

USAID



UNITED STATES AGENCY FOR INTERNATIONAL DEVELOPMENT

CRISIS AND RECOVERY

STRATEGY FOR INDONESIA
(FY 1999 - FY 2003)

PREFACE

“Those who cannot remember the past are condemned to repeat it.”

--George Santayana (1863-1952)

Rich in natural resources and situated astride one of the most strategic shipping lanes on the globe – the Straits of Malacca – Indonesia has always been a focus of great power attention, whether that of the once dominant British and Dutch colonial empires, or the martial gaze of Imperial Japan during the 1930s and 1940s. More recently, Indonesia, along with China, Vietnam and Malaysia, figures prominently in the simmering dispute over oil and gas rights in the Spratley Islands. It is well to keep Indonesia’s strategic significance firmly in view. Now that the Asian financial crisis has exposed the weak and corrupt underpinnings of Indonesia’s economic and political infrastructure, we have a unique opportunity to help Indonesians achieve democracy and remake the economic and social fabric of their country.

What should be done to reverse the slide into the abyss of this once prosperous, but still strategically vital country? If the world stands idly by, it is quite conceivable that much more, by many orders of magnitude, in economic and humanitarian assistance will be necessary to restore stability in Indonesia.

USAID has refocused its assistance programs to deal with the most pressing social and economic needs of Indonesia’s beleaguered millions. Over the longer run, USAID has developed a strategy, set forth in this document, to take full advantage of the opportunities presented by the crisis for political, economic and social reform. USAID has also taken the lead in organizing an inter-agency response to the crisis, the “Accelerating Economic Recovery in Asia” (AERA) initiative, which was recently announced by the Vice President and Secretary of State at the APEC meeting in Kuala Lumpur.

We look forward to working with the Congress, other USG agencies, the NGO and donor communities and regional institutions, such as APEC and PECC, to bring maximum resources to bear upon the crisis in order to aid this key ally in its recovery and reform efforts.

EXECUTIVE SUMMARY

Indonesia is gripped by a severe and lingering economic and political crisis which is creating widespread unemployment, impoverishing millions and causing extensive human misery. The world has not seen its equal since the days of the Great Depression. At the same time, the crisis provides unprecedented and previously inconceivable opportunities to bring about key economic and political reforms necessary for Indonesia's recovery, future sustainable growth, and peaceful transition to a more open, less corrupt and participatory society.

In response to the crisis and the opportunities created thereby, USAID has developed a flexible, yet focused, multi-year strategy for the period FY 1999 through FY2003. **USAID's strategy seeks to support essential political and economic reforms necessary for Indonesia's recovery and long-term sustainability as a prosperous democratic nation, while helping to mitigate the adverse impact of the recovery and reform process on the Indonesian people.**

Four strategic thrusts frame USAID's approach: *(1) shore up social safety nets and increase humanitarian assistance; (2) spur economic recovery, launch institutional reform and restore investor confidence; (3) facilitate transition to democracy; and (4) assist indigenous non-governmental organizations and local governments to initiate reforms that will strengthen environmental management.* Underlying these strategic thrusts are four crosscutting themes, namely: *(1) promoting the utilization of NGOs, particularly with respect to the next three themes; (2) promoting transparency in decision-making and anti-corruption efforts; (3) giving attention to the impact on and role of women in the crisis and our response; and (4) supporting continued decentralization of governmental authority and community participation.* These four themes resonate throughout the strategy and therefore enable us to magnify the impact of our assistance in these four areas.

In comparison to its pre-crisis strategy, USAID has:

- **Expanded into new assistance areas to respond to newly-emerged needs arising from the crisis** -- e.g., food aid; medical supplies; employment generation; technical assistance for financial and banking regulations and corporate restructuring; and civic education and elections-related aid to facilitate the holding of a truly free and fair election;
- **Capitalized on newly-emerged opportunities** -- e.g., supporting a greatly expanded number of indigenous NGOs who in turn represent a broader range of sectors and ethnic and religious groups than in the past; and supporting the adoption of a wide range of economic governance reforms which have been long needed and with which the government is now willing to proceed; AND
- **Coordinated an inter-agency response to the crisis, i.e., the Accelerated Economic Recovery in Asia Initiative (AERA)**. AERA was announced by the Secretary of State and Vice President at the recent APEC meeting in Kuala Lumpur.

USAID's strategy will be implemented through USAID's long-standing bilateral program as well as the newly-developed AERA regional initiative under which Indonesia will be the primary recipient. Through these vehicles, which will also marshal the resources of the MDBs and other donors, the USG has developed a robust yet targeted response to help move a key ally along the road of reform and help mitigate the social and economic impact on its people as such reform proceeds.

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I. CRISIS OVERVIEW

A. INDONESIA'S SLIDE TOWARD CHAOS

Economic Crisis: After 33 years of virtually uninterrupted annual growth rates of around eight percent, Indonesia's growth in 1998 will slump nearly 20 percentage points -- from plus five percent in 1997 to minus 15 percent in 1998. In Jakarta, one out of every three workers are out of work, and unemployment nationwide has reached 20 percent. The rupiah, after initially losing 85% of its value, has settled uneasily at a level that is one third of what it was a year ago. Inflation is raging at the 80 percent level. Per capita income has dropped from \$1,200, a level that enabled Indonesia to join the ranks of middle income countries, to \$400 (at prevailing exchange rates) and, as a consequence, 40 million people have moved into the ranks of the absolute poor. The International Labor Organization (ILO) predicts that as many as 80 million people will earn less than a dollar a day by the end of 1998.

The commercial financial sector is paralyzed and banks have virtually ceased operating. Twenty banks have gone out of business and numerous others are either foundering or likely to fold or be taken over shortly. Commercial banks have not made a loan since September 1997. Nearly two-thirds of the companies listed on Jakarta's stock exchange are technically bankrupt. Private debt to foreign sources alone is estimated at \$60-70 billion and an estimated \$20 billion of foreign and domestic capital has fled the country. Once booming building construction has halted, the real estate market has collapsed, retail shops are closing and manufacturers are shutting their gates.

Humanitarian Crisis: The political and economic crises are having dramatic social impact. The rapid economic decline, highlighted by the precipitous fall in value of the rupiah, escalating inflation and growing unemployment, threaten the social compact. Some reliable estimates have up to 20 million persons out of work or a three-fold increase since 1996. On average, some 15,000 workers in the formal sector continue to lose their jobs each day. Parents, unable to afford school fees, have enrolled only 54 percent of Indonesia's children in the current school year, down from 78 percent last year. The number of women licensed as sex workers has doubled and the number of unlicensed women entering the sex trade has risen exponentially. Consequently, health workers report dramatic increases in the number of sexually transmitted infections (STIs) and abortions. Improvements in maternal and child health could well be reversed. Health and family planning services, suffering from the inability of government and private suppliers to finance key imported commodities, are unable to respond. The humanitarian crisis creates a potential for widespread social unrest. It has disrupted commercial distribution systems, sown fear among traditional traders, and contributed to inflated food prices. Anger at inflated prices, in turn, has fueled more unrest, such as looting and burning of rice warehouses.

Political Crisis: Although events such as El Nino and the fragility in other Asian economies have played a role in sparking the Indonesian crisis, systematic misgovernance and abuse of power created the conditions for severe economic collapse and the potential for a humanitarian disaster.

These conditions have created enormous and unpredictable uncertainties in a culturally complicated and geographically diverse society. In place of the rigid, hierarchical and often repressive New Order government, there is now no clear or broadly accepted agreement on the overriding "rules of the game." Many issues are now a threat to national stability and sustainable growth. Long simmering disputes in East Timor, Irian Jaya and Aceh generate increasingly vocal questions about devolution of political authority and Indonesia's territorial integrity. The vicious anti-Chinese riots, intimidation and credible accusations of brutal rapes have strained ethnic relations and led to massive capital flight. Although the military has historically stood as the ultimate guarantor of law and order and an active arbiter of key political issues, there is increasing debate about its appropriate future role in politics. The long-established doctrine of *dwi fungsi* (a military role in social and political affairs) is increasingly under open attack. The decision to hold parliamentary elections in May 1999 has provoked questions about the processes governing access to public office. Finally, Soeharto's abrupt departure left no clear consensus on who should or could provide leadership to move the country forward.

Many fear that the new freedoms -- and the magnitude of key unresolved political issues -- could lead to social breakdown and a collapse of law and order. In the last six months, more than 150 people were killed in East Java under unexplained circumstances. In mid-October 1998, two minivans of thugs attacked the leading legal aid society, and volunteers investigating the events of last May, including accusations of organized rapes of ethnic Chinese women, have reported repeated threats and harassment. The armed forces, challenged by a more assertive press and NGO advocacy organizations and tainted by expanding revelations of past killings and abuse in Aceh, Irian Jaya, Lampung and East Timor, have lost much of the popular respect they once enjoyed.

On the other hand, elements of the political crisis, such as former President Soeharto's forced departure in May 1998, unleashed opportunities for democratization previously hardly conceivable. President Habibie agreed to elections, released many political prisoners, sought to reach agreement on East Timor, and began investigations into corruption. There has been a dramatic flowering of a free and independent press: 140 new newspapers were launched; Tempo, the leading newsmagazine until its banning four years ago, renewed publication; and dozens of new radio stations began to broadcast. Eleven unions and tens, possibly hundreds of new non-governmental organizations (NGOs) have been formed. More than 90 groups seek formal recognition as political parties. Megawati Soekarnoputri, a leading opposition leader, held a party convention attracting 500,000 person in Bali -- without incident. The country's largest Muslim organization, Nadhlatul Ulama, organized a rally in Jakarta with 20,000 participants, again without incident. In numerous localities, particularly on Java, popular movements threw out old village leaders.

B. INDONESIA'S SIGNIFICANCE FOR THE U.S.

What happens in Indonesia has significant implications for the United States. With more than 200 million people, Indonesia is the world's fourth largest country, has the largest Islamic population of any nation and has the potential to become the world's third largest democracy. Prior to the crisis, Indonesia's dramatic economic progress -- and in social areas such as education and family planning -- made it a leader in Southeast Asia. Indonesia is also of strategic importance to the US. It is a major market for U.S. trade and investment and a potential

leader in the development of democratic institutions. Situated astride strategic sea lanes, through which much of the world's commerce travels, Indonesia's stability is critical to many large trading nations. An important member of the Association of Southeast Asian Nations (ASEAN) and a stabilizing political force in the region, Indonesia had been a key factor in the region's economic boom.

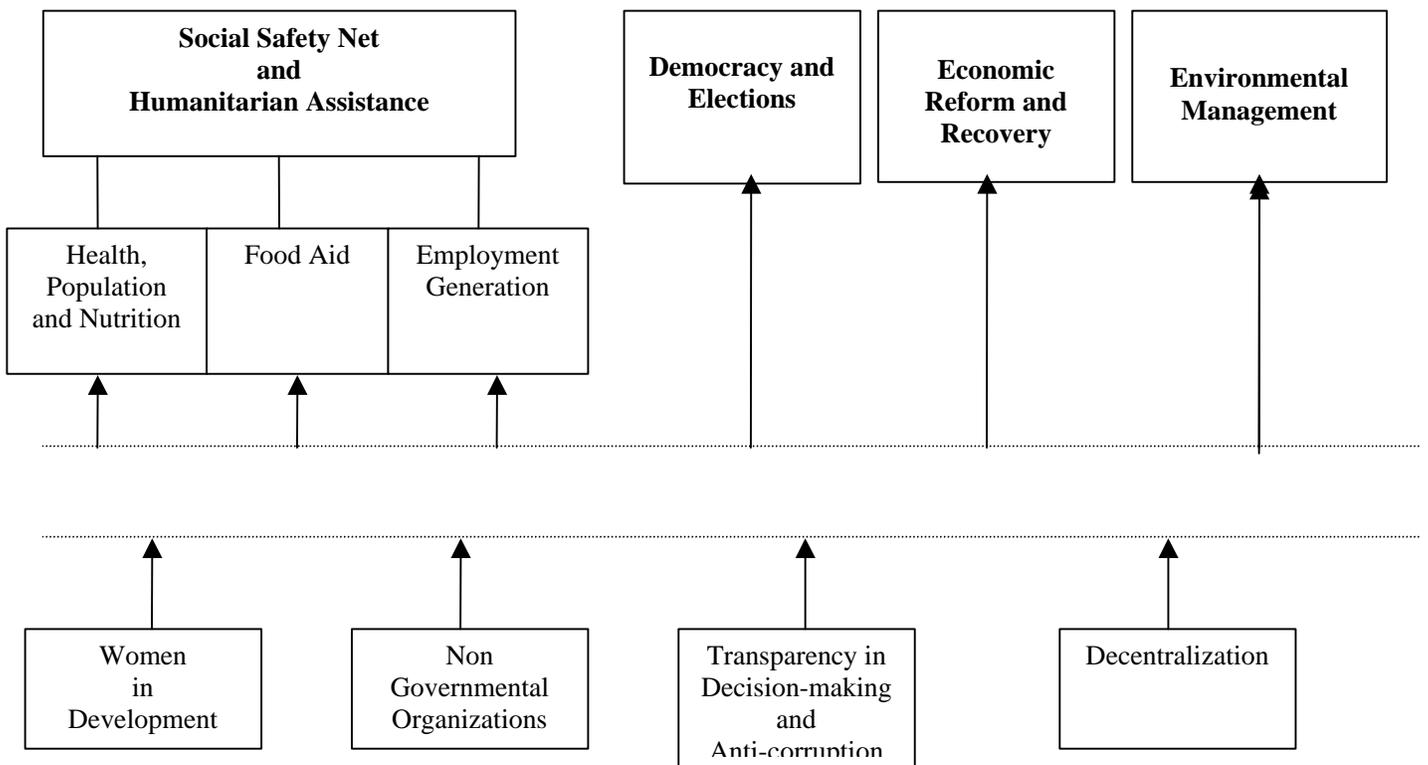
With over 17,000 islands and remarkable diversity of flora and fauna, it is one of the world's biologically most diverse nations. It holds much of the world's primary forests and enormous mineral and coastal resources. The way in which these resources are developed will have major impact not only on biodiversity but also on global warming and control of greenhouse gasses, issues in which Indonesia, as an archipelago, has particular interest.

Unless the US reacts, and responds quickly to arrest Indonesia's downward spiral and to reignite recovery, there is a likelihood of further economic and political destabilization of the kind which will require substantial injections of assistance. In the pages that follow, USAID outlines a strategy for helping to restart the Indonesian economy, while taking advantage of the opportunities presented by the fluidity of the situation to drive political and economic reform. This strategy will enable USAID to respond quickly to immediate pressing needs--indeed it has done so already--and to seize the surfacing opportunities for newly emerging development opportunities.

II. USAID'S STRATEGIC PLAN

USAID's strategy seeks to support essential political and economic reforms necessary for Indonesia's recovery and long-term sustainability as a prosperous democratic nation, while helping to mitigate the adverse impact of the recovery and reform process on the Indonesian people.

This strategy targets four strategic areas. Such assistance will be provided via: (1) an expanded bilateral program which places particular emphasis on creating social safety nets, promoting economic governance, and supporting Indonesia's democratic transition; and (2) a proposed five-year Asian regional initiative under which Indonesia will be the primary recipient. The "Accelerated Economic Recovery in Asia" (AERA) initiative takes principal aim at essential economic reforms, improvements in public and corporate governance, facilitating the role of small and medium enterprise as the engine for the recovery and growth of economic activity, and strengthening social safety net policy and implementation.



A. STRATEGIC OBJECTIVE: SHORE UP SOCIAL SAFETY NETS AND INCREASE HUMANITARIAN ASSISTANCE

Through the direct provision of aid and assistance to strengthen development and implementation of social safety net policies and programs, USAID seeks to mitigate the harsh impact of the crisis on Indonesia's citizens, thus providing the space needed for essential economic and political reforms to take place.

USAID has identified four areas where it believes it has a comparative advantage to help mitigate the humanitarian damage caused by the crisis. USAID will coordinate its interventions to target the same communities, where possible, to maximize the use and impact of USAID's social safety net assistance. *First*, USAID will help maintain health services to protect child and maternal health, including reproductive health. *Second*, USAID will target food aid to those communities most adversely impacted by the crisis. *Third*, USAID will launch a program to help communities access the considerable funds already available from the donor community for labor-intensive public works programs. *Fourth*, under the AERA initiative, USAID will promote the development and implementation of improved social safety net policies, through support for policy development and demonstration models. In addition, once the banking system has been restructured and, assuming the credit instruments are available for the purpose, USAID will support the use of credit guarantees to ignite economic activity.

1. Protect the Most Vulnerable Populations

Rationale: The economic crisis has led to both a *health crisis* and a *health care crisis*. As a result of the economic crisis, an estimated 80 million persons are now living below the poverty line, and are having trouble meeting basic needs, including an adequate and nutritious diet, transportation to health facilities, and payment of fees for health care, medicines, and contraceptives. Millions of Indonesians no longer have the purchasing power to seek care from private providers and must increasingly rely on community or government provided services. At the same time as demands on the public health system have increased, the GOI's funding for the health sector has decreased by as much as 15-20 percent in the past year, reducing the resources available to maintain the extensive public and private health care system and its ability to meet increased demand.

Without support for key primary health care interventions, the service system in Indonesia will deteriorate. As the service system deteriorates, the health of Indonesians – and particularly those most directly affected by the economic crisis -- will suffer. Fewer poor women will use trained providers for prenatal care and delivery of their babies resulting in increased complications and risk of mortality. A decline in the use of contraceptives is already leading to increased unplanned and unwanted pregnancies, higher birthrates and increased reliance on abortion. Declining use of basic child health services will lead to increased child morbidity and mortality. Nutritional status has declined, resulting in severe vitamin A deficiencies and anemia in some areas, as the quantity and quality of food available to poor families has decreased significantly. STI infections are reportedly rising with increased prostitution and reduced condom use, and shortages of diagnostics impedes the ability of the health system to diagnose and treat STIs.

USAID will work with its partners to *protect the health of the most vulnerable groups, particularly women and children, by ensuring that households continue to have access to essential primary health care services, that monitoring systems are in place to foster appropriate responses, and that information is available about appropriate health behaviors.*

Protection of the most vulnerable groups from the worst effects of the economic downturn will require the GOI and its partners to identify the effects of lower household and government expenditures on nutritional intake, disease outbreaks, and use of the health care system. This will allow the GOI, USAID and other donors to target resources toward those most affected, and to adjust programs to meet their actual needs. Eventually decisions on where and when to phase out certain social safety net measures will be able to be made on the basis of improved health, nutritional status and other considerations. This effort to strengthen the capacity of the GOI at all levels to monitor health and nutrition status and disease incidence will be important for the recovery period and beyond.

Proposed Action Areas:

- Assess trends in nutritional status and micronutrient deficiencies of vulnerable populations; use data to target food aid and micronutrient interventions (particularly Vitamin A and iron);
- Monitor and assess availability, cost and use of essential drugs, medical supplies and contraceptives at public and private facilities; use data to inform priority procurements and the formation of health messages;
- Track utilization of public and private health facilities and respond as needed with demand-stimulating actions, e.g., promotional messages, health cards and/or vouchers;
- Survey risk behaviors for STI/HIV/AIDS and use information to design prevention interventions targeted to groups at high risk;
- Support midwives including emergency supplies, contraceptives, training, and operational support for private practices;
- Support U.S. and indigenous PVO/NGOs and other private sector entities for primary health care programs at the community level; and
- Support information, education, communications and advocacy efforts that provide families with information that can enable them to cope with the challenges of a troubled economy, e.g., enhance their understanding of the value of girls education, vaccines, birth spacing and antenatal visits.

2. Improve Food Security

Rationale: The availability and affordability of rice, cooking oil, sugar and other basic food stuffs are central to stability in Indonesia. The May 1998 riots were spurred in part by the rise in food prices and street demonstrations to lower food prices have continued since May.

In 1997 and early 1998, El Nino weather patterns resulted in the worst drought in Indonesia's recorded history, thus creating severe shortfalls in food availability and higher prices. USAID responded with 85,000 tons of commodities to nearly one million beneficiaries through food-for-work and vulnerable group feeding programs located primarily in the eastern islands. However, now Indonesia's food crisis is primarily one of access, not supply. Inflation, growing poverty,

and disruption of the normal food distribution and marketing systems have reduced access to food in the urban and peri-urban areas on Java and Sumatra. A low-wage earner who spent only 27 percent of salary on rice in 1996 now has to spend 80 to 90 percent for basic food.

With estimates of the number of households at risk running as high as 17 million, there is a broad consensus within the donor community that any meaningful response to the current food crisis must rest on successful interventions to stabilize and reduce open market prices and target special assistance to those households most in need. The GOI must manage these interventions and, unless they are effective, the relatively small resources of the donor community will have minimal impact.

Proposed Action Areas:

- USAID will work with the GOI and the donor community to strengthen GOI policies and management systems for food prices and food stocks, A food policy and operations assessment will be completed by mid-December 1998 to identify technical assistance required to strengthen the GOI's food policies and management; and
- \$50 million in Title II emergency food assistance for FY99 to support food for work, direct distribution and vulnerable group feeding programs proposed by the World Food Program (WFP), Catholic Relief Services (CRS), CARE and other U.S. and indigenous NGOs.

3. Refocus Jobs Programs and Utilize New Mechanisms to Increase Employment

Rationale: The financial crisis has caused unemployment in Indonesia to soar. A recent Central Bureau of Statistics (CBS) survey showed that 13.9 million are unemployed, a three-fold rise since 1996. Informal estimates indicate as many as 20 million persons are out of work. Unemployment is concentrated in West Java (3.6 million), Jakarta (1.3 million), East Java (1.7 million), Central Java (1.6 million), and North Sumatra (1 million). Crisis-generated under-employment is even more serious. The hardest hit sectors are construction, real estate, finance, manufacturing, and hotels and tourism -- sectors predominantly situated in urban areas.

USAID aims to create temporary jobs by building, maintaining, and rehabilitating basic infrastructure and community facilities in the urban areas with the highest absolute numbers of unemployed. This helps mitigate the impact of the economic crisis because one workday of labor provides a family with access to one day's food.

The instruments to initiate a broad employment generation program already exist in the form of the government's labor-intensive projects (Padat Karya). However, thousands of projects worth millions of dollars are stalled in the approval system because local communities do not understand how to master the bureaucratic process. USAID will facilitate access to these considerable funds by accelerating implementation of Padat Karya programs financed in part by the WB and ADB. USAID is well-placed to play this role because of its long-standing work in fiscal decentralization which created financing channels that link central funding directly to local governments. To ensure the communities that are most in need are the targets of employment generation projects, USAID will help strengthen the GOI's monitoring and analytical capacity. USAID will give particular attention to improving gender analysis because food-for-work programs frequently have been designed in ways that have excluded women.

Proposed Action Areas:

- USAID will work with NGOs and local governments to identify appropriate projects and match them with the requirements of the Padat Karya program; and organize communities to identify and design basic community infrastructure (such as footpaths, drains, solid waste collection points and other basic projects), using unemployed workers in the target areas.
- USAID will support the formation of a secretariat at the GOI's Planning Ministry to coordinate and improve the targeting of employment generation programs; build independent data collection and analysis capabilities; and develop program approaches and monitoring techniques to ensure that women benefit from employment generation efforts.

4. Promote Development and Implementation of Improved Social Safety Net Policies and Programs

The collapse of the social safety nets provides an opportunity for the USG, working with the multilateral banks, to build more effective social service delivery systems to reduce the impact of future economic downturns. Under the AERA initiative, potential areas for assistance include pension system reform, unemployment insurance system development, development of programs for displaced workers, development of labor market information systems, design of efficient systems for government subsidies, where such subsidies are needed; and food policy reform.

B. STRATEGIC OBJECTIVE: FACILITATE TRANSITION TO DEMOCRACY

Five elements comprise USAID's democracy and governance strategy – *elections, media, NGO advocacy, improved governance and legal reform*, with elections support holding the highest priority in the immediate term. USAID will reach out to new development partners and greatly expand the range of assistance activities to undertake this strategy and facilitate the efforts of Indonesians to effect a democratic transition.

1. Make Elections Support a Priority Focus

Rationale: The forthcoming parliamentary and presidential elections planned for May 1999 and December 1999, respectively, offer both an important opportunity and potential threats to Indonesia's political transition. Because the success of these elections is so critical to Indonesia's political transition -- and will profoundly affect the shape of USAID's program across the board -- USAID has identified elections support as the priority focus of its democracy program and has already initiated activities to help address each of the following challenges.

First, there is concern about the basic laws and ground rules for the election: who can compete, and under what terms and conditions. Failure to reach agreement on these basic issues will severely jeopardize the legitimacy of the elections and undermine the credibility and effectiveness of the new government. It would also pose serious dilemmas for many newly active political groups: Whether to continue to work within a system whose basic legitimacy

they severely question, or withdraw from electoral politics and work for more fundamental and wide-sweeping changes.

Second, there is the challenge of encouraging meaningful competition. More than 90 new parties have formed, and most are still defining their platforms and have little time to build a national constituency.

Third, the success of any economic recovery program will be based on the ability of the new government to generate sufficient public support for actual reform – economic, political, judicial and social. It will be important for the election campaign to provide an opportunity to identify and debate key policy options, and then for the election results to propel these toward a resolution that claims broad support. Political parties themselves need to understand the complexities of the issues and the range of choices, and they need to use the campaign to educate voters, to generate a debate and to form a broad, workable consensus.

Fourth, there is the challenge of simply administering a free and fair election across 17,000 islands in a culturally and religiously diverse nation of some 208 million people. This includes the capacity to deal with a wide range of issues from electoral rolls to ballot security, the role of independent observers and counting procedures, training of poll workers, and orienting members of an independent Election Commission. Also needed are the requisite machinery to conduct a free and fair election, educate the citizenry on the most important reform issues, and build sufficient momentum in the pre-election period for advancing the consolidation of democratic reforms in the post-election era.

Proposed Action Areas: To implement its elections strategy, USAID will support assistance to:

- NGOs, think tanks, and the media engaged in advocating for reform and monitoring both the political and economic reform processes;
- political parties and NGOs engaged in the formulation of issues and policy agendas that address transition issues and the economic crisis;
- an independent Election Commission involved in overseeing actual election administration;
- a network of national, region and local NGOs and civic organizations capable of undertaking independent election monitoring; and
- an independent body of national and international observers to help establish the legitimacy of the election.

2. Strengthen Media's Role in Advancing Democratic Development

Although suppressed in the past (through multiple license requirements, threats of closure, etc.), the media has become a conduit of information exchange, analysis and debate, and also checks the powers and abuses of government and non-government actors. Further media development will be critical to advancing democracy in Indonesia, before, during and after the planned May 1999 parliamentary elections. USAID will support a major initiative to enhance the capacity of the mass media to engage in independent news reporting and analysis, and to function as a medium of public service programming.

Proposed Action Areas:

USAID assistance is expected to support:

- drafting and passage of new laws that protect the freedom and independence of the media, including licensing, anti-trust measures, appropriate guidelines for media regulation;
- political party access to the media in election campaigning;
- public service programming;
- print and broadcast journalist training, particularly in news production about critical transition issues; and
- building professional organizations to advocate on behalf of the media, and strengthen standards of accountability and professionalism within the sector .

3. Promote NGO Advocacy

During the entire strategy period, civil society will continue to assert itself in Indonesia's political transition, contributing to the debate about the ground rules for the election process, monitoring the performance of the Election Commission in administering the election, questioning the new government's policies, and challenging the implementation of government programs. Assistance will help liberalize labor laws and support dialogue among labor, business interests, other elements of civil society, the government and military. Taking advantage of a more favorable environment for civil society development, USAID will redouble its support for NGOs addressing human rights, free speech, women's, children's, and laborers' rights, and advocating religious tolerance and reconciliation; and providing civic and electoral education.

USAID will utilize new indigenous NGOs at the regional and local levels and in various sectors (e.g., business and professional associations) to implement these activities. An additional and important element of USAID's effort to strengthen the role of indigenous NGOs is assistance targeted specifically to develop the institutional capacities of NGOs. USAID will finance improved institutional management systems and leadership development.

Proposed Action Areas:

USAID will support activities to:

- establish self-regulating mechanisms for NGO standards of professionalism, accountability, transparency and linkages with their constituents;
- assist new public interest associations to develop their constituency base and to expand their capacity to interact with the public, government, political organizations, and in coalitions with other NGOs; and
- support independent unions to enhance their capacity to play a constructive role in Indonesia's political transition and economic recovery.

4. Improve Public Governance and Facilitate Decentralization

Vastly improved public governance is essential to a successful and sustained democratic transition. Governance in Indonesia is highly centralized in the executive branch, and few checks and balances emanate from either the legislative and judicial branches, or from regional or local governments. There are few avenues to ensure transparency, responsiveness and accountability in government and there is ample opportunity for corruption at all levels.

If the national elections are successful and establish a widely accepted government, USAID will review how best to use its resources over the longer term to assist with reorienting the major institutions of governance. Assistance is expected to include:

- Facilitating decentralization. More effective, responsive and accountable governance requires that real authority and revenue generating capacity be transferred to regional and local governments. In the event a new government decides to increase the authorities of local governments, USAID will provide advisors to relevant ministries and local governments, support civil society/media efforts to promote devolution, and assist in decentralizing financial management.
- The national parliament. Indonesia's post-election parliament may play a more active and independent role in initiating, analyzing and debating legislation. If so, USAID would provide assistance to strengthen the parliament's ability to carry out its legislative and oversight functions.
- The judicial system. USAID will explore how to channel assistance for legal and judicial reform over the longer term. If the new government shows little interest in legal system reform, USAID will expand its assistance for mediation, arbitration and alternative dispute resolution as vehicles for adjudication of labor and agrarian disputes, consumer protection and bankruptcy.
- Civilian control of the military. Given the central role ABRI has played in Indonesian politics since independence, the military's support is critical for peaceful and lasting transition. USAID will support civil/military dialogue on civic/human rights, democratic/legal reform and the role of the military in a democratic society, especially in East Timor, Irian Jaya, and Aceh. These areas harbor independence movements, and the potential for further human rights abuse is ripe.

C. STRATEGIC OBJECTIVE: SPUR ECONOMIC RECOVERY, LAUNCH INSTITUTIONAL REFORM AND RESTORE INVESTOR CONFIDENCE

USAID will concentrate on urgent actions to spur economic recovery and restore investor confidence in the economy, coupled with other assistance that, over a longer term, will strengthen economic and financial governance.

Rationale: Successful implementation of this strategy will be challenging. It is not merely a matter of getting the right technical fix to a specific financial system question, but also of getting it adopted by the government, understood by the bureaucracy and broadly supported by the public. Much of the Indonesian economic and political culture is suspicious of capitalism, sympathetic toward state interventions and narrowly nationalistic. Within the Habibie administration, no clear center of gravity has emerged for identifying key policy issues, assessing options, building consensus on agreed programs, and effectively overseeing implementation. Outside the GOI, the tenure and authority of the current administration are widely and publicly debated, and policy statements are often viewed skeptically. Despite the urgency of the economic crisis, many do not believe the GOI has the technical understanding, commitment or political authority to provide the leadership necessary for an effective reform program.

Effective and quick economic recovery in Indonesia requires sound macro-economic policy, bank restructuring, bank supervision, and bank re-capitalization. In the immediate term, USAID's objectives are to bring about a framework and methods to support private sector workouts and corporate restructuring. To sustain a recovery, USAID's assistance will help improve accounting policies and standards in the public and private sectors, strengthen strategic management and risk analysis in the banking system (through AERA), strengthen capital market implementing and oversight institutions (through AERA), and expand and strengthen financial instruments (such as national government, corporate, and local government bonds). Additional legal and regulatory reforms will be required to support proper economic governance in such areas as investment, intellectual property, and contract laws. More importantly, a series of institutions will need to be created or strengthened to support application and enforcement of these laws and regulations. Among the most critical are commercial courts and other institutions that support bankruptcy, secured transactions laws, and an independent commission to support competition law.

Proposed Action Areas:

- In close coordination with the U.S. Treasury and major multilaterals (the IMF, the World Bank, and the ADB), USAID will provide technical assistance to the Indonesian Bank Restructuring Agency (IBRA) and Bank Indonesia (1) to strengthen the bank supervision system and eliminate the kinds of abuses that contributed to the current crisis and (2) to improve macroeconomic policy.
- USAID will continue its support to the Indonesia Debt Restructuring Agency (INDRA), which is a vehicle for supporting debt workouts by private sector companies, and to the Jakarta Initiative, which promotes alternative dispute resolution mechanisms to foster private debt workouts. Assistance would target legal and regulatory reforms to address asset ownership, transfer rights, and new procedures governing bankruptcy proceedings to support corporate workouts.
- USAID will support NGOs, including special interest associations and universities, think tanks, and research and development organizations in their roles as watchdogs and sources of technical analysis in order to foster continued economic reform in Indonesia. This assistance will help establish linkages between Indonesian NGOs with American counterparts to

strengthen their capacity (1) to analyze critical issues and improve the quality of the public dialogue on economic issues and (2) to prompt critical changes in monetary policy, exchange rate regimes and fiscal policy as well as in other key areas such as bankruptcy, secured transactions, competition policy, and arbitration, which are needed to support corporate and financial restructuring.

D. STRATEGIC OBJECTIVE: ASSIST INDIGENOUS NGOS AND LOCAL GOVERNMENTS TO LAUNCH REFORMS THAT WILL STRENGTHEN ENVIRONMENTAL MANAGEMENT

Rationale: Indonesia's economic crisis and political transition have brought increased stress on the environment. Virtually all government resources for national parks and protected areas has been eliminated. In addition, just as corporate interests are increasing their exploitation of Indonesia's natural resource base to generate foreign exchange, millions of households are turning to marginal forests, coastlines, and protected areas (a critical part of Indonesia's traditional "social safety net") to supplement their collapsing incomes. Poor management of these resources could seriously undercut Indonesia's longer-term development prospects and threaten long-term interests in biodiversity conservation. The GOI must also find ways to ensure that, despite the crisis, its people retain access to piped, potable water.

On the other hand, the crisis and political transition provide previously unavailable opportunities to support fundamental reforms that will move both the management of natural resources and the energy sector onto a more sustainable footing. For example, Indonesia now has the opportunity to replace its closed and generally corrupt system of allocating and exploiting forest resources with one more open, decentralized and accountable, thus ensuring decisions about the use and conservation of resources are made in a more transparent and democratic manner. Given the demonstrated political sensitivity and great potential for destabilizing social unrest over the prices of electricity and petroleum products and the inability of the GOI to sustain its subsidy program, the GOI must embark on a series of major policy and structural reforms, including a judicious move toward privatization.

Proposed Action Areas:

- To conserve and protect Indonesia's natural resources, USAID will continue to assist indigenous NGOs and local and national governments to:
 - map, assert, recognize and protect traditional land (and sea) use claims from corporate encroachment;
 - develop and monitor IMF-sanctioned forest sector reforms.
 - develop alternative income sources in coastal areas hardest hit by economic recession and climate change, such as micro-enterprise initiatives on seaweed processing, ecotourism, prawn aqua-culture rehabilitation, aquarium fish collection and the adoption of non-destructive fishing practices; and
 - ensure that new investments are properly designed, located and managed to ensure long term sustainability.

- USAID will also develop public-private partnerships that will:
 - engage local communities and business groups in governance of protected areas; and
 - explore the feasibility of debt-for-nature swaps to supplement financial and management resources and drive substantive changes in protected area governance.
- In collaboration with the World Bank, USAID will help the GOI to (1) develop and implement the legal and regulatory reforms needed to restructure the electricity sector; (2) formulate the policy and implementation plan to restructure the “downstream” portion of the oil and gas industry; and (3) develop a limited subsidy strategy and implementation plan to help allocate limited GOI resources for energy subsidies to the most needy target populations.
- To ensure continued access to water, despite increasing financial distress of municipal water companies, USAID will finance technical assistance to improve their efficiency in operating water pumps and use of chemicals, minimizing water loss, and strengthening the management of their finances.

III. Other Considerations

A. CROSS-CUTTING ISSUES

Four critical themes permeate USAID’s strategy: *strengthening the role of indigenous non-governmental organizations (NGOs), in particular with respect to the three following themes; supporting and strengthening transparency and anti-corruption efforts; supporting the role of women in development; and promoting decentralization of governmental authority.* By ensuring these themes are addressed in each area of the strategy, USAID expects to magnify the impact achieved by its assistance activities.

1. Strengthening Indigenous NGOS

NGOs are a key link to grassroots needs and issues and an effective channel for ensuring community needs are known and addressed. Consequently, in Indonesia USAID historically has relied heavily on a wide range of NGOs to implement its activities in virtually every sector of its portfolio. In fact, USAID is recognized within the donor community as a leader and innovator in its assistance for indigenous NGOs. USAID will continue and expand this long-standing collaboration with the NGO community.

USAID programs work with NGOs in three closely related and mutually reinforcing ways. *First*, our programs support NGOs that deliver services to people or help make service delivery more effective. In connection with employment generation, Indonesian community-based organizations will help local governments and communities identify appropriate labor-intensive infrastructure projects and recruit unemployed workers to supply the labor. Muslim, Christian,

and women's NGOs will support USAID's efforts in food assistance by organizing income-generating activities that can be funded by monetized food.

Second, USAID is supporting efforts of Indonesian NGOs to assume an active monitoring and oversight role in order to increase transparency and public accountability. For example, USAID will support groups that provide public oversight to limit corrupt practices and promote transparency, equity and fairness in the economic system as well as NGOs that advocate better corporate behavior, more open public procurement procedures and fairness in the parliamentary and presidential elections.

Finally, USAID supports NGOs that address the inter-related problems of economic recovery and democratic transition, for example, by encouraging the emergence of a transparent, inclusive, participatory and well-informed public dialogue on key issues of economic reform.

A key companion to the assistance on these substantive issues is USAID's assistance to enhance the capacities of NGOs in strategic planning, advocacy, resource mobilization and organizational management. In this way, USAID can leave behind a more sustainable framework for a vigorous civil society in Indonesia.

2. Promoting transparency in decision-making and anti-corruption

Corruption in Indonesia has deep roots and is commonplace in almost all sectors and all state and political institutions, from minor transactions to major contracts. Corruption is not simply routine but often a recognized method of augmenting meager resources to allow routine work to be accomplished. This incorporation of corrupt practices into the routine of government operations often moves it beyond a matter of personal greed to an unspoken but widely understood, accepted and even necessary requirement. Eliminating this culture of corruption is critical to creating a new and higher standard for public and corporate governance.

Attitudes in Indonesia towards corruption are beginning to change, however. The financial and economic crisis and Soeharto's resignation have provoked public condemnation and opened the possibility of bringing this previously unspoken practice into the open. Although much of the current attention and debate has focused on investigating and possibly recovering the ill-gotten gains of the Soeharto family and its friends, there are also new opportunities to address systemic corruption. Indonesian NGOs are jumping into the fray with a great deal of enthusiasm with the encouragement of the newly liberated mass media.

USAID's involvement in resisting corruption is focused on areas where USAID has considerable experience: legal reform (including competition law, privatization and government procurement policy) and support for civil society (including the media). USAID will continue to look for synergies between different strategic objectives, such as the collaboration between economics and urban and rural environmental management teams to dissolve monopolies and marketing cartels.

USAID will also actively search for opportunities to coordinate anti-corruption efforts with multilateral and bilateral institutions since it is important for the donor community to present a united front and a common message to whatever new government assumes power in the months

ahead. The World Bank's recent emphasis on anti-corruption, leading to the public dismissal of 18 officials who were misappropriating World Bank funds in the Ministry of Education and Culture, suggests that there is new receptivity to a common approach. This is reinforced by the recent OECD accord on anti-corruption which for the first time provides a common policy framework among donor nations.

3. Women in Development (WID)

Women were some of the main beneficiaries of Indonesia's long economic expansion over the past decades. For example, since the 1980s, women provided a large part of the formal labor supply in the country's rapidly growing export-oriented economy -- up to 80 percent of the workforce in export processing zones. Just as they were early beneficiaries of economic expansion, however, women have been hardest hit by the rapid economic contraction, often the first to be laid off as factories reduced workers. As societal tensions rise due to political and economic pressures, women and girls bear the brunt in terms of physical abuse inside as well as outside the household. Crisis centers report there has been a sharp increase in domestic violence. Widespread violence against women, including rape, occurred during the May 1998 riots.

Specific attention to gender issues in the context of framing a crisis response is essential if we are to ensure women remain central participants in and beneficiaries of Indonesia's economic recovery and development. USAID's employment generation assistance will develop approaches for ensuring women's participation and that women benefit from infrastructure and other assets created by public works. USAID will also finance a WID Advisor for the GOI's Planning Ministry who will ensure gender issues are addressed in the design, planning and implementation of the Padat Karya program and that women benefit from assets created in the future by the program. At the same time USAID will explore other employment generation measures (such as credit guarantees) to support small and medium enterprise (SME) employment opportunities for women.

Health and nutrition needs of mothers and children are receiving particular attention to minimize the lasting societal impact that deficient nutrition and health can have. USAID's support for the election process will include special programs to ensure that women are given an opportunity to participate fully. Finally, to the extent possible, USAID will disaggregate data collected in routine monitoring so that it can track the differential gender impact of its projects and, where necessary, make appropriate adjustments to ensure that women's needs are more adequately addressed.

4. Decentralization

Increased decentralization is a critical stepping stone for Indonesia's continued political evolution and transition and efforts to broaden citizen participation in and oversight of public governance. USAID has long worked on decentralization and will continue to do so.

Recent changes in laws concerning local government and local government financial management give more authority to local governments in managing their resources and affairs. In order to ensure these new developments contribute to real decentralization, USAID's assistance will promote continued fiscal decentralization, provide management training to local

government officials with new responsibilities, promote participation of local communities, and increase local officials' accountability to their constituents. In a more immediate time frame, USAID will provide technical assistance to urban local governments to enhance their ability to continue to deliver critical urban services despite the economic crisis.

In addition to strengthening the role of local governments, there is also an unprecedented opportunity to improve and expand NGO involvement in the management and delivery of health services at the community level, an approach which USAID will support.

B. DONOR COORDINATION

The donor community in Indonesia can be broken into two distinct groups: (1) those with programs of nearly \$1.0 billion and more yearly; and (2) those with annual programs and budgets of around \$250 million and less. Multilateral organizations -- the IMF, WB, ADB and Islamic Bank -- and the Japanese bilateral program constitute the big donors. USAID is the largest contributor in the group of smaller donors, which also includes the EU, the bilateral programs of Australia, Germany, Britain, France, Italy, the Netherlands, Canada, New Zealand and South Korea, and private U.S., German and Dutch foundations.

USAID's influence within the donor community is substantial. Since the USG holds the largest capital and voting positions at the IMF and WB, and significant sway at the ADB, these institutions listen to U.S. interests and seek to collaborate with USAID whenever possible. As the largest of the smaller donors, USAID maintains a leadership role within this group and frequently represents it when dealing with the multilateral institutions. There is close and mutually beneficial coordination with the large Japanese assistance programs. USAID's overall influence is further reinforced by the knowledge and relative continuity of its staff, strong influence with the GOI, and long history in Indonesia.

In the DG sector, USAID has been, and expects to remain, the largest and most active donor. However, UNDP will take the lead in coordinating direct election support for the GOI. When dealing with social safety net concerns, USAID works closely with other donors (1) to monitor and survey needs; (2) to ensure coordinated programming of resources; (3) to avoid overlapping and redundant provision of assistance; and (4) to leverage other donor resources. In the economic sector, the IMF is underwriting much of Indonesia's broad economic reform measures, and the WB and ADB have major ancillary programs. USAID's technical assistance on financial system and corporate restructuring and macroeconomic reform has been designed in collaboration with these major donors while taking into account USG interests and the long-term needs of Indonesia.

IV. SUMMARY

USAID has adopted a focused, yet flexible, strategy covering the period FY1999 to FY2003 in order to respond to Indonesia's severe political, economic and social crises. This strategy supports the USG's short-term goal to restore stability to a key ally as well as longer term foreign policy goals, namely

- Increasing adherence to democratic governance and respect for human rights

- Improving economic growth and expanding income distribution
- Protecting human health and reducing the spread of infectious diseases
- Stabilizing population growth
- Promoting responsible environmental policies and practices prevent from environmental degradation
- Preventing or minimizing the human costs of conflict and natural disasters
- Expanding U.S. exports
- Promoting U.S. economic prosperity by opening foreign markets

New implementation partners have been embraced with the number of indigenous NGOs receiving USAID assistance expected to reach 200 during FY 1999. USAID is playing a leadership role within the donor community in areas critical to Indonesia's recovery and transition, e.g., promoting and strengthening the role of an independent media and laying the foundation for robust support for elections planned for 1999. Moreover, USAID has moved beyond the limits of its bilateral program to assume a leadership role in drafting a regional initiative (AERA) which targets additional assistance to support critical economic needs, governance reforms and small business stimulus activities as well as social safety net policy and program development, all with the intention of ensuring the USG responds aggressively and meaningfully to the needs of a key ally.

APPENDIX A: Abbreviations/Acronyms

ABRI	- Indonesia's Armed Forces
ADB	- Asian Development Bank
AERA	- Accelerated Economic Recovery in Asia
AIDS	- Acquired Immune Deficiency Syndrome
APEC	- Asian Pacific Economic Conference
ASEAN	- Association of Southeast Asian Nations
BAPPENAS	- National Development Planning Agency
BI	- Bank Indonesia
BKKBN	- National Family Planning Coordinating Board
BULOG	- National Logistics Agency
CARE	- Cooperative for Assistance and Relief Everywhere
CBS	- Central Bureau of Statistics
CRS	- Catholic Relief Services
DG	- Democracy and Governance
EU	- European Union
GOI	- Government of Indonesia
IBRA	- Indonesian Bank Restructuring Agency
ILO	- International Labor Organization
IMF	- International Monetary Fund
INDRA	- Indonesian Debt Restructuring Agency
MDB	- Multilateral Development Bank
MOH	- Ministry of Health
MPR	- People's Consultative Council
NGO	- Non-governmental Organization
OTI	- Office of Transition Initiatives
PECC	- Pacific Economic Cooperation Council
PVO	- Private Voluntary Organization
SME	- Small and Medium Enterprise
STI	- Sexually Transmitted Infections
UNDP	- United Nations Development Program
USG	- United States Government
WB	- World Bank
WFP	- World Food Program
WID	- Women in Development

APPENDIX B: USAID ASSISTANCE TO INDIGENOUS NON-GOVERNMENTAL ORGANIZATIONS

While USAID/Indonesia has supported Indonesian non-governmental organizations (INGOs) in virtually every sector of its portfolio over the past 30 years, the fall of Soeharto and the wave of reform sweeping Indonesia have produced remarkable new opportunities for collaboration. The importance of INGOs has never been greater--they are critical to the democratic and economic transition currently underway. They provide a voice to Indonesians shaping the transition, train and support those articulating change, offer services to those in need, and do the monitoring to ensure reforms are implemented.

Under its crisis strategy, USAID is expanding its work with INGOs and community organizations throughout the country. We are providing technical assistance in institutional strengthening and extending financial support to new INGOs as well as creating new programs with existing partners. A common concern is that most of the new indigenous organizations may be long on commitment but are short on implementation and management skills, constraining their ability to absorb and effectively apply new funds. Thus, a major thrust of our program is to engage our local partners in carefully targeted training in financial management, advocacy, communications and other technical skills. In the case of the more than 30 small grants to date under OTI's program, institutional strengthening is an integral part of the grants issued through the three large "umbrella" NGOs. The natural resource management program, to cite another example, works through U.S. based NGOs in a continuing process of local NGO capacity building through training, mentoring and skills transfer.

USAID's current goal for FY 1999 is to provide support to more than 200 INGOs, and this number is expected to increase over the coming year. In FY 1999, we plan to allocate over half the USAID budget to support INGOs and other Indonesian community organizations. USAID/INGO collaboration includes a wide number of areas:

Economic Recovery: The dramatic political changes of the past several months have created opportunities for INGOs to engage with the Government of Indonesia (GOI) as never before. USAID is now supporting INGO participation in policy dialogue on economic legal reform with the GOI in the areas of financial regulation, banking and fiscal policy, competition law, corporate transparency, accountability and financial disclosure standards. USAID's economic recovery team also supports INGOs that provide public oversight and monitoring to identify and limit corrupt practices and promote transparency, equity and fairness in the economic system. Examples include:

- Supporting GOI, civic organizations, NGOs, university groups, and think tanks working on the removal of barriers to trade and investment, focusing on obstacles to free and open trade and fair competition for small businesses;
- Supporting partnerships between US NGOs and Indonesian universities, think tanks or NGOs to encourage discussion and debate on key economic reform issues;

Community and Civic Participation: This sector constitutes the greatest area for expanding USAID's support to INGOs. Drawing on both development assistance and international development assistance funds through the Office of Transition Initiatives (OTI), the Mission is providing extensive support to INGOs on human rights, violence against women, community participation, and legal defense and advocacy. It is developing--and has already launched--new programs with INGOs on voter education, election support, inter-ethnic relations media programs and strengthened civil military relations. In addition, we are working with INGOs with whom we have had programs in the past in new ways--funding environmental groups with a wide grassroots networks to do voter education. New mechanisms developed by OTI are facilitating rapid expansion of work with INGOs. In FY 98, through OTI, we were able to provide some \$4 million to 37 INGOs in less than three months. We hope to triple these numbers in FY 99. Highlights include:

- Grants to NGOs for democracy, civil society, human rights and work related to the elections;
- Establishment of NGO and donor working groups on the elections;
- Support for voter education, independent media and election management and administrative needs assessments;
- Support to local groups working on human rights and violence against women, with specific reference to the rapes of ethnic Chinese women in May;
- Support for NGOs working on investigating human rights abuses in Irian Jaya, East Timor, and Aceh;
- Support for election law reviews and discussions on election laws, procedures, and regulations to the GOI, NGOs and political parties;
- Support to media groups developing or reviewing laws governing freedom of expression, and;
- Expanded support to Indonesian umbrella organizations working on political reform.

Strengthened Environmental Management: USAID supports environmental INGOs working to empower local communities by strengthening their skills in land management and community organization so they can play an increased role in natural resource governance and management and in defining, arbitrating, and resolving local resource conflicts. With USAID funding, these groups are now using their networks to expand into voter education and election support. \$2.4 million went to 16 INGOs in FY 98 and this will increase to \$3.5 million in FY 1998 to support 20 INGOs. In addition, the USAID-endowed Indonesian environmental foundation KEHATI is supporting 200 INGOs active in biodiversity in FY 1998. Examples of INGO funded activities include:

- Support and strengthening of 15 Indonesian NGOs working to redress human rights abuses stemming from confiscatory land use practices;
- Technical assistance to local governments and NGOs to identify, articulate and arbitrate local natural resource conflicts; and
- Provide assistance to NGOs working to rewrite laws affecting natural resource use and management to eliminate sources of corruption and misdirected exploitation of natural resources.

Social Safety Net: USAID is supporting 15 regionally based, Muslim and women's INGOs and inter-ethnic community committees in distributing and monitoring Title II food commodities to the poorest communities. In addition, USAID will fund a block grant mechanism with \$2.7 million in local currency proceeds from the monetization of food commodities. The grants will go to INGOs for institutional strengthening and to support their food security and crisis-relief activities. USAID is also seizing this unprecedented opportunity to improve and expand INGO involvement in the management and delivery of health services at the community level. In employment generation, Indonesian community-based organizations will help local governments and communities to identify appropriate labor-intensive infrastructure projects using unemployed workers. In this broad sector, USAID supported 33 INGOs in FY 1998. These numbers are expected to double in FY 1999. Examples of INGO funded activities include:

- Technical assistance to municipal governments and local NGOs to develop public works. (220,000 person-days work created since March; an estimated 7,600,000 person-days of employment by March 2000);
- \$50 million in PL 480 Title II food through the World Food Program (WFP) and US NGOs working with Indonesian NGOs on the eastern islands, Kalimantan and central Java; over 83,000 tons of food commodities have been delivered. The food is for food-for-work programs, supplementary feeding of vulnerable groups and targeted feeding for the poor;
- Support to an Indonesian NGO to monitor food delivery to five major cities;
- Planning with USDA on distribution or monetization of up to 1.5 million tons of wheat through WFP and NGOs;
- Support for NGOs and local health providers on delivery of health and family planning services to meet crisis priority needs; and
- Support to NGOs and GOI working on prevention of sexually transmitted infections, including HIV/AIDS.