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Q1: Respondent details

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Q2: Country or Customs territory

- MULTILATERAL OR REGIONAL DEVELOPMENT BANK

Q3: Organization

Other (please specify) Regional Development Bank

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Q4: Title of case story

Indonesia: Improving Access to Finance in Aceh and North Sumatra

Q5: Case story focus

Infrastructure upgrading and the development of related services markets, including through support for investment climate reforms.

Q6: Case story abstract

The proposed Technical Assistance project (TA) will support the Government of Aceh and the Government of North Sumatra in developing integrated support to improve access to finance in Aceh and Nias. On the supply side, the TA will (i) provide support to enhance the capacity of the governments in Aceh and North Sumatra in managing the Microfinance Revolving Fund (MRF); (ii) assist local banks to develop new microfinance products, including Grameen-type products and suitable follow-on products, and (iii) support the Government of Aceh to develop sustainable Local Guarantee Cooperation to facilitate credit access of feasible borrowers. From the demand side, the TA will provide assistance, on a pilot basis, to the cluster of potential borrowers/producers to make them more bankable for more financial products. To encourage and sustain knowledge development in this area in the two provinces, the TA will involve local universities in the survey and training activities.

Q7: Who provided funding?

Other (please specify) Asian Development Bank

Q8: Project/Programme type

Single country

Q9: Your text case story

Although commercial banks have expanded their size and branch network significantly over the last 2 decades, close to half of Indonesia's population still does not have access to formal financial services. About one-third of the country's population does not save at all and can be considered financially excluded. Of those who save, about two-thirds use informal or semiformal non-bank institutions. The distribution of access to financial services across the country is also uneven, with places like Jakarta being over serviced relative to the rest of the provinces. Aceh, in particular, is significantly underserved. The amount of credit for working capital and investment relative to its gross regional domestic product is low at 7.8%, compared to the national average of about 32.1%. As a result, the cost of credit has been relatively higher in Aceh than in other provinces.

Micro, small, and medium-sized enterprises (MSMEs) dominate the business landscape in Aceh, providing 97.9% of total employment. While their numbers are still relatively small, most of the MSMEs are relatively new and many do not have an established track record with the banking system. They are in need of additional capital for expansion, but their access to capital has been constrained by the lack of collateral. The December 2004 tsunami and March 2005 earthquake also caused severe damage to Nias Island's infrastructure and economy, both of which were already weak prior to the disasters.

ADB provided assistance to support the recovery of the commercial microfinance system in Aceh and Nias Island under the livelihood and microfinance support (LMS)⁷ component of the Earthquake and Tsunami Emergency Support Project (ETESP). The LMS focused on rebuilding activities and introducing Grameen-type microfinance to the provincial government-owned rural banks and the private rural banks in Aceh and Nias Island.

The impact will be improved access to finance in Aceh and North Sumatra to widen economic opportunities for poor households. The TA will enhance the capacity of key stakeholders by improving the environment for the expansion of sustainable and commercially viable microfinance programs in Aceh and North Sumatra.

The TA is estimated to cost \$941,000, of which \$800,000 will be financed on a grant basis by JFPR and administered by ADB. The TA will be implemented over 24 months, from November 2012 to October 2014. MOHA, Director General of Regional Development, will be the executing agency. MOHA will transfer TA to the provincial governments of Aceh and North Sumatra as the implementing agencies through a direct grant mechanism. A steering committee comprising of officials from MOHA, Bank Indonesia, BAPPENAS, and the provincial Government of Aceh and the provincial Government of North Sumatra will be formed to oversee the implementation of the TA.

Q10: Lessons learnt

ADB provided assistance to support the recovery of the commercial microfinance system in Aceh and Nias Island under the livelihood and microfinance support (LMS) component of the Earthquake and Tsunami Emergency Support Project (ETESP). The LMS focused on rebuilding activities and introducing Grameen-type microfinance to the provincial government-owned rural banks and the private rural banks in Aceh and Nias Island. Under the LMS, ADB supported the merger of Aceh's provincial government-owned rural banks, allocated seed capital in the form of the Microfinance Revolving Fund (MRF), and provided training on the start-up of Grameen-type microfinance operations. Because there were no rural banks in Nias Island, Bank Sumut (the provincial development bank of North Sumatra) participated in the training activities. In addition, ADB provided assistance to pilot commercial microfinance to Bank BPD Aceh (the provincial development bank).

ADB's earlier support and subsequent efforts to enhance the rural banking system in Aceh and North Sumatra through LMS and MRF have provided a good base for improving credit expansion in Aceh. However, Aceh is still in the early stages of improving access to finance. Further progress is needed in a number of areas including (i) managing the MRF more productively, while ensuring its sustainability; (ii) enhancing the capacity in Bank BPD Aceh to develop additional microfinance products to suit new borrowers from qualified community clusters in agriculture, fishery, and other sectors; (iii) addressing the local risks affecting access to finance; and (iv) developing a more integrated approach by supporting the capacity of selected producers through community clusters for products such as tuna, patchouli, soft-shell crabs, and prawns. The project completion memorandum of the ADB-provided grant assistance suggests that capacity building needs to be sustained. The Government of Aceh and Bank Sumut have also requested further capacity building assistance from ADB.