to a larger extent than hitherto, the final engineering of projects which are specifically intended for Bank/IDA financing where the use of those funds would substantially reduce the leadtime between project identification and appraisal and between approval and disbursement. There is one immediate project which requires detailed engineering as a basis for appraisal and where no assistance from sources other than the Association can be obtained. This is the highway project in Sumatra, identified on the basis of a UNDP-financed feasibility study referred to in paragraph 6 above. Because of the severe shortage of budgetary funds for development purposes the Government has asked that the foreign exchange cost of the detailed engineering be financed from the proposed technical assistance credit rather than reimbursed to it from the eventual credit for the project. This sub-project alone is likely to absorb about \$2.5 million. The credit for the project itself, assuming it is made, would of course, be smaller to that extent.

12. Other contemplated studies are in agriculture (beef cattle industry in the Eastern islands, crop pest investigation) transport, industry (iron and steel, industrial estates, pulp and paper, timber processing), and in power for an engineering feasibility study of additional thermal power generating capacity in West Java. This feasibility study is estimated to cost about \$500,000. It is expected that some studies planned by the Resident Staff will, as in the past, be financed from other sources; it is therefore not possible at this time to specify the use of all of the credit funds. But since more than \$3 million of the new funds requested can be expected to be promptly committed as indicated above, a credit of \$4 million appears justified. As indicated earlier, \$160,000 of the first Technical Assistance Credit do not have a use immediately in sight, so that a total of \$1.5 million for purposes still to be specified over the next 18 months to two years remains available.

13. The proposed credit would in all essential respects follow the pattern used in the first credit. The Government of Indonesia would contribute to the financing of the various technical assistance activities not less than 15 per cent of the cost of the services concerned, including contributions in kind. In subprojects committed so far, the Government's contribution has always exceeded 15 per cent. Standard IDA terms will apply to the credit since refinancing from a project credit, on which the normal ten year term of technical assistance credits is based, would be difficult to accomplish, because the credit is to finance various studies, related to various projects, some of which may be financed from other sources. The Director of the Bank's Resident Staff would continue to act for the Association in dealing with all matters related to the selection and execution of all subprojects.

14. Before proceeding with the proposed credit, the availability of technical assistance from other sources, and other ways of providing it from IDA have been reviewed. For a number of technical assistance projects identified or prepared by the Resident Staff, grant financing has been obtained or is expected -- from UNDP (for the Bali Tourism and Sugar Industries Studies) and from bilateral aid-givers (for studies in the fields of transport, agriculture, industry and power). Efforts will continue to be made by the Government in cooperation with the Resident Staff in each instance to obtain grant financing from these sources but as in the past there will be cases where such alternative financing cannot be arranged at all or on an appropriate basis. Although considerable technical assistance is available from UNDP and from bilateral aid sources, substantial additional technical assistance is required for both planning and execution of programs and projects for which funds would be available once they had been prepared. The Bank Group's usual procedure of providing funds for such assistance as part of a project-credit in the same field, has so far had little application in Indonesia because the need for such technical assistance could not always be clearly enough identified when a credit was made and because new fields of economic activity are considered for Bank Group lending as the rehabilitation and development of Indonesia's economy proceeds. While we would expect to make increasing use of project credits to finance studies related to future lending in the respective fields there is still presently, and will continue to be in the foreseeable future, a pressing need for the funding of technical activities which the credit would provide.

#### PART IV - Legal Instruments and Authority

15. The draft Development Credit Agreement between the Republic of Indonesia and the Association, the Recommendations of the Committee provided for in Article V, Section 1 (d) of the Articles of Agreement of the Association, and the text of a Resolution approving the proposed Credit are being distributed to the Executive Directors separately. The text of the Development Credit Agreement follows closely that of the Development Credit Agreement for the First Technical Assistance Project.

PART V - THE ECONOMY

16. The last full economic report on the position and prospects of Indonesia (EAP-10a) was issued on November 14, 1969, and has since been supplemented by a special report, "Current Investment Activity in Indonesia" (EAP-11a) dated March 27, 1970.

17. Indonesia's recent economic performance has been satisfactory. Inflation has been kept under control and, given the new condition of relative stability, a good start has been made on programs of rehabilitation and development. In April 1970, a basic exchange reform was introduced, including the unification of the exchange rate (except for a special rate for program aid); the foreign exchange markets have since been in balance, and internal price changes have not been significant. Also in April 1970, agreement was reached between Indonesia and the "Paris Club" countries (the western creditors and Japan) for the re-scheduling of their share of Indonesia's pre-1967 external debt. The settlement accounts for about 36 per cent of this debt amounting to some \$2.1 billion.

18. The 1970/71 development program is larger than last year's, and more of it is being financed from Indonesia's own resources. The effort to expand the hitherto very low levels of public saving and foreign and private domestic investment has been impressive; domestic revenues increased 36 per cent in 1969/70, and a similar increase is expected for the current year (1970/71). Development expenditures are still relatively low, however, and the very considerable amount of project aid committed in recent years by the member countries of the Inter-Governmental Group for Indonesia and by international agencies, including IDA, is only now beginning to flow into Indonesia in significant quantities.

19. Pledges of aid for 1970/71 by the IGGI approached the \$600 million requested by the Indonesian Government. This figure included a request for project aid of \$260 million, primarily for projects requiring an estimated \$150 million in foreign exchange ready for commitment at the end of 1969 but also for other projects expected to be ready during the 1970/71 fiscal year. Commitments of this order are likely to be needed in future years if the investment requirements of Indonesia are to be met. Any delay in undertaking and completing the pre-investment studies and technical assistance required to bring projects to the stage at which commitments are appropriate, could reduce potential project aid below development needs.

20. The immediate development prospects depend largely on the rate at which the economic and institutional damage caused by past mismanagement can be repaired. The efforts of the Government in this respect are, in some ways, already becoming effective. However, the administrative framework required for the effective implementation of development projects has yet to be firmly established. If this is done, and if present economic policies continue and the flow of technical and financial aid is maintained, the prospects of growth appear good.

PART VI - COMPLIANCE WITH ARTICLES OF AGREEMENT

21. I am satisfied that the proposed Development Credit would comply with the Articles of Agreement of the Association.

PART VII - RECOMMENDATION

22. I recommend that the Executive Directors approve the proposed Development Credit.

Robert S. McNamara  
President

Washington, D.C.

September 2, 1970