Post-Tsunami Microfinance in Aceh, Indonesia: The Challenge of Sustainability

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The Tsunami and earthquake disasters in Aceh and Nias have opened the eyes of the world and given important lessons, not just to Indonesia but also to the people in the world. (Kuntoro Mangkusubroto, Director of BRR, at the occasion of the third anniversary of the Tsunami)

The challenge

Microfinance in Aceh, or NAD[1] has been severely affected by the Tsunami of December 2004, an earthquake in early 2005 and three decades of conflict. While the Tsunami led to an unprecedented influx of human and financial resources for relief and reconstruction, the peace accord of 2005 opened a window of opportunity for long-term development, drawing attention to large numbers of disadvantaged and neglected people throughout the province. Donor interventions were designed in response to a natural calamity; sustainable development requiring a longer-term presence was rarely an objective. Between 2005 and 2007, assistance shifted from emergency relief to reconstruction, laying at the same time some foundations for sustainable development. This has been paralleled by a shifting balance from disbursement to capacity-building.

Most donors had left by the end of the 2008. The reconstruction agency BRR[2], a central government body, terminated its work by April 2009, with more than 90 percent of its work completed according to an assessment by the Governor, and local government has taken over. It is too early to evaluate the impact of donor interventions, sustainable or not. At an interim point in 2008 we asked what lessons have been learned to date that may guide donors at future calamities in Indonesia and elsewhere and perhaps local government agencies in Aceh preparing for a takeover from BRR. At the same time, this may provide a framework for a more systematic study, perhaps in 2010, jointly with government and donor agencies.

Lessons learned

Tailoring assistance: Interventions have to be tailored to types of microfinance institutions (MFIs).[3] In Aceh they comprise informal financial institutions (FIs) such as self-help groups (SHGs), semiformal FIs such as cooperatives and credit NGOs, and the microfinance providers or services of regulated FIs comprising rural banks/People's Credit Banks (BPRs), regional development banks (BPD) and national commercial banks. Among the latter, not all

[1] Official name: Nanggroe Aceh Darussalam (NAD).
[2] Badan Rehabilitasi dan Rekonstruksi (BRR) NAD-Nias.
[3] Here we follow the definition by CGAP: "MFIs are defined as licensed and unlicensed financial institutions that include nongovernmental organizations, commercial banks, credit unions and cooperatives, and agricultural, development, and postal savings banks. They range from specialized microfinance providers to programs within larger, multipurpose development organizations." (Jennifer Isern and Julie Abrams with Matthew Brown, Appraisal Guide for Microfinance Institutions: A Technical Guide. CGAP, Washington DC, March 2008, p. xiii; www.cgap.org/)

have welcomed donor and government assistance; eg, Bank Rakyat Indonesia with its successful network of Microbanking Units and an abundance of excess liquidity at national level has preferred to do without donor assistance. In Aceh there are member-, community- and privately owned MFIs, with widely varying strengths and weaknesses. All of these, except credit NGOs, mobilize savings and may thus require strengthening their deposit as much as their credit services. A major distinction in Aceh is between conventional and Islamic MFIs, particularly among BPRs and financial cooperatives, providing a special challenge to donors mostly familiar with conventional banking and microfinance. Most of the MFIs have been affected not only by the calamity, but by decades of conflict, poorly developed infrastructure and markets, low levels of human resource development and well-meaning but ill-guided government interventions, using some of the MFIs as channels for the disbursement of government funds. While the various types of MFIs serve different market segments, each of them responds in its own way to the challenge of expanding outreach to victims and the unbanked.

The rush to help: After a calamity, there is a strong sense of urgency. The most immediate response has come from Indonesian agencies: governmental, civil society and private. Subsequently, about 400 donor agencies have come into Aceh, wanting to help immediately, for varying lengths of time, each with its own mandate, agenda and experience. Only few coordinated their activities with those of ongoing Indonesian efforts, crowding them out in some instances. The rehabilitation and reconstruction agency BRR was established in April 2005 and became operational in May, with the mandate of harnessing the full potential of the will to help. It has been struggling with the task of first registering and then coordinating the activities of donors – a continual effort. Few among the donor agencies, particularly among the smaller ones, took the time to analyze, plan and cooperate.

Analyze first: Effective help needs thorough preparation and prior analysis. Few have been aware of the microfinance landscape and the strengths and weaknesses of the existing institutions. Early on BRR asked for a mapping survey and a rapid analysis of the financial landscape. This request was eventually complied with by the German technical assistance agency GTZ. The earlier such a survey is done and the wider its results are shared, the more useful it is.

A considerable body of information on rural and microfinance exists in Indonesia, which is also relevant to Aceh; a quick review by a well-informed donor could have been shared through a website. Other information, peculiar to Aceh, would have to be newly gathered, providing basic data on the financial landscape and on Acehnese culture and society, to allow donors to adjust their approaches to local conditions and practices, not only with regard to microfinance. This would have included information on ubiquitous institutions of self-help, such as *gotong royong* (community self-help), *arisan* or *julo-julo* (rotatings savings groups) and numerous others. In turn this might have prepared the way for joint work through rotating working groups in house construction, sanitation or cleaning of farm land and ponds; or community participation in road repair, terracing and irrigation. Donors should first know about indigenous self-help institutions, then build on them, lest unsustainable external help replaces sustainable self-help. This is likely to slow down disbursement, which is a predicament to donor organizations under disbursement pressure.

Initial analysis should also include a study of potential implementing partner organizations, including NGOs and government agencies, as most donors will be facing the same challenge of needing competent local partners. This would best be done through a review of existing cross-organizational studies, plus a joint survey, resulting in brief descriptions and assessments. Major partner organizations, particularly those that will be involved in services to the cooperative and rural banking sector, may require a due diligence by one or several cooperating major donors.

Decide on what to do and what not: There is a double risk of donors being overambitious: being led by what is desirable rather than feasible, and of replicating approaches that may have been successful elsewhere, but may not be appropriate to Aceh or to the particular situation of a target group in the various stages of transition from relief and rehabilitation to development. Donors have to focus on what is feasible and appropriate, which is easier said than done. Microfinance is no panacea; in the early stages of relief and rehabilitation, institutional microfinance may not be appropriate at all. Clearly decide whether your input is limited to temporary relief objectives, or is to be carried over into sustainable development. If the former, don't meddle with institution-building, which takes longer, unless you find partners who will take over once you leave. If the latter, then outreach and sustainability have to be built into your approach from the beginning, even though your agency may not have the mandate or the resources to do so; perhaps other cooperating agencies can pick up where you leave, provided you have made provision for that and start early looking for development partners. Any effort at institution-building will meet with strong pressure to disburse, from one's own agency or others. Disbursement does not equal effectiveness, though disbursement may be all, or most of, what donors look at to measure aid effectiveness. Aid may be wasted if not properly focused; disbursement in a rush may do more harm than good. Donors have to analyze, test and adjust their approaches before implementing them on a broad scale.

Financial and non-financial interventions, and the institutions handling them, have to be separated. Very different competencies and capacities-to-be-built are required. Grants and loans must not be provided by the same institution lest both staff and recipients will be confused, and any emerging, or pre-existing, credit culture will be undermined. Agencies providing grants should coordinate with those who build local financial intermediaries and establish credit systems, paving the way for a transition from grants to loans as early as possible. They have to be aware of the risk of portfolio contamination, and take precautions accordingly.

Whatever you do, do it well: Else, don't do it at all, or do it jointly with donors or partner organizations who are more specialized or have more capacity. This requires first of all to find out what it takes to do something well. Eg, some donors realized that shortage of funds and portfolio quality were not the fundamental problem of MFIs they were working with. Only after an in-depth analysis did they find out that there were fundamental problems of mandate and governance, and they shifted their emphasis from the financial to the institutional. Others found it far more difficult to rescue projects or MFIs that had gone astray than setting them up right from the start; this however requires multiple inputs such as appropriate institutional models, hardware and software, training, consulting, monitoring and supervision. Many tasks exceed the capacity of a single donor and need to be done jointly, capitalizing on the comparative advantage of each; only few donors have the capacity to do all this. Examples would be the cooperation between GTZ, Asian Development Bank (ADB) and MercyCorps in developing new banking software[4] and standard operating procedures (SOP) for conventional and Islamic rural banks that might also be used by cooperatives; and various cases of cooperation between providers of loanable funds and capacity-building services. Some donors found it more effective to transfer resources to other, more competent donors than disbursing their resources in inappropriate ways. This requires information on other donors and mechanisms of cooperation.

Assisting microfinance rural banks (BPR): Having decided to work with existing financial institutions such as BPR, due diligence must be carried out, covering the total institution and not just focusing on its financial performance. A quick assessment misses too much information. Basic questions have to be clarified first: Is the institution geared to outreach and

[4] The conventional MicroBanker was originally developed by FAO. The Islamic Microbanker, initially developed in response to demand from Aceh, is now commercially available (further information from ralph.houtman@fao.org).

sustainability or channeling of loan funds on behalf of a third party, particularly government? Does the political will exist, or can it be generated, to reorient the institution to self-reliance and profit-making? Is it possible to convince the government, and perhaps donors, that the best way of reaching large numbers of the unbanked with sustainable financial services is not through targeted subsidized loan channeling? Due diligence may arrive at surprising findings. Eg, loan channeling may not be immediately evident. Channeling funds were found to be listed as government deposits and, when disbursed, transferred to clients' deposit accounts, without ever appearing on the active side as loans outstanding. This has confused clients as well as loan officers about the difference between savings and loans, which were rather regarded as grants. This is an import issue in due diligence if government interference is to be kept at bay; and if the poor credit culture of particular types of MFIs is not primarily due to any intrinsic factor but to their use as a preferred instrument of government loan channeling.

Working with BPR in Aceh has required intensive care over an extended period of time. Assistance has had to cover all spheres of the institution, from mandate and governance to MIS and banking software (such as Microbanker, conventional and Islamic), products (such as cash-flow lending), and the development of a variety of tools adapted to the respective needs. Among the benefiting private BPR, technical assistance has been extraordinarily successful, turning the five BPR most affected by the Tsunami (out of a total of eight) into profit-making institutions, with ratings in the top two categories on Bank Indonesia's scale. This assistance must be continued for some time to come, perhaps beyond the official period of rehabilitation and reconstruction. It is not yet clear whether the same success will extend to twelve government-owned BPR yet to be amalgamated into one, which have been far more damaged by loan channeling and are more difficult to protect against government interference. While there was agreement among the donors involved that support functions should be institutionalized in banking associations (such as Perbarindo and Asbisindo), no steps were taken in that respect as this exceeded their mandate during reconstruction.

Assistance to microfinance cooperatives: Given the poor record of cooperatives in Indonesia overall and the damage done to the sector in Aceh by decades of conflict, effective assistance to the cooperative sector, including the cooperatives directly affected by the Tsunami, has been considered a major challenge by everyone involved. Assistance started with a mapping survey upon the request of BRR. Of 1502 financial cooperatives reported in official statistics, only 17 were fully registered as savings and credit cooperatives (Koperasi Simpan Pinjam, *KSP*); the remaining ones were units (*USP*) of multipurpose cooperatives. 708 could be traced, 85 were found to be active, 22 of these Islamic; only a few were found to perform satisfactorily. How best to proceed in a situation of strong disbursement pressure from the government and a culture of non-repayment of government loans? BRR and the Office of Cooperatives agreed to donors choosing a cautious approach. Donors would support the establishment of new microfinance cooperatives; the focus would be on Baitul Qiradh (BQ), an Acehnese term meaning *house of financing,* in order to promote a brand image of well-performing Islamic cooperatives; the legally required social capital of BQs would be raised from a broad local membership (and not just a small number of founding members); and external funds would best be invested in BQ Centers as part of a secondary structure for refinancing BQs with agreed-upon performance standards.

When establishing small local MFIs, one may start either informal or formal. Starting as an informal entity or SHG has the advantage of minimal overhead costs; but growth will be slow, and sustainability will be threatened by the lack of legal status, regulation and supervision. There is little documented experience in Aceh with upgrading informal SHGs into registered cooperatives. In its initial documents BRR together with the Office of Cooperatives had planned to focus on the establishment of SHGs to be capitalized with government resources, eventually to be upgraded to cooperatives. This met with widespread skepticism and was abandoned in favor of disbursement to existing cooperatives, though many of them were subsequently found non-performing.

Alternatively, one may start formal and professional, establishing a BQ as was agreed upon. PNM[5] was found to be the most competent implementing partner, a government corporation specialized on financial assistance and a range of technical support services to Islamic and conventional cooperatives as well as BPR and BPR/S[6], including hardware, software and capacity-building. Establishment and operational costs would be subsidized during a transitional period. Yet, building a small number of well-performing BQs proved to be a major challenge. There was agreement that the establishment of BQs would require adequate resources comprising equity, savings and borrowings to generate enough revenue for cost coverage. There was to be access to private, governmental and donor funds as sources of refinance. Here are some observations:

- Green-fielding requires intensive care by implementing partners including effective supervision, as expected, but more than what was actually provided.
- Even a strong and competent implementing partner (such as PNM) needs capacity-building and institutional strengthening.
- This in turn requires a framework contract, rather than a series of short-term contracts, with an implementing partner, and agreement on phased performance-based allocations of funds
- The implementing partner should be an executing partner agency, rather than a handling agency, with overall responsibility for institutional maintenance, perhaps beyond the rehabilitation phase.
- Target group organizations and their members must be involved in the decision-making process
- Coordinate continually with all relevant agencies. Share information timely among partners at all relevant levels; this requires documentation in two languages (English and Bahasa Indonesia)
- Assure effective information and knowledge management; respond immediately to queries, take action quickly.
- There must be a clear understanding of the terms of cooperation and obligations of the partners before a BQ is established (eg, regarding capital injections as grants, loans or investments and operational subsidies). The partners have to stick to their obligations and promises, particularly with regard to timely capital injections. Legal issues of fund ownership and transfer have to be clarified well in advance.
- The cooperating donor and implementing agency staff have to spend more time in the field than in the office; staff must be located in the field where the BQs are.
- Good practices matter, insistence on best practices may produce worst practices. This means being flexible and adjusting to local conditions, insisting at the same on adherence to basic cooperative principles – a delicate balance, requiring good judgment, compromises and working in steps toward good-practice goals.

Assistance to microfinance self-help groups: International NGOs, operating outside the official development assistance framework, have tended to work with local NGOs as partners and SHGs as local financial intermediaries, which also lie outside the official, or formal, sectors of the economy and financial system. Here are some of their lessons learned[7]:

- *SHGs as local financial intermediaries:* SHGs are local financial intermediaries collecting savings and providing loans to members. In the present stage of reconstruction in Aceh, loans are more appropriate than grants. This requires local capacity to handle them, ie, the formation of groups. Loans encourage responsibility, buy-in and participation on the

[5] Permodalan Nasional Madani, carved out of the central bank’s small credit division after the Asian financial crisis.
[6] Bank Perkreditan Rakyat Sharia.
[7] Freely adapted from: Oxfam International, Aceh/Nias Tsunami Response Partnershisp Programme: Oxfam’s Micro-Finance Partnerships in Aceh: Key Findings & 10 Lessons Learned. October 2006.

part of the borrower and their groups; they have a wider outreach than a few targeted grants, and are more likely to be used productively. They also provide space for resource distribution to be negotiated locally on a group basis, in contrast to externally organized cash interventions, which may create social tensions.

- *Are loans helping livelihoods:* Productive loan use is frequently mandatory. The need for non-productive consumer loans is usually ignored. Urban and market-based loans have been particularly successful. Most loans are in fact used wisely in productive assets and working capital. Many loans have been instrumental in starting or scaling-up small businesses. The resulting increase in earnings has been largely attributed to capital injection. There are tangible economic, and intangible social, effects of SHGs, the latter particularly in the form of empowerment. This has created social capital that will further strengthen the sustainability of microfinance. Compulsory savings are widely used to increase loanable group funds, though this has increased the monthly burden of payments, which may be difficult for the very poor and the cash-strapped; there is little emphasis on the collection of voluntary savings. The potential of SHGs as local financial intermediaries to be linked to banks has not been explored by the NGOs, in Aceh even though there has been a national linkage banking program (*PHBK*) and movement since 1988 that most banks are familiar with.
- *Repayment rates:* Repayment rates, ranging among four NGOs who provided data from 82% to 95%, are not satisfactory, which may be partially attributed to the unstable environment. Partner NGOs have to be more selective and more stringent in their enforcement of loan repayment.
- *Institutional sustainability:* SHGs come at low costs. Their sustainability is questionable; but they may play a useful, albeit transitory, role for many years to come. During the rehabilitation phase many SHGs, particularly all those newly established, come to rely on NGOs whose support is not guaranteed as they rely on external funding.
- *Markets:* The usefulness and sustainability of microfinance will depend on market access, a factor which is rarely assessed. Partners may be trained to assess alternative livelihood sources. In this context, the CEFE small enterprise training offered by GTZ to local trainers on a commercial basis is geared to local microentrepreneurs exploring new market opportunities.
- *Financial accountability, participation, transparency:* Loan funds have tended to be spread over large areas and large numbers of groups. This has reduced community ownership and local checks and balances. Loan funds should be confined to single, or small numbers of, groups in a given community. Some community funds have been observed to turn into an NGO-owned mechanism, which is less transparent and may run into legal problems, as NGOs are not permitted to mobilize savings.
- *Targeting:* Most NGOs reportedly target those directly affected by the Tsunami, who are swamped with loans and grants. Major donors recognize that the majority of the population have been affected by the conflict; and that viable financial institutions should have a wider outreach. A shift is advocated from urban tsunami-affected to rural poor and conflict-affected not to be left behind in Aceh’s long-term development. Special emphasis should be placed on reaching fisheries and agricultural sectors with financial services.
- *Gender:* Gender awareness among NGOs has been found to be poorly developed. Donors and partners may have different ideas about gender sensitivity. As a result, there has been little interest in gathering evidence of differential impact of microfinance on men and women. It is surmised that targeting women-only may ignore household dynamics and an Acehnese sense of social justice, thus leading to social tensions. The exclusion of men by some NGOs does not fit into the concept of inclusive finance.
- *Integration:* Should microfinance be integrated with other development activities or best be left free-standing? Most NGOs include both; but effective implementation of both is mostly beyond their capacity. The emphasis should be on building financial institutions, while coordinating with other agencies who provide business development and other non-financial services.

- *Capacity-building:* Most NGO training has focused on general organizational development and technical capacity-building. There is still a considerable skills gap that needs to be addressed if microfinance is to perform well. Future focus areas reportedly should include assessment and planning, community facilitation, monitoring, evaluation and organizational learning, gender sensitivity in project management, and conflict sensitivity in project implementation.

Loan channeling: In a situation of rehabilitation and reconstruction, many BPRs and cooperatives found it difficult to resist the many offers of cheap and easy money. Some ground rules should be observed: Handle government and donor funds off-balance sheet unless they are given as portfolio refinancing without strings attached. Accept such funds only on the condition of compensation for transaction costs; take no responsibility for (full) repayment. On the passive side register government and donor funds as restricted funds; indicate clearly where these funds appear on the balance sheet when transferred to recipients. Be aware that there is a high risk of portfolio contamination; therefore, try by all means to have these funds converted into equity or portfolio refinancing, to be treated as own loanable funds and then, of course, reported on-balance sheet.

Donor coordination: For effective aid delivery, donors have mobilized partnerships with the private sector, multilateral and bilateral donors, and with international NGOs; many more could have done so had there been a framework for cooperation early on. Several initiatives have been taken by BRR and major donors to coordinate their activities in microfinance: a challenging task. It requires a determined effort, a lead agency taking charge, task forces with their own specific agendas, regular meetings, and the will to cope with frustration. Effective coordination takes time; so donors have to budget for it, expecting a return for their time input. In a number of cases coordination has led to cooperation and integrated actions. Some activities have led to services available to institutions assisted by a variety of donors, such as the *Microfinance Innovation Fund* established by ADB available to all BPRs and BQs. There has been little visible coordination with, or among, small donors: an unresolved issue. This would require a special effort; more work needs to be done in this respect. It is feared that their inputs have remained scattered and unsystematic.

Donor preparation for coming disasters: Big organizations should have a joint concept in advance, being prepared for future disasters. So far, joint initiatives in that respect, as in Great Britain, seem to be more concerned with fund raising than effective future implementation on the ground. Preemptive coordination would allow for longer-term planning and more effective cooperation from the outset. Also, they should realize that reconstruction cannot be done in a year or two, and that big chances are being missed if no preparation is made for the ensuing longer-term development needs.

Information sharing: Over time numerous studies were carried out on a wide range of topics, usually proprietary to the agency that paid for them. A joint microfinance website, preferably interactive, with links to more specific webpages (such as www.aceh-microfinance.org/, would be an effective instrument of information sharing. This should contain feasibility studies, project information (preferably in a part-standardized format as developed by a group of microfinance donors), and recent studies and reports on Aceh. In addition, this could also contain existing studies on microfinance in Indonesia prepared by some of the donors in prior years; they could have been quickly assembled even before the start of projects. The website would have to be updated regularly. A task force would be needed for periodic summaries and tabulations of key aspects of microfinance projects. By the end of 2007, an internet search led only to scattered information. Without a well-maintained website, many are still not be aware of the results of the MFI mapping survey or of a study of SHGs and their potential for loan channeling, bank linkages or upgrading as local financial intermediaries, both done in 2005. Meanwhile, many donors arrived at their own approach to SHGs, frequently based on a view through the lens of their partner organizations rather than comprehensive analysis.

Sharing tools: Some donors have shared or jointly developed tools and instruments, to everyone's benefit, as in the case of the FAO/GTZ *Microbanker* adapted jointly with MercyCorps to the requirements of conventional and Islamic BPR in Aceh (marketed by Micra, a newly established microfinance service provider in Jakarta). Many more tools exist in the hands of donor agencies and their partners which are not generally available. Sharing them would provide a basis for their improvement and perhaps harmonization. Some tools are free, others are combined with installation and maintenance services and come at a price; examples are the MIS and SOP for BQ by PNM and the Microbanker. In either case, short descriptions and references to institutions in charge available on a website would be useful. This might motivate some donors to professionalize and commercialize their tools and services, building local capacity in their partner organizations to disseminate the tools, and provide maintenance services.

When to cooperate, and not to cooperate, with government: A major unresolved policy issue pertains to the question whether there should have been closer cooperation of donors with BRR in the microfinance cooperative sector as requested by BRR as early as 2005. BRR reports that in 2005 there was little or no collaboration from donors, particularly many of the smaller ones, who, under disbursement pressure, just wanted to disburse. BRR admonishing donors not to spend but to plan first did not help. Similarly, donors, particularly some of the bigger ones, admonishing government agencies, equally under disbursement pressure, not to disburse large sums to non-performing cooperatives at the end of 2005, and then again in 2006 (*We did not have the luxury of not disbursing,* was given as an explanation), did not help. GTZ did respond to a request by BRR to carry out a mapping survey of the microfinance sector and subsequently a due diligence of microfinance cooperatives, both in 2006. The result of the decision of donors to stay away from non- or poorly performing cooperatives has been the shifting to serious institution building efforts of the government from 2005/06 to a future point in time, intending, without disbursement pressure (the Aceh Microfinance Innovation Fund having an unlimited life expectancy) to put the sole focus on capacity-building of cooperatives. Should donors have cooperated with BRR as early as 2005, abandoning their adherence to *best practices* and making the best of the unavoidable disbursement of government funds to cooperatives – not applying *good* or *satisfactory practices*, but still better than *no practices* of any standard? This is a dilemma which donors will have to confront realistically.

Policy dialogue at sectoral level: Successful restructuring and reform of the BPR and the cooperative/BQ sectors require engagement in policy dialogue of major donors involved to create a conducive policy environment and effective supervision. In the case of BPRs this implies enforcement of prudential regulation after the end of a Tsunami-related moratorium, on 31 January 2008, agreed upon with Bank Indonesia as the regulator and supervisor. Non-performing banks should have been closed long before the Tsunami, as has been the case in other parts of Indonesia, but have been kept alive, sometimes at enormous cost as in the case of public BPRs in Aceh.

Similarly, the vast majority of cooperatives, many of them not even registered throughout Indonesia including Aceh, should have been closed. Restructuring and reforming the cooperative sector would imply the transformation of a state-aided sector into a genuine self-help movement, starting with the transfer of the functions of the Ministry of Cooperatives & SMEs to a self-organized structure of apex organizations. This would also have to include the establishment of a separate financial authority, unless the decision would be taken to bring financial cooperatives under the supervision of the central bank (as for example in Vietnam). In the absence of the political will to do any of these, incipient policy dialogue in Aceh has focused on separating a sub-sector of newly established BQs from the rest of the cooperative sector and doing all of the above. In particular, preliminary discussions were held about the desirability of a separate cooperative law on BQs in Aceh as part of Qanun, a special legal framework for Aceh, and the establishment of a separate financial authority for the BQs under that law. This however is a long-range agenda, for which the donors are not prepared in a setting of reconstruction.

Some preliminary steps have been taken toward the development of the microfinance sector in Aceh, such as establishing the Aceh Microfinance Forum for mutual dialogue in 2005, converted into, or followed by, the Aceh Microfinance Center as an apex in January 2007; the Coordinating Forum for Aceh and Nias (FFAN), with a task force on Access to Finance; the Aceh Microfinance Fund (MIF) as a refinancing apex; and the founding of Aceh International Society of Microfinance subsequently launched as a school (supported by ADB) with training, advisory, research and development services, in collaboration with Syiah Kuala University's microfinance program (supported by GTZ).

The policy dialogue on sustainable microfinance in whatever institutional form will have to confront a political conflict of objectives: between social-political objectives (of disbursement and outreach to particular target groups) and economic objectives (of profitability and sustainability). This is an issue pertaining in particular to the public BPR, which are technically bankrupt and will almost certainly require a compromise between prudential and political feasibilities given the special situation in Aceh.

One of the most frustrating aspects in policy dialogue is ***the seeming absence of learning from lessons learned,*** particularly from decades of negative experience with government interference, loan targeting and interest subsidies. Large numbers of subsidized programs (30 out of 34) were closed in 1990, to be followed by new programs at the next politically convenient opportunity. Throughout Indonesia, there has been a lack of consistency in policy support for sustainable banking and non-bank microfinance, though Bank Indonesia has been increasingly insistent on prudential bank performance, and has closed or amalgamated many commercial and rural banks after the financial crisis of 1997/98. Subsidized funds, from government as well as from donor sources, continue to be widespread in Aceh; cheap money to be lent at subsidized interest rates has been undermining institutions striving for sustainability. For good reasons, one of the most successful banks in microfinance, majority government-owned Bank Rakyat Indonesia, has stayed away from government and donor resources. Many donors in Aceh have aggravated the situation with cheap and easy money.

In Aceh policy dialogue on sectoral and institutional development in microfinance has to involve the central bank, government and donors. The task of policy dialogue toward a conducive environment, and continued technical assistance to the microfinance sector in its various forms extends beyond the period of rehabilitation and reconstruction and will present a major challenge not yet adequately addressed by the donor agencies involved, particularly the multilateral and bilateral ones. This is an obvious conclusion that the donors involved should have been aware of from the outset. Whether, and how, to convince donors in emergency situations of the necessity of addressing development implications in a wider policy and sustainability framework is an issue requiring further dialogue.

How to go about learning lessons: This presentation of lessons learned is but a first step. It should be followed by a more systematic and comprehensive effort as a participatory process around the turn of 2009/10. It may be carried out by a consortium of government and donor agencies. Bank Indonesia would be involved as the guardian of the financial sector, BRR as the agency responsible for coordinating rehabilitation and reconstruction, and Bappeda, the regional planning authority in charge of the overall follow-up after the closing of BRR. One of the major donors should be selected as a lead agency, assisted by (at least) one Indonesian and one international consultant. The feasibility of subgroups – eg, for banks, cooperatives and SHGs, or for donor categories – would have to be discussed.

This venture would have been greatly aided if provision would have been made early on for a participatory process geared to drawing lessons learned every year-end, to be revised in the following year. Those involved would keep an eye on continually learning and discussing lessons throughout the year. This at least is one lesson learned and to be applied at coming calamities: establishing early on a forum or consortium of agencies for learning and disseminating lessons, with their own website, using and adapting a framework as an outcome of a mutually agreed upon participatory process.