



# Alleviating Poverty through Local Economic Development

## Lessons from Nusa Tenggara

*Oleh*

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# **Alleviating Poverty through Local Economic Development**

Lessons from Nusa Tenggara

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## **PROMIS-NT**

Poverty Alleviation and Support  
for Local Governance in the Nusa  
Tenggara Provinces

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## Foreword

To stimulate an increase in people's incomes, synergy between government and the private sector is essential, so that implementation of programmes matches local characteristics, conditions and potentials and responds to local problems.

The experiences in the effort to increase people's incomes presented in this book illustrate the dynamics of the process and the benefits of poverty reduction activities in the Provinces of NTT and NTB. A cooperation between the Indonesian and German governments, this programme has two components: PRODA (Support for Local Governance) and PNT (Poverty Reduction).

Finally, I would like to thank everyone who contributed for their support. I hope that these valuable lessons can be used as a reference and, as far as possible, be replicated in other regions of Indonesia.

Jakarta, December 2004

DIRECTOR GENERAL OF REGIONAL  
DEVELOPMENT

SEMAN WIDJOJO



## BUPATI DOMPU

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### **Foreword**

*Assalamu'alaikum Waramattullahi Wabarakatuh!*

Praise be unto to Thee Allah, the Almighty, for giving us the strength to keep on working to help our people who are living in poverty.

Poverty reduction is a regional development priority that all development actors in the regions make every effort to implement. Most of the potential funds from regional government and central government, as well as from overseas aid, is directed to developing sectors that are hoped will significantly increase the incomes of poor people, such as the agricultural, plantations, fisheries, and animal husbandry sectors. Despite this, it must be acknowledged that the results of what has been done so far have fallen short of expectations. For this reason, the district government of Dompus is committed to innovating development strategies for the sustainable well-being of the people of Dompus.

This book, "Alleviating Poverty through Local Economic Development: Experiences from Nusa Tenggara", which presents local economic development strategies as part of the technical cooperation between the Indonesian and German governments is written based on a sample of local economic development experiences in Nusa Tenggara in evaluating and revising local economic development strategies to be more comprehensive, which will ultimately support efforts to expand the job market and to reduce poverty.



To the authors, who have worked hard to complete this book, I thank you on behalf of the people of Dompu. Let us hope that works like this will be drawn on continually for the benefit of those in need.

*Wassalamu'alaikum Warahmatullahi Wabarakatuh.*

Dompu, 27 December 2004  
Bupati Dompu,

H. ABUBAKAR AHMAD, SH



## BUPATI BIMA

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### **Foreword**

*Assalamu'alaikum Waramattullahi Wabarakatuh!*

Praise to God, praise be to Thee Allah, Lord God Almighty, for His abundant mercy, love and guidance, allowing this book, “Alleviating Poverty though Local Economic Development”, to be completed.

Poverty is a problem that is very closely related to economic development policy. At the same time, we recognise that economic development now, and in the future, as well as facing the difficulties and challenges of global competition that relate to the development of strategic local and regional environments, is also greatly influenced by the dynamics of global competition. In this context, it is necessary to design balanced economic development policy that prioritises the use of local economic potentials, while taking into account global potentials and external resources as supporting factors. Local economic development is an economic development approach that emphasises the optimal use of local resources based on the three pillars of attractiveness, resilience, and competitiveness.

Regional governments are working as hard as possible to facilitate the creation of conditions conducive to the emergence of healthy competition, while promoting the growth and development of local initiatives and innovations in order to enable the optimal and proportional use of the potentials of available natural resources for the well-being of the people and the development of the region.

Publication of this book is an Indonesian-German cooperation, a result of the concern GTZ PROMIS-NT has for the development of Nusa Tenggara, including the



district of Bima. This book discusses local economic development strategy based on real local conditions, on empirical experiences in implementing local economic development programmes in the region. Therefore, on behalf of the local government and people of Bima, I would like express my sincere gratitude and appreciation to GTZ PROMIS-NT and the editorial team for contributing their thoughts.

This book should become a reference for regional government work units in explaining the principles of local economic development in regards to efforts to exploit existing potentials.

Finally, let us hope that this book will be of great benefit in further developing the Nusa Tenggara region in general and the district of Bima in particular. Amen.

*Wabillahitaufiqwalhidayah Wassalamu'alaikum Warahmatullahi Wabarakatuh.*

Raba-Bima, December 2004  
Bupati Bima,

Drs. H. ZAINUL ARIFIN



## **Content**

<b>Foreword</b>	i
<b>Foreword - Bupati Dompu</b>	ii
<b>Foreword - Bupati Bima</b>	iv
<b>Content</b>	vi
<b>CHAPTER I - INTRODUCTION</b>	1
1.1 Background	1
1.2 An Overview of Local Economic Actors and Institutions	2
1.3 Scope and Focus	3
<b>CHAPTER II - STRATEGIC CHALLENGES AND GENERAL PERSPECTIVE OF LOCAL ECONOMIC DEVELOPMENT AND POVERTY ALLEVIATION</b>	4
2.1 Strategic Challenges	4
2.2 General Perspective	8
<b>CHAPTER III - LOCAL ECONOMIC DEVELOPMENT STRATEGY</b>	13
3.1 Working Definition of the Local Economy Approach	13
3.2 General Framework of Local Economic Development Strategy	14
3.3 Major Components of Local Economic Development Strategy	18
<b>CHAPTER IV - THE PROMIS-NT EXPERIENCE AND RECOMMENDATIONS</b>	37
4.1 Important Experiences	37
4.2. Recommendations for the Future	39
<b>Bibliography</b>	41



## CHAPTER I

### INTRODUCTION

#### 1.1 Background

With the emergence of global awareness of the need to reduce the number of the world's poor by 2015, the governments of several countries together with international and national organisations have been developing strategies and approaches that will be implemented to achieve this goal. One international organisation that is concerned with measures for reducing poverty is GTZ, a German organisation for international technical cooperation. In Nusa Tenggara, through a programme called "Poverty Alleviation and Support for Local Governance in the Nusa Tenggara Provinces" (PROMIS-NT), GTZ works to build the capacity of local governments, local parliaments, and non-governmental organisations to carry out poverty alleviation tasks in an autonomous and effective way. PROMIS-NT also facilitates cooperation between the public and private sectors in the context of local economic development.

PROMIS-NT is implemented in two provinces of Indonesia, the province of West Nusa Tenggara (*Nusa Tenggara Barat* – NTB) and the province of East Nusa Tenggara (*Nusa Tenggara Timur* – NTT). These two are among the poorest of Indonesia's provinces, with around 27.5% of the 7.5 million population of Nusa Tenggara living below the poverty line (National Social Economic Survey, 2000). Most of these poor people depend on the agriculture and fisheries sectors for their livelihoods. Yet, in general, these farming and fishing activities are done on a small scale using traditional methods.

This poverty is a dilemma that has various causes and consequences. Natural resource conditions such as poor soil fertility, lack of water due to low precipitation and uncertain distribution of rainfall, limited access to irrigated land, and crop pests and diseases are the most serious challenges faced by people living in NTB and NTT. Besides these natural factors, poor people and micro and small & medium enterprises (SME) have limited access to capital and productive land, lack adequate physical and social infrastructure, and have insufficient access to services and information. These, and various other social cultural factors, are key factors



## **Alleviating Poverty through Local Economic Development**

Lessons from Nusa Tenggara

preventing poor people and small and medium entrepreneurs from extricating themselves from the trap of poverty and social underdevelopment.

Meanwhile, although regional autonomy, which was implemented in Indonesia in early 2001, has given the people more space for political participation in policy making and development programmes, the economic and social gap remains. While regional autonomy is a necessary precondition towards better and more equal welfare for the people, this alone is not sufficient. To achieve these goals requires a political economy that consistently supports the people's economy together with coherent strategies to promote the integration of poor people into productive enterprises and the market.

### **1.2 An Overview of Local Economic Actors and Institutions**

The "Poverty Alleviation and Support for Local Governance" programme, which is known as PROMIS-NT, links poverty alleviation directly with policy dialogue and good governance. This programme is the result of the combination of two previous projects, "Self-Help Group Oriented Poverty Alleviation" and "Support for Local Government". PROMIS-NT is implemented by the Indonesian Department of Home Affairs and the German Technical Cooperation (GTZ) in cooperation with regional governments, local actors and the private sector.

Local economic development has become a cross-sector issue in the activities of self-help groups and in stakeholder discussions at the district level. Therefore, one focus of the programme is on processing and marketing agricultural products for self-help groups that are funded through the German government Action Programme 2015 for poverty reduction. Since 2002, several pilot activities to identify local economic potentials and facilitation of dialogue between the public sector, private sector and the people's economy sector have been carried out in pilot locations, in the Districts of Bima and Dompu.

The major actors in local economic development are district/municipal government institutions, provincial and national government, local business people – for the most part minority Chinese and Arabs, chambers of trade and industry, and local producers including farmers and fishers and small craft industries, most of whom are native to the area. Other general features of the local economic environment in NTB



and NTB are: (i) public sector domination of local economic development; (ii) much overlapping of responsibility in the public sector; (iii) unreliable checks and balances functions of local parliament; (iv) weak position of business associations; (v) orientation of not-for-profit non-governmental organisations leans too far towards government and their own interests; and (vi) poor performance of producers associations and cooperatives in rural areas.

### **1.3 Scope and Focus**

This paper was compiled as a supplementary reference for decision-makers and economic development service organisations in underdeveloped areas, above all in the east of Indonesia. This paper contains a brief description of conditions and changes in the strategic environment at the regional-global level that may affect and stimulate the development of pro-poor<sup>1</sup> economic development policies and strategies in the regions. In this context, this paper offers several key elements of local economic strategy that could be translated in a flexible way by the underdeveloped regions of eastern Indonesia in the form of sustainable action programmes. As well as recommendations for changes in regional development paradigms, this paper also links three cornerstones of local economic development: (i) increasing attractiveness; (ii) increasing resilience; and (iii) increasing competitiveness.

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<sup>1</sup> See topic 3.2 in Chapter III.



## **CHAPTER II**

# **STRATEGIC CHALLENGES AND GENERAL PERSPECTIVE OF LOCAL ECONOMIC DEVELOPMENT AND POVERTY ALLEVIATION**

Indonesia has been experiencing a dynamic political and economic transformation, in which a process of rapid decentralisation that has brought devolution of power and responsibility to around 400 districts since January 2001. At the same time, a new fiscal system between central and regional government has also been introduced. Although implementation of regional autonomy has begun to open up the space for public participation in regional decision-making, development planning and budget control, regional governments, the private sector and civil society still face numerous challenges and difficulties in building a better, sustainable life. These challenges and difficulties are discussed in section 2.1 “Strategic Challenges”. Section 2.2 “General Perspective” discusses several key perspectives as part of the normative framework of local economic development.

### **2.1 Strategic Challenges**

#### ***2.1.1 Poverty and Unemployment***

Pro-poor development policies and strategies that were initiated soon after Indonesian independence and continued and intensified by the New Order government produced impressive results up until the time of the financial crisis that hit parts of Asia and Indonesia in mid-1997. Official reports in Indonesia show a drastic decrease in the number of poor in Indonesia during the period 1976-1996. In 1976, there were around 54.2 million poor people in Indonesia (40.1% of the total population). In 1981, it was reported that the number of poor people had fallen to 40.6 million (26.9% of the total population). In 1990, the figure had fallen to around 27.2 million (15.1% of the population), and by 1996 had dropped even further to 22.5 million or only around 11.3% of the total Indonesian population (Sumodiningrat,



2004)<sup>2</sup>. According to official government statistics (Sumodiningrat, 2004), around 76% of poor families live in rural areas and work in the agricultural sector, while the remainder live in urban areas and their main source of income is from outside the agricultural sector. Only around 25% of poor families in urban areas earn their livelihoods from the agricultural sector.

The financial crisis, which then developed into an economic crisis, and further a multi-dimensional, political and social crisis as well as a crisis of credibility, along with the factors that were its root causes, ultimately destroyed the headway made towards poverty alleviation in Indonesia since the mid 20th century. An economist from the University of Indonesia, M. Chatib Basri, estimates that around one-third, and even up to one half, of the Indonesian population is still vulnerable to poverty<sup>3</sup>. Inadequate access to education, health and environment could cause them to slip back into poverty. They exist just above the poverty line, and are therefore very vulnerable to price changes.

Today, around 16 million people or about 7.5 percent<sup>4</sup> of the Indonesian population are living below the poverty line set by the World Bank, which is defined as living with a purchasing power of less than 1 US dollar a day. But the number of Indonesian people vulnerable to poverty, that is those living on less than 2 US dollars a day, is reported to be far higher, at more than 110 million people or around 53% of the population (Soedjito, 2004)<sup>5</sup>. In the 2004 Human Development Report on Indonesia, the country's HDI (Human Development Index) ranks 111th out of 177 countries<sup>6</sup>. This indicates that the results of development achieved by Indonesia in terms of increasing the standard of living of its people fell behind that of a large number of other countries. Furthermore, there was a significant gap in human development between regions. The human development indices range from 76 in East Jakarta to 47 in the District of Jayawijaya. Another indicators also related to human

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<sup>2</sup> Gunawan Sumodiningrat. 2004. Perkembangan strategi penanggulangan kemiskinan (Developing a poverty alleviation strategy). This paper was presented at a workshop on Sharing Local Experiences in Poverty Alleviation held at Sanur Paradise Plaza Hotel Denpasar, Bali, July 2-4, 2004, jointly organised by the National Development Planning Agency (Bappenas), The World Bank, GTZ and DFID.

<sup>3</sup> Kompas, July 26, 2004: p 1.

<sup>4</sup> Source: Kompas, November 1, 2004, p 15.

<sup>5</sup> Soedjito, B. Bintoro (2004). Decentralization and poverty reduction: from lessons learnt to policy action-the case of Indonesia. A paper presented at a workshop jointly organized by the OECD Development Center and the Development Cooperation Directorate, OECD Headquarters, Paris, September 29-30, 2004.

<sup>6</sup> Source: [http://hdr.undp.org/statistics/data/country\\_fact\\_sheets/cty\\_fs\\_IDN.html](http://hdr.undp.org/statistics/data/country_fact_sheets/cty_fs_IDN.html).



## Alleviating Poverty through Local Economic Development

### Lessons from Nusa Tenggara

development is the Gender Related Poverty Index (GDI)<sup>7</sup> that according to a recent UNDP report the GDI for Indonesia is ranked 90th out of 144 countries, far below neighbouring countries such as Malaysia, which is ranked 52nd, and Thailand, the Philippines and Vietnam, which are ranked 61st, 66th and 87<sup>th</sup> respectively. Gender issues are sensitive, cross-sector issues, which if not managed properly can upset social dynamism and investor interest.

Poverty and unemployment are two sides of the same coin. At least 10 million people are reported as being without work, and if people without full-time employment are included, the figure rises to around 40 million<sup>8</sup>. Job creation presents a huge challenge for Indonesia at a time when it has yet to fully recover from the multi dimensional crisis. With the elasticity of demand for labour over recent years, in which economic growth of one percent created job opportunities for only 400,000 people<sup>9</sup>, to eradicate unemployment would require economic growth of more than 6.5% p.a. for the next five years, which would of course require enormous investment way beyond the current fiscal capacities of this country.

### **2.1.2 Natural Resource Degradation**

Indonesia's forests are estimated to be disappearing at a rate of at least 1.5-2 million hectares a year as a result of clear cutting by companies with forest management permits as well as illegal logging and shifting cultivation. Re-greening and forest rehabilitation programmes, and law enforcement measures, have not been able to offset such a rapid rate of deforestation. As well as flaws in programme design and implementation, there are many basic problems, which include a general perception that the structure of control of natural resources is unfair due to policies which are biased towards large corporations and tend to disregard communal property rights, due to scarcity of land for crop agriculture, the half-hearted efforts of those in power to uphold the law and justice at grassroots, and due to corruption, collusion and nepotism that is still prevalent in the management of forest resources, and so on. The problem becomes even more complex when deforestation is followed by degradation of land, which in turn causes damage to downstream and coastal ecosystems.

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<sup>7</sup> GDI is measured based on figures for life expectancy, literacy, participation in school, and real GDP per capita for men and women (see [http://hdr.undp.org/statistics/data/country\\_fact\\_sheets/cty\\_fs\\_IDN.html](http://hdr.undp.org/statistics/data/country_fact_sheets/cty_fs_IDN.html)).

<sup>8</sup> Nitisastro, Widjojo (Kompas, August 4, 2004, p 13).

<sup>9</sup> Nitisastro, Widjojo, *Ibid*.



### **2.1.3 Regional-global Competition**

Today, trade liberalisation is a reality, even though some of the conditions and game rules are still being debated by the representatives of industrialised and developing countries, such as the domestic and export subsidies industrialised nations give to their farmers and the exporters of their agricultural products. This subsidy policy adopted by industrialised countries is seen as a serious threat to the competitiveness of the agricultural products of Indonesia and other developing countries. Although academic debate over the ideology of modern economic policy continues, and the anti-globalisation movement pioneered by certain economists, politicians and the civil society elite is gaining ground, the public perception that globalisation and economic liberalisation represent a new chance for economic development and poverty alleviation is becoming increasingly popular in Indonesia and other developing countries. The Indonesian government recognises that globalisation and liberalisation will create complex and risky economic playing fields, and for this reason decentralisation and deregulation policies are accompanied by measures to synergise efforts to protect and empower poor people and actors in the micro, small & medium enterprise sector (SME sector).

But, Indonesia still has relatively low investment attractiveness and is more vulnerable to the risks of economic globalisation and liberalisation compared with neighbouring countries such as Malaysia, Singapore, Thailand and Australia. The World Investment Report 2004<sup>10</sup> places Indonesia at rank 139 out of 144 countries as destinations for global investment. As a comparison, Brunei Darussalam ranks second after Belgium and Luxembourg that share rank one. Another Southeast Asian country, Singapore, ranks sixth, while Malaysia is ranked 75th, Myanmar 85th, and Thailand 87th. Besides domestic conditions related to economic factors, the factors that most concern investors are security and the high level of corruption in Indonesia. Although Indonesia has begun to take more serious measures to eradicate corruption and uphold law, the perception of Indonesia as a country of high economic cost cannot be erased overnight. As well as persistent corruption, the large number of civil servants is one of the causes of inefficiency and high economic cost in Indonesia. A World Bank report<sup>11</sup> states that the initial cost of investment in Indonesia is higher than in any other ASEAN country, at 1,163 US dollars or around Rp 10,000,000. Also,

<sup>10</sup> For more details see Kompas, September 8, 2004, p 13.

<sup>11</sup> Source: Kompas, August 2, 2004, p 35.



## Alleviating Poverty through Local Economic Development

### Lessons from Nusa Tenggara

to obtain a business licence in Indonesia takes around 150 days, longer than in any other ASEAN country. As a comparison, the initial cost of investment in Malaysia is around 966 US dollars and a business licence is issued within 30 days, and in Thailand the cost is even lower, at 160 US dollars, and it takes around 33 days to obtain a business licence.

## 2.2 General Perspective

### 2.2.1 Indonesia's Economic Policy Vision

The realities of the financial and economic crisis demonstrated that the people's economy not only has an amazing resilience exceeding the expectations of leading economists, but has also been a factor in saving the national economy from "collapse". Learning from this experience, policy makers in Jakarta and in the regions as well as economists have, quite rightly, made the people's economy the backbone of the national economy and it is in this direction that policy and support is focused. This perspective is in accordance with the constitutional mandate of the 1945 Constitution, as stated in article 33.

Placing focus on the people's economy, which is largely micro and small & medium-sized enterprises, does not mean disregarding large-scale private sector enterprises. On the contrary, public policies and services should be more conducive for the creation of mutually beneficial partnerships between large companies and micro and small & medium-sized enterprises. One example of possible partnerships that has yet to be taken advantage of to any significant degree is the opportunity for cooperatives to have share ownership in public companies (state-owned enterprises) or in private companies, although the legal framework to support this is already in place. If the government were to facilitate cooperatives to obtain shares in public companies and private enterprises through a policy to strengthen the capital base of cooperatives, *for instance by reducing subsidies on refined fuel oil and fertilisers and using these funds instead for capital assistance for cooperatives as well as for health and education*, then poor people and owners of micro and small & medium enterprises who are members of cooperatives would gain larger profits from the chain of production and marketing of products and services. This in turn would have economic, social and environmental impacts on their lives. This is discussed in more depth in section 3.3 in Chapter III.



The academic debate over “growth-first strategy” and “development-first strategy” aside, we believe that high economic growth, at least in the mid-term (next five years), is crucial for Indonesia in order to reduce poverty and create new job markets.

With the perspective described above, the mission of the people’s economy should be focused on building agricultural-based rural industry. For regions in Nusa Tenggara, agricultural-based rural industry is particularly relevant and feasible. Optimal use has yet to be made of the potentials of coastal areas, where the fishing communities are dependent on trap fishing, seaweed and shrimp farming. Likewise, the potentials of agriculture in low-lying areas, as well as in upland areas around the forests. To realise pro-poor rural industrialisation, poor people urgently need greater access to economic resources through development of physical infrastructure for transport, energy and telecommunications and provision of incentives or direct subsidies for productive activities, as well as development of institutional infrastructure for the people’s economy at the local level, especially in Nusa Tenggara. Access to economic resources and infrastructure development are discussed in more detail in Chapter III.

But this target of high economic growth and rural industrialisation must not give rise to nothing but export-oriented policies that disregard domestic market potential. The 200 million or so Indonesian population is a vast market with diverse demands. Cooperation between regions in a spirit of nationalism and regional partnerships that have been established with neighbouring countries must continue to be pursued in order to create new business opportunities in the face of global competition. In the latter, regional governments and enterprises need to be more intensively involved. For their part, regional governments and enterprises need to be more active in giving information and input to central government, which facilitates regional partnerships with neighbouring countries. This concept of partnership is discussed in more detail in Chapter III in the section on Regional Partnerships.



## Alleviating Poverty through Local Economic Development Lessons from Nusa Tenggara

Deregulation and debureaucratisation in Jakarta and the regions, which is implemented through regulations that distort the market and rationalisation of the bureaucracy (both its structure and its personnel), is certain to create new business opportunities that will give value added for local communities and the regions<sup>12</sup>. Furthermore, a “national umbrella” (legal framework, vision, mission) for economic development is needed that can serve as guideline for the regions in order to create synergy in national development.

### **2.2.2 Regions that Develop, instead of Development of the Regions**

In the context described in section 2.1, the words “think globally, act locally” are becoming more and more relevant. Figure 1 below illustrates the local perspective in the regional-global context, focusing on the economic-business dimension, on attractiveness, resilience and competitiveness. Decentralisation policy based on Law 32/2004 and Law 33/2004 provides the legal basis for a local economic development strategy.

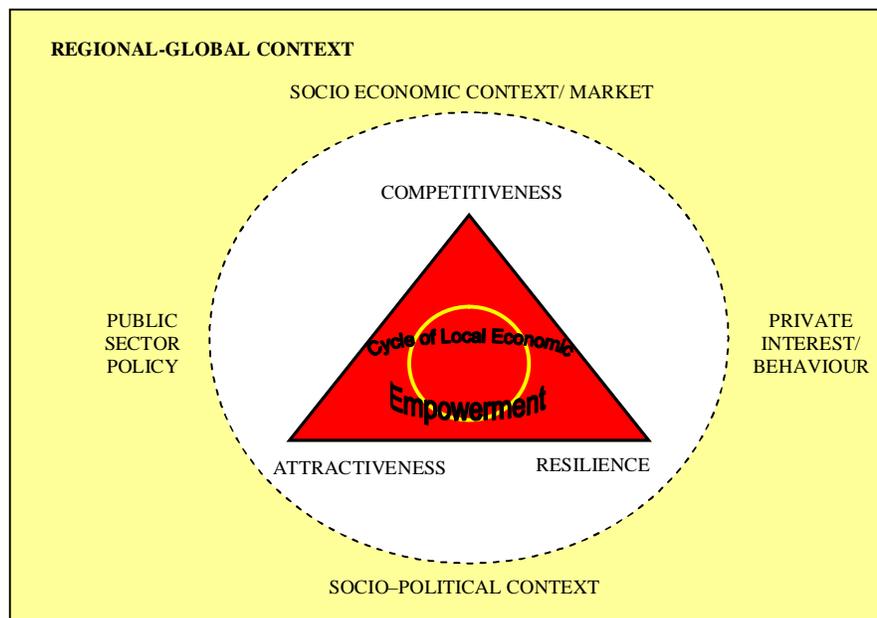


Figure 1: Context and Focus of Local Economic Development

<sup>12</sup> Dr. Birgit Kerstan discusses this perspective in the Bali Post, August 5, 2004, p 10.



Indonesia, with a population of around 207 million consisting of more than 300 ethnic groups, 700 languages and dialects, and a variety of religions constitutes a complex, conflict-prone reality. From the economic perspective, implementation of regional autonomy is expected to raise economic value added for local communities by increasing public participation in the market. Regional governments, the private sector and the local communities, of course, have better knowledge and understanding of the potentials of their regions. But reorganisation of the bureaucracy carried out by regional governments in the context of decentralisation has not yet proven to be effective and efficient in supporting local economic development. The bureaucracy that has been created is too “fat” and its personnel lacks the required capacity. In addition, regional governments in general concentrate above all on increasing regionally generated income rather than focus on products as a way of raising the region’s revenue/financial capacity. Policies focusing on regionally generated income are implemented by introducing various levies, in the form of tolls, taxes and other fees. These levies put off domestic and foreign investors, and deter poor people and entrepreneurs from starting up or developing businesses.

To be consistent with the principles of pro-poor economic development, regional governments should think not only about increasing regionally generated income but more so about how to expand the region’s fiscal capacity and expand the productive base of the people’s economy. In other words, strategy for increasing gross regional domestic product is more relevant than strategy for increasing regionally generated income. In the same vein, expanding the regional government’s fiscal base and building the capacity of planners in the regions in formulating economic policy is considered to be crucial to support developing regions. Synchronisation of development policy and planning between central and regional government should be improved, so that central government programmes in the regions financed by deconcentration funds can be carried out effectively and efficiently. So, a “national umbrella” or blueprint for economic development is needed that can serve as guideline for the regions in order to create synergy in national development.

In the developing regions perspective, increasing civil society access to and participation in the formulation of economic policy, development policy and fiscal control is important. Achieving this goal requires flexible regulations that grow and



## **Alleviating Poverty through Local Economic Development**

### Lessons from Nusa Tenggara

activate stakeholder dialogues at the village level through to the national level. Today, stakeholder forums have begun to appear in large numbers at the national level, but nearly all are to a high degree financially dependent on foreign donors.

In the same way, the potential of regional partnerships that aim at reducing transaction costs and obtaining economic value added for local communities and regional governments needs to be utilized effectively. From the economic perspective, regional autonomy is expected to encourage competition between regions in development, not regionalism of development. Regions need to think about joint planning and economic development forums. This topic is discussed in more detail in Chapter III.



## CHAPTER III

### LOCAL ECONOMIC DEVELOPMENT STRATEGY

#### 3.1 Working Definition of the Local Economy Approach

Section 2.2 discussed key arguments relating to the relevance of decentralisation, economic deregulation, and a local approach to economic development. This chapter discusses the scope and focus of the local economic development approach (section 3.1). This is followed by a general framework of local economic development strategy and its key principles (section 3.2), and a description of the main elements of local economic development strategy (section 3.3).

Although interest in the local approach to economic development is gaining ground in developing countries, a broad agreement of its definition has yet to be reached. But local economic development initiatives need not wait for such a definition since one may never be agreed on. More important is a working definition that can be used as a guideline and blueprint for programme scope. Local economic development should not be seen as exclusive, but as an integral part of regional development. Following is a description of the direction and scope of local economic development initiatives in the GTZ perspective<sup>13</sup>:

- Stimulate growth of local economies and create new job markets,
- Make the best use of available local resources,
- Create space and opportunities to balance supply and demand, and
- Develop new business opportunities.

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<sup>13</sup> See GTZ Local Economic Development position paper (draft 2004): What makes LED LED?



## Alleviating Poverty through Local Economic Development

### Lessons from Nusa Tenggara

As a comparison, the World Bank's definition of local economic development is: "... the process by which public, business and non-government sector partners work collectively to create better conditions for economic growth and employment generation."<sup>14</sup>

It can be concluded that local economic development is a process that forms partnerships between economic stakeholders, between regional governments, community based organisations and the private sector, in managing the resources available for creating job markets and stimulating the local economy. This approach emphasises local control, and utilises human, physical and institutional potentials. Thus, local economic development partnerships integrate efforts to mobilise actors, organisations and resources, while developing new institutions through dialogue and strategic activities<sup>15</sup>.

### 3.2 General Framework of Local Economic Development Strategy

Figure 2 illustrates the focus, elements and major principles of local economic development strategy, in parallel with Figure 1 in Chapter II. Local economic development focuses on achieving three inter-connected goals: (i) creation of economic growth and job markets; (ii) reduction in the number of poor people, and in turn (iii) realisation of sustainable livelihoods. To achieve these goals, focus is on three strategic dimensions: attractiveness, resilience and competitiveness of the local economy. These three dimensions do not exist in isolation, but form an inter-dependent chain. Thus, all factors that generate attractiveness and resilience are fundamental to creating competitiveness.

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<sup>14</sup> Ibid.

<sup>15</sup> For a more complete explanation of the definition, scope and categorisation of local economic development, see A.H.J. Helmsing (2001). Local economic development: new generations of actors, policies and instruments. Draft paper for the 2001 Cape Town Symposium (downloaded in June 2004).

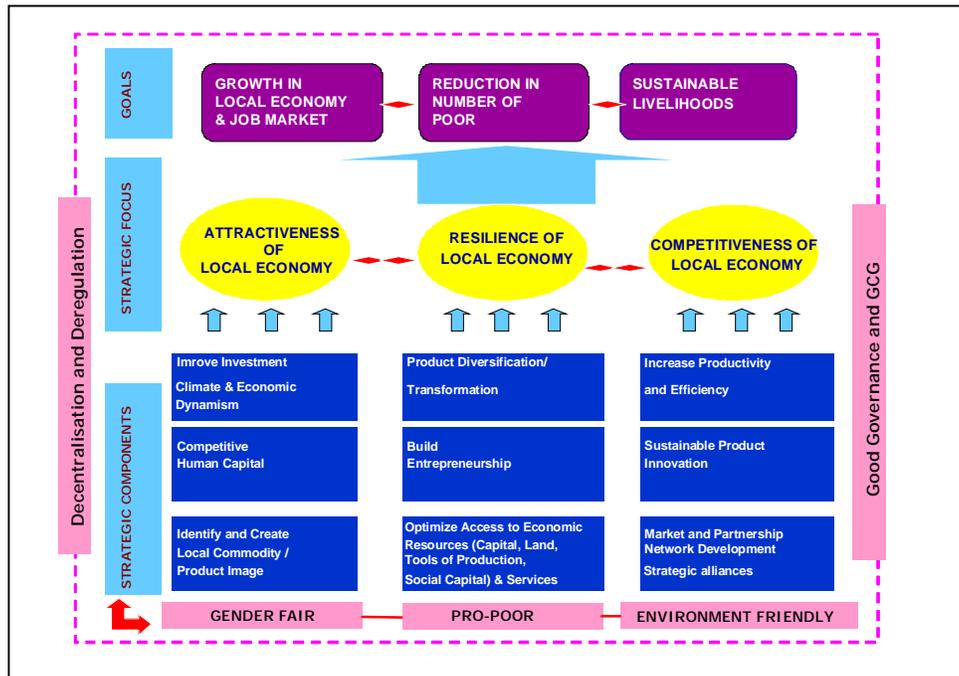


Figure 2: General Framework of Local Economic Development Strategy

**Note:** GCG = Good Corporate Governance

### 3.2.1 Conditions and Major Principles of Local Economic Development Strategy

#### Cohesive and Consistent Decentralisation and Deregulation that Supports Markets/ Trade Liberalisation

Regional autonomy brings public services closer to the people by giving authority to regional governments to manage their economic activities using available capacities to utilise the potentials of the region. Decentralisation of governance is a tool, not a goal, of regional development. Yet, only if regional autonomy comes with commitment and healthy deregulation policy, will public participation in the market really raise and generate value added to improve people's lives and the region's economy. To create healthy deregulation policy, regional government, the private sector and civil society (including experts) need to intensify dialogue and give more input to central government through bureaucratic channels and through existing formal public participation platforms (local parliament, regional delegates, and



## Alleviating Poverty through Local Economic Development Lessons from Nusa Tenggara

national parliament), as well as through the mass media and informal stakeholder dialogues.

### **Good Governance/Good Corporate Governance**

Consistent implementation of the principles of good governance at all levels of administration produces effective and efficient public services, and so avoids the trap of high economic cost. This perception must be created to attract investors. There are at least ten principles of good governance that should be adopted consistently and continuously in regional governance: (1) citizens' participation in the policy making process; (2) rule of law; (3) transparency; (4) equality; (5) responsiveness; (6) strategic vision; (7) public accountability; (8) professionalism; (9) efficiency and effectiveness, *which means optimal use of resources for public services*; and (10) supervision, which means tighter supervision of public administration and implementation of development activities by involving stakeholders.

### **Pro-Poor**

The strategic framework and implementation of local economic development programmes should focus on participation of poor people in activities in the production and marketing cycle, not just on trickle down effects, to improve their welfare. So, the starting point of support for poor people is their opportunities, not their barriers. The dimension of this potential includes the accessible as well as the actual. The potentials of poor communities and their access<sup>16</sup> to resources and services are important factors in achieving the goals of local economic development described in Figure 2.

No consensus has been reached on the definition of pro-poor strategy. Nevertheless, in this paper, the pro-poor concept emphasises several key principles: (i) investment in improving the human and social capital of poor people; (ii) policies and services that result in the widespread and sustainable availability of people's basic needs (access to food, clean water, housing, health and education); (iii) policies and

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<sup>16</sup> This perspective has also been described by M. Chatib Basri (Kompas, July 26, 2004, p 1). Winner of the 1998 Nobel Prize for economics, Amartya Sen, as quoted by Basri (*ibid*), believes that access is crucial to increasing people's capabilities. Furthermore, Sen believes that people are poor because their capability space is small (they are unable to do something), not because of something they lack. In other words, welfare is achieved not from the goods we own, but from the access that allows us to own these goods. With regard to this concept of access, Basri feels that expanding the access poor families have to economic resources from the demand side, such as developing physical infrastructure, and their access to subsidies for economic activities and scholarships, is important.



services that reduce transaction costs, so giving poor people more opportunities to obtain employment and/or greater value added from their own enterprises; (iv) increasing poor people's access to economic resources (capital, land/space, tools of production, market information, and so on); and (5) environment-friendly development that conserves or improves ecological function and the capacity of natural resources to produce.

### **Gender Equality**

The principle of gender equality has been integrated into the United Nations sustainable development framework, because gender is a cross-sector issue. One focus of the gender issue is on equality of access and control for men and women to economic resources and the employment market. Any local economic development initiative should first analyse the costs and benefits for both men and women. The green revolution, while rendering a huge service in multiplying food production through a system of intensive agriculture and mechanisation, was detrimental to women because this mechanisation caused loss of employment for many women workers in rural areas. This kind of phenomenon can be avoided by designing "gender neutral" technology or creating new employment for those who are marginalised. Furthermore, implicit in acknowledging the principle of gender equality is respect for the reproduction function of women, so that women workers continue to enjoy their rights as workers while on pregnancy and maternity leave.

### **Sustainable Development**

The principle of sustainable economic development has become an integral part of the United Nations sustainable development framework. Sustainable development emphasises the inclusiveness of economic development with social development and environmental conservation. So, the principle of sustainable development integrates the market mechanism with institutions (law/ legislation, social norms, reward and punishments) to shape the conduct and actions of the public, private and non-government sectors in managing development. Moreover, sustainable development is knowledge-intensive development, which substitutes capital with knowledge. Using bio-agents instead of pesticides to control certain crop pests is a concrete example of how knowledge replaces capital. Another example from the field of agriculture is the adoption of farming methods that integrate legumes that are able to form a symbiosis with rhizobium bacteria in the root system in converting nitrogen from the air into a



## Alleviating Poverty through Local Economic Development

### Lessons from Nusa Tenggara

nitrogen compound that can be absorbed by the plant, so that all, or at least part, of the plant's urea-based fertilizer needs is supplied by this symbiosis between the bacteria and the legume. Sustainable development strongly emphasises the importance of resource- and energy-saving development, which means that renewable energy and conservation of natural resources needs to be intensified.

### 3.3 Major Components of Local Economic Development Strategy

#### 3.3.1 Building Attractiveness

Besides fulfilling the basic principles of local economic development, as described in section 3.2, there are at least three other strategic components to building investor interest in the region: (i) improvement of investment climate and regional economic dynamism, (ii) commodity presence and image, and (iii) availability of competitive human capital. The following sections will provide a brief description of each of these components.

#### Improving investment climate and regional economic dynamism

Creating a healthy investment and business climate means creating conditions conducive to attracting domestic and foreign investment to generate economic growth and improve the welfare of the local inhabitants. So, in the context of local economic development, policy makers and the local community must understand the key factors that determine whether or not the business climate is healthy from the point of view of investors or business people, so that policies and services can be directed to create these conditions.

There are several key factors:

**Cost factor.** Policies and conditions that give rise to high economic cost will discourage investors from starting or expanding businesses, and also restrict the participation of poor people in the market. There are several conditions that may stimulate investor interest, and the more of these conditions that exist in a region, the greater the chance that investment will flow in. These conditions are: (i) transparent and efficient system of licensing and taxation; (ii) efficient and adequate infrastructure



(transport, telecommunications, energy and water); (iii) competitive local labour; and (iv) image and perception of the culture of good governance.

**Economic dynamism factor.** The previous section explained that decentralisation policy and cohesive deregulation to support the market mechanism is a determining factor in the attractiveness, resilience and competitiveness of a region's economy. At the same time, investors will also look at the factor that will help their businesses prosper, and that is the dynamism of the local economy. The dynamism of the local economy can be interpreted from two criteria: (i) its economic potential, and (ii) the structure of its economy. For the former, per capita gross regional domestic product (GRDP) is generally used because this indicator reflect the capacity of the people to fulfil their life needs. The second criteria, economic structure, uses the indicator of aggregate gross value added for all economic sectors in the region. From this information, investors will be able to see the main potentials (economic base), and whether the region's experience is in the primary sector, secondary sector (industry) or services sector.

**Risk factors.** These factors include: (1) macroeconomic stability and conducive social political dynamics; (2) policy transparency, stability and predictability; and (3) effective institutions providing guarantee of property rights and contracts.

Improving the business or investment climate in the regions requires synchronisation of policy and strategy between central government and regional governments. Nonetheless, many of the factors described above can be implemented or facilitated by regional governments alone.

### **Developing Human Capital**

Availability of workers with qualifications that match market needs is an important factor in attracting investment to a region. But qualifications alone are not enough, because the job market is competitive. Competition emphasises productivity and efficiency. As a consequence, the level of wages/wage policy is also a determining factor in attracting investment.

Development of human capital may take the formal education route (state school or private school) or the informal education or vocational training route. Because employment market demands vary widely, it would be impossible for the government



## Alleviating Poverty through Local Economic Development

### Lessons from Nusa Tenggara

to prepare curricula to respond to all these demands. Thus, private sector participation or partnerships of public sector, private sector and communities in developing human capital need to be intensified.

Returning now to the dilemma of wages. Creating investor interest by relying on competitive advantage through implementation of low wage policy benefits employers, but is not pro-poor. Conversely, if the government sets a high minimum wage, this may stifle investment and/or a black market in employment that could marginalise poor people and low-skilled job seekers from the employment market, so this kind of wage policy cannot be called pro-poor either. Thus, central government and regional governments need to implement gradual deregulation of wages, and at the same time implement supporting measures or facilitate the following steps:

- Develop human capital by providing affordable education for the general public, including poor people. The government needs to support local and national fund-raising initiatives to fulfil the basic right of all citizens to education. Innovative measures that do not give rise to high economic cost need to be championed, such as giving tax cuts to state enterprises, large private companies, and enterprises owned by regional governments that are prepared to contribute a portion of their profits to a people's education fund.
- Optimise the function of government-owned training centres in providing training services to job seekers.
- Give coupons (vouchers) to poor families, job seekers and actors in the micro, small & medium enterprise sector to receive training that meets the needs or demands of the job market from government and private training centres, and from non-governmental not-for-profit organisations.



### **Identifying and Promoting the Image of the Region's Leading Commodities and Products**

Almost every region in Indonesia has a thriving leading product that is the trademark of the region and contributes value added (gross regional domestic product and regionally-generated income) for the local populace. In regard to generating investment in the region, it is important to consider not only which commodity/product or service could be the region's mainstay, but also what special characteristics give this commodity/product or service distinctive competitiveness.

**[Insert 1:**

**Identifying and building a new image for vanilla from the District of Alor**

The district government of Alor in East Nusa Tenggara, with the support of GTZ PROMIS-NT, is in the process of researching and building the image of one of its leading products, vanilla. Although the price of vanilla on the world market is high, vanilla farmers in Alor do not receive a fair price for their product, because the world market perceives Indonesian vanilla to be of low quality. To design a new image, the district government has identified a distinctive characteristic of Alor vanilla as its trademark, which is that the vanilla is produced organically and is pesticide free. Although Alor farmers rarely use pesticides, the threat of vanilla pests has begun to grow with the increase in human and crop traffic between islands. So, the district government of Alor, with the support of GTZ PROMIS-NT, also undertook joint research with Udayana University of Bali to offer disease free and /or disease resistant vanilla seeds using tissue culture techniques. At the same time, a website has been developed to promote Alor's leading products, which include vanilla and hand woven cloths. There has been a fairly rapid response from the market, with large domestic and foreign traders requesting product samples. Alor district government also took the initiative to build the distinctive competitiveness of vanilla by providing funds for the chemical analysis of the vanillin content of Alor vanilla in a cooperation with Udayana Bali University. The results of the analysis show that the vanillin content of Alor vanilla is above the standard average for Indonesian vanilla in all quality categories.]

In regard to the principles of pro-poor local economic development, the selection of leading products should be based on the criterion of the direct potential value added of a commodity/product for poor families, in addition to the criteria of technical feasibility, market demand and the multiplier effect of a commodity/product of one sector on other business sectors. However, this does not mean that only existing commodities or products can become mainstays of the region. Viable new commodities, as well as commodities with the potential to create value added for the region's economy and for the poor and the environment, may be developed as regional mainstays.



### **3.3.2 Building Resilience**

The concept of resilience was adopted from a theory pioneered by ecologists that see the economy as an ecosystem (ecological nation) that is striving to maximise the long-term value of limited land resources by developing interdependent biological systems. In other words, diversity and interdependence of species and environments is a key factor in building the long-term productivity and resilience of a system. Resilience is a dynamic concept. Put simply, the resilience of an economy refers to the ability of the economic sector to adapt and recover from economic and non-economic pressures. In an ever-changing environment, in which opportunities and risks may appear at any time, each economic unit, be it the household, company or region, needs to be prepared. Following is a description of the three-fold strategy to build resilience and the expected role of the public sector.

#### **Business Diversification and Product Transformation**

Diversification includes commodity diversification and enterprise diversification, while product transformation in the narrow sense is modification in the form or structure of a product (peeling cashew to make cashew nuts and processing cashew apple into syrup are transformation processes). The purpose of diversification and product transformation is: (i) to enable actors in the micro and small & medium enterprise sector and the private sector in the regions to minimize the overall risk of failure; (ii) to protect themselves from the threat of external products or substitute products entering the market; and (iii) to create job markets and value added for local communities in particular and the region's economy in general.

The choice of diversification or product transformation, or indeed a combination of the two, should be based on technical and non-technical criteria, including: (i) compatibility and natural risk factors that are difficult for farmers/entrepreneurs to control (climate, pests, diseases); (ii) balance between demand and supply, including the implications of economies of scale; (iii) the capacities and priorities of farming families (entrepreneurs); (iv) local culture (for example, food habits). The second criteria requires further explanation. Over-diversification, a situation where there is not even one leading commodity, generally causes marketing difficulties because there are no economies of scale. Thus, creating economies of scale at the production unit level (household or company), and at the local level, are key factors that need local and cross-sector planning and coordination.



Creating a conducive investment climate is an essential condition for the success of diversification/product transformation strategy; but it is not sufficient. As a support, regional governments need to facilitate:

- § Revision of spatial plans, taking into account the condition and needs of poor people, and effective socialisation of these plans.
- § Transformation of the marketing structure to eliminate price distortions resulting from a marketing chain that is too long and dominated by middlemen, through establishment and empowerment of producer's economic institutions (cooperatives, marketing associations, and so on).
- § Improving public access to information and technology by revitalising information services and forming partnerships with business development service providers.
- § Regional governments provide financial incentives and capacity building incentives for poor families, such as:
  - Subsidies on tools of production (for example cashew seed peelers, concrete floors for drying seaweed and so on),
  - Giving vouchers to poor families, job seekers and actors in the micro, small & medium enterprise sector to receive technical and management training that meets their needs at public training centres, non-governmental not-for-profit organisations, and private training centres, paid for by regional government. The expectation is that this training model will promote competitiveness and efficiency in providing good quality training that meets market needs.
- § Providing credit (and grants for revolving funds) for poor families and their organisations (cooperatives, associations) to promote the processing and marketing of local products. This topic is discussed in more detail in the following sections of this chapter.



## Alleviating Poverty through Local Economic Development

### Lessons from Nusa Tenggara

#### Developing Entrepreneurship

Entrepreneurship is about making changes or doing something differently. In the narrow sense, entrepreneurship is how to exploit innovations to create value, which cannot always be measured in financial terms alone (Wickham, 2001). Entrepreneurship is concerned with the potentials for change. These potentials for change exist in three dimensions (Wickham, 2001): (i) the financial dimension (the potential to create new value); (ii) the personal dimension (the potential to achieve personal goals, not only money); and (iii) the social dimension (the potential to make structural changes).

In line with this thinking, the following measures should be an integral part of local economic development strategy:

- (i) Building a culture of democracy to increase the effectiveness of participation and individual and collective bargaining power in all domains, including the economic, socio-cultural and political domains. Healthy democracy is important for economic development and, vice-versa, democracy cannot grow without a healthy economy. Entrepreneurs, but also poor producers, and consumers must get the capacities and opportunities to influence and/ or determine decisions that will affect the continuity of their enterprises and their lives.
- (ii) The government develops structures and facilities to improve access of the public to information and its capacities to analyse economic and business information, so that appropriate and efficient use can be made of limited resources. These capacities enable producers to be more productive, creative and realistic in the long-term management of their businesses, rather than just doing what their colleagues do or responding to market signals (price).
- (iii) Support for change in marketing structures to create more competitive and efficient supply chains. One important opportunity here is to form producers organisations such as associations, cooperatives or other model of organisation that complies with the prevailing formal legal framework. But, because most producers in the micro, small & medium enterprise sector, and poor people, are involved in “exploitative” relationships with traders and/ or creditors, these producers organisations do not have to “kill” or completely break off these



relationships. What is needed are win-win options, in which local farmers and traders build new relationships to share value added more fairly in a new and appropriate forum, such as a cooperative or association.

### **Optimising Access to Economic Resources and Building Social Capital**

#### ***Access to Land and Space***

The small scale of land ownership, i.e. less than 0.25 ha on average, is one of the main factors limiting the creation of economies of scale and value added in rural areas. As in other areas of Indonesia, around 60-70 percent of the land area in Nusa Tenggara is within the forestry regulatory framework, not the agrarian regulatory framework. Because of the lack of land for farming, some rural inhabitants practice illegal farming and illegal logging, adding to deforested areas and areas of critical land. Control and legal action by the government has so far proved ineffective, because the root of the problem remains.

Thus, a more contextual and pro-poor strategy is needed, which includes:

- (i) Adopting the concept of social forestry developed by the Department of Forestry, which allows local people access to forest lands, to make investment, and to gather products required for subsistence and commercial needs.
- (ii) Granting local communities, especially poor families, the right to access and use forest lands formerly used for farming and forest lands that were once private forest concessions and on which the licence has expired. In other words, part of the land that is within the forestry regulatory framework is transferred to the agrarian regulatory framework, where the local people have right of access (use rights), not the right of ownership. To obtain this right of access, civil society and regional governments need to communicate their aspirations/give input to central government via existing mechanisms.



## Alleviating Poverty through Local Economic Development

### Lessons from Nusa Tenggara

- (iii) This second strategy needs to be translated into a legal framework, or zoning regulations. Although each district and municipality in NTB and NTT have definitive spatial plans, it remains unclear in how far they are pro-poor and what their long-term flexibility is. Also, there is still room for revision on the question of how far these spatial plans synchronise the existing regional development strategy.

#### ***Access to Capital***

Unlike large scale urban industry, actors in the micro, small & medium enterprise sector in rural areas often face difficulties obtaining bank loans. As a result, they are forced to borrow from informal financial sources whose credit volume does not fulfil the economies of scale. The situation is even worse for poor people, who often can obtain loans only from exploitative traders and middle-men at very high rates of interest. To give actors in the micro, small & medium enterprise sector, and poor people, better access to capital, several strategies that have been piloted in other regions could be adapted and adopted, such as:

**Revolving funds.** Several government and non-government organisations in Indonesia have adopted the concept of the revolving fund with varying degrees of success. Revolving funds are provided to poor self-help groups or micro enterprise groups that do not meet technical criteria of banks, to start up or develop productive enterprises. One critical issue that threatens the continuation and sustainability of revolving funds is the question of ownership. Although revolving funds provided by sectoral projects are always labeled as “community owned” funds, the concept of ownership and the revolving of these funds after the project finishes (in the long term) is unclear. Usually, revolving funds are controlled by an ad hoc committee, and recipient groups repay the money in instalments through the committee’s account. In theory, this money is then lent to other groups in the same village. For revolving funds to run effectively and efficiently, a clear concept of ownership needs to be formulated, and an organisational structure for the management of these funds needs to be created. Possible models of organisation include: self-help groups (group associations), village-owned enterprises, and industry cluster organisations.



**Building links between groups and banks.** This strategy can be realised through development and empowerment of intermediary financial institutions. Models of organisation appropriate to the current formal legal framework in Indonesia are saving and credit cooperatives (credit unions) or general cooperatives that have a saving and credit unit. Organisations like these can obtain credit from the banking sector and then channel it to their members and/or customers at commercial rates of interest, but with flexible conditions.

But cooperatives do not normally grow themselves, and not all cooperatives fulfil bank conditions, especially fledgling cooperatives. Here is where regional government, particularly the Cooperatives Agency, must take a role to raise public awareness for the benefits of forming cooperatives and to facilitate the establishment of cooperatives. At the same time, regional governments must support the strengthening of the institutional and capital base of cooperatives. One innovation that offers a chance to strengthen the capital base of cooperatives is to remove subsidies on refined fuel oil and fertiliser, and to give these funds to cooperatives to strengthen their capital base.

Several regions in Indonesia have begun testing new approaches to giving poor people and actors in the micro, small & medium enterprise sector better access to capital. As an example, in the District of Tanah Datar, the regional government has made a capital investment in *Bank Perkreditan Rakyat* (BPR), that was taken from the 2002 and 2004 regional budgets. In the District of Dompu, in 2003 the district government provided funds of Rp 2.5 billion via the Indonesian Rice Traders Association (*Persatuan Pedagang Beras Indonesia – PERPADI*) to purchase rice from farmers; but unfortunately this initiative was a “failure” because, among other reasons, of problems related to the organisational structure and professionalism, as well as internal problems. The District of Alor adapted a concept introduced by Bank Indonesia, of building links between banks and self-help groups through the mobilisation of group savings. Facilitated by village motivators, groups opened savings accounts at banks and saved regularly at *Bank Daerah NTT*. Village motivators and the bank provided advice about financial administration and designing business plans. If group members need credit, the funds in the group's savings account at the bank can be used as collateral for members who want to borrow from the



## Alleviating Poverty through Local Economic Development

### Lessons from Nusa Tenggara

bank, and the bank extends a loan in the name of the group of up to five times the balance on the savings account.

[Insert 2:

#### Investment Funds

Credits, revolving funds, and other forms of funds (such as loans from moneylenders) with conditions poor people can meet, and payment and repayment schedules that stick to the seasonal calendar are incentives for poor people to expand the processing and marketing of agricultural products. For example, credits for cashew farmers should be given at the harvest time for this commodity. These credits will help poor families meet their life needs, allowing them to store the newly harvested cashews until such time that family members have time (when there is no other work to do) to peel the cashews and they can be sold at a higher price. With the value added obtained from the product transformation of cashew seeds into cashew nuts, farmers will be able to repay the credit and the interest.

A credit system like this is being tested by PROMIS-NT, in which groups can use and manage funds known as investment funds, which are given to selected groups. The investment funds are managed by a committee consisting of members from the Community Empowerment Board (*Badan Pemberdayaan Masyarakat – BPM*), banks, village motivators and representatives of self-help groups. Groups or individuals can obtain investment funds by presenting a feasible business plan for the enterprise they wish to develop. The presence of banks on the committee opens up opportunities to obtain bank credit in the future if the enterprise is a success and grows. Involving the bank as assessor of the quality of groups and business plans also paves the way for communication between the group and the bank using a scheme pioneered by *Bank Indonesia* known as PHBK (*Pengembangan Hubungan Bank dengan Kelompok*, or Linking Banks and Groups).]

[Insert 3:

#### World Bank NTAADP Funds in the District of Bima

Funds for the Local Community Initiative (*Inisiatif Masyarakat Setempat – IMS*) programme of the Nusa Tenggara Agricultural Area Development Project (NTAADP) come from soft loans from the World Bank to the Indonesian government, which is entrusted with administering these funds to organisations known as Village Financial Management Units (*Unit Pengelola Keuangan Desa – UPKD*). Villages that meet the criteria for poor villages but have agricultural land that could be developed can form UPKD. The managers of the UPKD are elected and appointed by the village community. In the District of Bima there are currently 57 UPKD in 57 villages in 7 subdistricts. Each UPKD receives funds of between Rp 50 million and Rp 100 million each distribution period. These funds are perpetual funds that are owned collectively by the village community where the UPKD is located, provided that they are managed according to the agreed mechanism.

UPKD give loans to groups, not to individuals. Although in theory these funds are owned collectively by the community, priority for loans is given to groups that meet the following criteria: (1) farmers groups or poor self-help groups that want to start up or develop feasible productive enterprises; (2) women's groups and youth groups whose members have no permanent employment; (3) that are not participants/ aid beneficiaries of other ongoing programmes;



and (4) one head of household may participate in no more than one productive activity package in one fiscal year. Other important characteristics of the NTAADP programme are:

- Activity proposals are determined by the local community, facilitated by facilitators from NGOs.
- The amount of funds a group receives is based on the proposal, which is verified by teams at the village and district levels, the main criteria being the technical feasibility of the business plan.
- IMS funds are distributed directly at the village level by transfer to the UPKD account, and then distributed to self-help group members.
- Professional credit management and simple administration with an affordable interest rate of around 1.5%-2.0% a month.

As a beneficiary of NTAADP funds, between 1999 and 2002 the District of Bima received funds of around Rp 7 billion. As of August 2003, there were 892 core self-help groups with 13,557 members, consisting of 9,717 men and 3,840 women. The self-help groups developed 541 groups with 7,422 members (4,545 men and 2,809 women). The latest study (LP3M, 2003) reports that initial funds of Rp 7 billion have grown significantly to around Rp 10 billion. This growth comes from loan interest and local community savings. Furthermore, the LP3M study (2003) reports a significant increase in the income of NTAADP target groups, ranging from 12% to 70% depending on the type of business they run.

The key to success lies in the members having a collective vision, accompanied by clear organisational structures and regulations, guarantee of ownership of the funds by the community, participatory management, and transparent and professional management. Yet several UPKD have failed in the management of these funds because of an absence of these factors, coupled with difficulties in transport to several locations, which has hampered support.

Source: LP3M and Bima District Development Planning Agency, 2004]

### ***Building Social Capital***

Although classical economists do not wholly accept the concept of social capital, the term 'social capital' is becoming more and more popular. Even international institutions such as the World Bank, have acknowledged the importance of social capital in the global effort towards sustainable development. Social capital is a dynamic concept and a broad agreement has yet to be reached on its definition. But several dimensions of social capital are very relevant in the context of local economic development, including: (i) social and religious norms that from generation to generation have shaped the views, morals and conduct of the community; (ii) networks established and maintained by the community to deal with their problems based on the principle of helping and respecting one another; (iii) mutual trust among members of the community formed in a process of social interaction.



## **Alleviating Poverty through Local Economic Development**

Lessons from Nusa Tenggara

These dimensions of social capital are dynamic. Some have faded as a result of the influence of modernisation, while others have evolved as the community develops. So, these dimensions can change over time. Furthermore, not all the norms and values a community abides by will support or be consistent with sustainable economic development. Local governments naturally better understand the challenges and opportunities of developing the dynamism of social capital in a coherent direction with the aim of a more evenly spread and lasting economic development. Regional governments need to support local initiatives for “reinventing” and “enriching” social capital, by:

1. Intensifying support for research and sharing experiences about social organisations that encourage communities to be self reliant;
2. Stimulating and facilitating self-help groups to build forums or platforms for sharing experiences and sharing responsibility in development;
3. Supporting informal education initiatives (programmes) in rural areas.

### **3.3.3 Building Competitiveness**

The key question that needs to be addressed in this section is: What role does the public sector need to take to improve the competitiveness of the business sector in the arena of regional-global competition? As explained in section 3.2, building competitiveness is not a strategy isolated from strategy to build attractiveness and resilience. In other words, a successful building of attractiveness and resilience of businesses and the economy is a precondition for the success of the strategy to develop competitiveness, which is discussed in this section. Definitions of the local economic development approach (section 3.1) emphasise that the public sector plays the main role in creating a climate conducive to starting or expanding businesses. The following paragraphs describe several important elements of a strategy to build competitiveness that complements the strategies discussed in the sections above.



### **Support for Improving Productivity, Efficiency and Sustainability**

In the arena of business competition, the winner is the one who is most productive, efficient, and innovative. In addition to the factors of human resource and business climate, other key factors that determine the productivity and efficiency of a business sector are the quality of natural resources (for example land and genetic resources), the technology factor, and the economies of scale. Although entrepreneurs are very concerned about productivity and efficiency in order to maximise profits, not all of them have a long-term vision for sustainable development. Behaviour that only emphasises short-term profits will lead to over-exploitation of natural resources. Access to energy efficient modern technology is important, but it needs government intervention and incentives to improve productivity and sustainability, such as:

- § Micro and small & medium scale producers need support in identifying potentials and new opportunities for increasing their productivity.
- § Providing effective and efficient energy and telecommunications infrastructure in rural areas
- § Providing a regulatory framework that supports synergy of the market mechanism and social capital (norms, morals, mutual help) in promoting efficient and sustainable use of natural resources. The polemic discussion of the law on natural resource management must be continued by giving proportional consideration to the economic, social, and ecological dimensions of natural resources.
- § One important dimension of the regulatory framework mentioned above is clear and secure property rights, which also includes safety of contracts. This is an essential condition to promote investment.
- § To facilitate the creation of economies of scale and fair access to natural resources, regional governments also need to develop mid and long-term spatial plans based on the regulatory framework mentioned above.
- § Intensify control of the use of natural resources and consistent application of the law by involving local stakeholders (civil society forums).



## Alleviating Poverty through Local Economic Development

### Lessons from Nusa Tenggara

[Insert 4:

#### **Increasing the productivity of the resources of the poor entering the market**

A “food for work” approach, combined with institutional strengthening, has helped poor farmers in rural areas of East Sumba, which is located in Indonesia’s dry zone, to enter the market.

In the District of East Sumba, the Nusa Tenggara Project (*Proyek Nusa Tenggara – PNT*) component of GTZ PROMIS-NT supports several groups of poor farmers to dig wells as a source of water for irrigating their fields. The project adopts a “padat karya” approach, which integrates the concept of “food for work” and group saving and loan activities. Farmers that help to dig wells get 3.5 kg of rice from the project. Of this amount, only 2.5 kilograms are handed directly to the farmers. The remainder goes into the group’s savings account. From these savings, farmers may purchase a pump to pump water to the surface and store it in a tank, so that the water in the tank is ready to be distributed to the plots of land owned by the members of the group. With this irrigation, production of corn and vegetables increases, and the farmers have now begun selling their surplus on the market. Although the scale of this activity is relatively small in terms of the area of land that can be irrigated and the number of farming families that benefit, lessons are continually being learned from this approach and adopted in similar locations elsewhere in the scheme of pro-poor development programmes.]

Although globalisation brings about unexpected economic and social impacts, the opening up of the regional and global markets is an enormous opportunity for business to create economic growth and improve people’s standard of living. The capacity to create changes or innovations is a determining factor in the success of a business. Owners of established private corporations in urban areas may not have much difficulty when it come to innovation. But actors in the micro, small & medium enterprise sector in rural and urban areas of Nusa Tenggara still need public sector support and services to profit from market opportunities that exist outside the local area and overseas. Entrepreneurs in the regions cannot rely entirely on the “dribbles of market information” that come from large corporations or export-import associations in metropolitan cities. The following section discusses some of the key facilities and services regional governments should provided to support innovation.



### **Support for Continuous Innovation of Leading Products**

Regional government need to bridge supply chain linkages, in other words link consumers and producers, among others by:

- (i) Making the results of studies of the domestic and overseas markets widely available to producers;
- (ii) Supporting promotion and/or integration of new products on to the local-regional and global markets, by:

§ Providing continuous support for infrastructure development and promotion institutions, and providing financial support for implementation. The approach adopted by the Chinese government (see Insert 5) could perhaps be used as a model to be adopted for promotion at the regional and international levels. Management of these promotion agencies should be assigned to private or non-governmental organisations, but with government (regional government) paying the salaries of management, at least in the initial phase.

§ Facilitating micro, small & medium enterprises to obtain product certification.

#### **[Insert 5:**

##### **China – Indonesia's toughest competitor on the export market**

China has emerged as the toughest competitor for producers of components of processed food, textiles and textile products, furniture, and electronic products in several export markets, including the Middle East. Chinese producers not only get many facilities from their government, they are also able to create effective promotion and market share strategies, allowing them to supply goods to the market at competitive prices. Irrespective of the fact that in terms of quality and after sales service Indonesian products can compete with, even surpass, Chinese products, demand for Chinese products is enormous because people perceive that Indonesian products are more expensive than Chinese products. China must be acknowledged as the strongest competitor. The strong competitiveness of Chinese products, is enhanced by various facilities, such as subsidies from production to promotion. To intensify the influx of Chinese products on to the United Arab Emirates market, the Chinese government has build a special permanent exhibition centre.

Source: Adapted from Kompas, 15 September 2004, p 15,]



## Alleviating Poverty through Local Economic Development

### Lessons from Nusa Tenggara

#### Regional Partnerships

The concept of *regional management* integrates different administrative territories to become an economic zone with one *joint inter-regional stakeholders forum* in the domains of economic policy, information communication, and regional marketing.

The coming into force of Law 32/2004 on Regional Autonomy grants regional governments broad authority to manage their own economic development activities. This has given regional governments the opportunity to transform centralised planning into a decentralised development planning process. But regional autonomy tends to place a greater burden for regional development on the shoulders of the private sector and poor communities as local hegemonies emerge and sectoral egoism proves hard to eliminate. Unfortunately, there have been no significant efforts by the central government or initiatives from regional governments themselves to promote the process of regionalisation. Although article 195 of Law 32/2004 could be used as the legal basis for regionalisation, the influence of the habitual use of a centralistic style in policy making, and the weakness of planners in designing economic development strategies still poses a challenge in building mutually beneficial regional partnerships.

In view of the problems and obstacles in implementing regional development, the concept of regional management is essential for exploring the development strengths in the regions, reflecting the interests, situation, and the real conditions in local communities. In this regard, GTZ also facilitates regional partnerships in the Special Region of Yogyakarta through the Urban Quality Management project, and in Central Java, through the Regional Economic Development programme. It is hoped that stakeholders on Sumbawa island and in other areas of East Indonesia can learn lessons from the project experiences in these areas of Java. In the context of the Urban Quality Management project, partnerships focus more on developing infrastructure such as roads, transportation systems, clean water data collection, and solid waste and waste water management. The focus of the Regional Economic Development project is on economic partnerships, taking into account local supporting factors or locational factors, such as regulations that influence the business climate and the room for manoeuvre of businesses, facilities and infrastructure, and business development services.

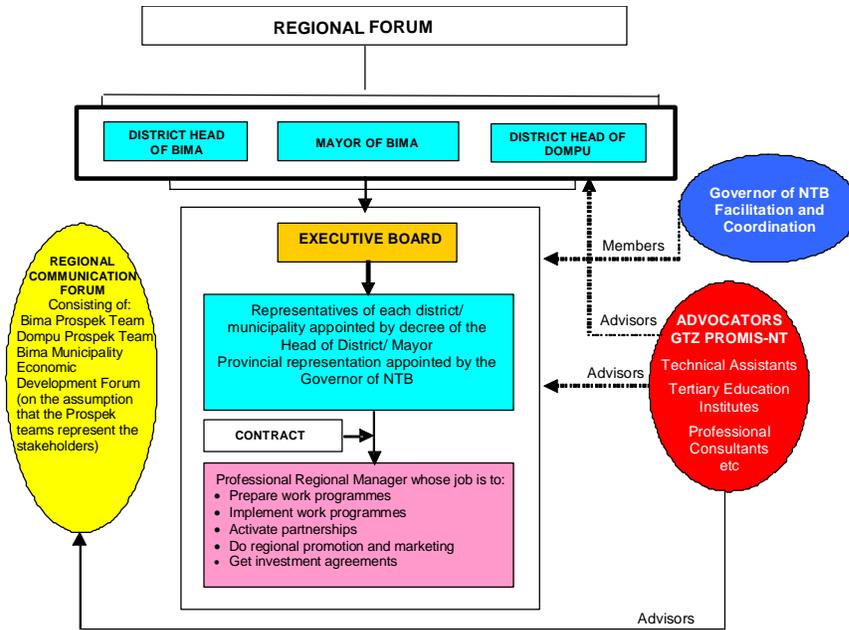


Figure 3: Organisational Structure of Regional Management and Marketing

In the Districts of Bima and Dompu, however, an appropriate organisational model is still being explored through dialogue with stakeholders in the regions facilitated by the local economic development partnership forums (PROSPEK Teams). One organisational model that could be considered is shown in Figure 3, and Insert 6 below gives an overview of some of the key aspects to consider in the context of developing regional partnerships.



## **Alleviating Poverty through Local Economic Development**

### **Lessons from Nusa Tenggara**

[Insert 6:

#### **Managing the Process of Forming Partnerships**

##### **Tasks and Functions of the Partnership Organisations**

1. Partnership organisations are set up to achieve certain goals/ strategic issues.
2. They implement programmes in partnership with other institutions/ organisations for the long-term benefit of all those involved.
3. They ensure the commitment and consistency of stakeholders to the agreed tasks.
4. It is the job of partnership organisations to serve the process, not control it.

##### **How to Form a Partnership Organisation**

1. Find the management needed.
2. Understand the role of intermediary.
3. Choose the right intermediaries.
4. Manage the establishment of the partnership systematically.
5. Monitor the intermediaries.
6. Strive for sustainable capacities.

##### **Key Principles for Managing a Partnership Organisation**

1. Build non-financial resources to help run programmes and the partnership organisation.
2. Continue to aim and be oriented towards achieving results, even if the partnership gets off to a slow start.
3. Ensure that the partnership organisation also pursues social change.
4. Choose managers that are results-oriented and intermediaries to steer the process.
5. Know about and face up to problems directly, honestly and openly.
6. Use research produced by stakeholders as feedback to make sure the partnership is on the right track.

Source: Rifai Saleh H. (2004).]



## CHAPTER IV

# THE PROMIS-NT EXPERIENCE AND RECOMMENDATIONS

### 4.1 Important Experiences

GTZ PROMIS-NT and its two components, **PRODA** (*Dukungan Pemerintahan Daerah* – Support for Local Governance) and **PNT** (*Penanggulangan Kemiskinan* – Poverty Alleviation) focus on two entry points, regional governments and local communities. Working with PROMIS-NT in reducing poverty, the Indonesian government is committed to providing services oriented towards local economic potentials. Pilot projects to develop local economic development strategies, however, are focused in two districts, Bima and Dompu, in the Province of West Nusa Tenggara (*Nusa Tenggara Barat* – NTB).

PROMIS-NT takes the initiative and supports the process of the formation of Local Economic Development Partnership Forums, which are known as PROSPEK, the purpose of which is to coordinate efforts to develop strategies and promote local economic development. Members of these forums consist of regional government, the private sector, not-for-profit non-governmental organisations, and representatives of the implementing agencies of ongoing regional and national programmes in the region.

Monitoring of the short-term impacts shows that local economic development initiatives (programmes) have at least three positive impacts: (i) since the formation of local economic development partnership forums in the Districts of Bima and Dompu, the private sector in these two districts has shown increasing interest in forming partnerships, and participating more intensively in assessment, planning and implementation of local economic development strategies. The PROSPEK teams in the Districts of Bima and Dompu have begun taking the initiative and assuming responsibility, without waiting for GTZ PROMIS-NT, in facilitating the process of strengthening local producers and building collaborations between local producers and traders, especially for leading commodities. This was based on the results of a



## **Alleviating Poverty through Local Economic Development**

### Lessons from Nusa Tenggara

participatory appraisal of competitive advantages (PACA) of local commodities and industrial clusters, which are seaweed, peanuts, salt and traditional weavings in the District of Bima, and cashews, marine fish and cattle farming in the District of Dompu. (ii) Likewise, local producers are now more motivated and very interested in forming organisations, that jointly assess, plan and implement economic development initiatives. Furthermore, several of the producers organisations or cooperatives that have been established, were able to make business plans and have obtained capital grants from the district department of cooperatives. (iii) The existence of Local Economic Development Partnership Forums means that local government and local parliament (DPRD) have better information about the real local economic situation, and a better understanding of the economic challenges and opportunities. One positive consequence is that recommendations from the participatory appraisal of competitive advantages have been integrated by the regional governments in both districts into next year's (2005) economic development programme, and some are undergoing implementation this year (2004) with funds from regional government (APBD) and deconcentration funds from central government. One example is the coastal community empowerment programme in the District of Dompu. (iv) Also, the existence of Local Economic Development Partnership Forums has stimulated public sector and private sector awareness of the need to develop a more comprehensive regional economic development strategic plan, that is pro-poor and oriented towards sustainable development.

Comparing the performance of the local economic development partnership forums in these two pilot districts, Bima and Dompu, several preliminary lessons learned can be discussed here. The dynamism and performance of the forum depend greatly on a number of factors: (i) harmony of vision among the stakeholders in the forum; (ii) the incentive of institutionalization, i.e. the legitimisation of the forum by regional government; (iii) socio-political dynamism in the region, which is marked, among others, by growing critical response, the openness of leadership and the community; and (iv) motivation and challenges to build capacities/ professionalism.



## **4.2. Recommendations for the Future**

The design of a local economic development strategy as discussed in this paper is a synthesis of ideas that have not yet been put into practice and of experiences in implementing local economic development initiatives in the context of the Indonesian-German Technical Cooperation in West and East Nusa Tenggara. So, regional governments as the partners in this cooperation, need to be continuously supported during field trials for a comprehensive adoption and verification of the concept. Several strategic steps towards adoption and verification of the concept need to be made, including:

1. Regional governments need to open dialogue to review how far existing spatial plans are consistent with pro-poor and sustainable development principles. In this respect the role of local economic development partnership forums is regarded as crucial. The outputs of this dialogue should be used as input for fine-tuning/ revising spatial plans.
2. Regional governments, with the support of local economic development partnership forums, elaborate a district/ municipal economic development strategic plan for 2005-2009, which includes a spatial plan for the area.
3. Selecting several locations that have the potential to be developed as new growth centres, where relevant local economic development strategies or components are tested.
4. Developing the concept of profit-sharing between district governments and village governments based on development needs criteria, which include the existence of poor inhabitants, and the performance of the village government, to replace the approach of the regional government of giving an “equal share” to all villages. This new approach is expected to give communities at the village level more space to plan and implement their own programmes to escape from poverty. This concept is becoming increasingly important with the coming into effect of Law 32/2004 (article 212 on village finances, clause 3), which describes and guarantees the right of villages to a share of fiscal balance funds from central and regional governments received by the district.



## **Alleviating Poverty through Local Economic Development**

Lessons from Nusa Tenggara

5. Developing a flexible and accurate monitoring system to evaluate the performance of local economic development initiatives, and at the same time intensifying sharing the experiences of success and failure in local economic development initiatives through seminars, workshops and so on.
6. Developing a flexible and effective organisational structure that supports regional partnerships in economic and social development. These regional partnerships can be promoted through facilitation by provincial government.

In implementing the proposed strategies, there must be synergic cooperation between central government on one hand and provincial and district/ municipal governments, as well as public sector and private sector partnerships on the other hand. To do this, regional governments need to be more transparent and provide reliable and easily accessible information about the business climate and business (investment) opportunities in the region, including realistic data about the level of poverty, to the private sector and the central government.



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