



ISLAMIC DEVELOPMENT BANK GROUP



IDB Group and the Republic of Indonesia

Unleashing the Potential of Indonesia

Overview of IDB Group's interventions in Indonesia

Indonesia joined the Islamic Development Bank as a founding member in 1975. Subscribed capital in IDB is Islamic Dinars (ID) 406.480 million (2.70%) (equivalent to US\$594.22 million). In addition, Indonesia is a member of other entities of IDB i.e. International Islamic Trade Finance Corporation (ITFC), Islamic Corporation for the Development of the Private Sector (ICD) and Islamic Corporation for Insurance of Investments and Export Credits (ICIEC).

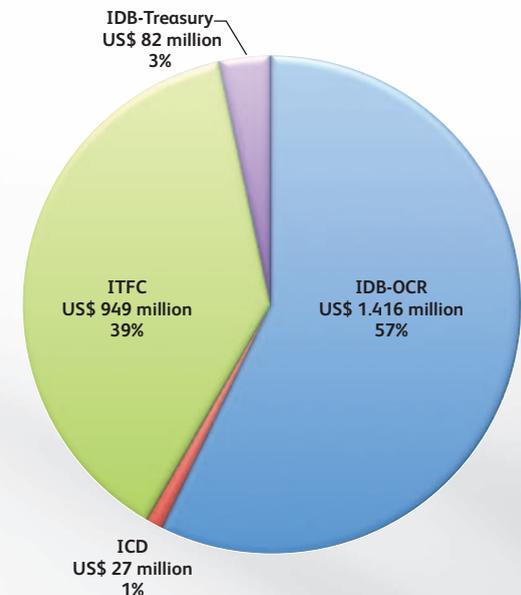
IDB Group continues to provide financing to Indonesia through these arms in private sector development, trade finance for strategic commodities and insurance of investments and export credits.

IDB Group operations in Indonesia can be

divided into three main categories: IDB-OCR operations (Ordinary Capital Resources), Private Sector Operations, and Trade Financing Operations. Since IDB does not provide budget support lending, the bulk of the IDB financing went to public sector projects and trade financing.

As of end of March 2011, IDB Group has provided Indonesia with a total financing of around US\$2.5 Billion for 159 operations with allocations for Group entities shown in the following chart. Islamic Development Bank and ITFC are the largest development partners of Indonesia with 58% and 41% of total IDB Group resources.

Chart: IDB Group Operations by Entity in Indonesia



IDB-OCR Financing to Indonesia

The Islamic Development Bank has provided financing to Indonesia in Infrastructure development, Human Development, Agriculture and Rural Development, Development of Small and Medium Enterprises and Islamic Financial Services Industry Development.

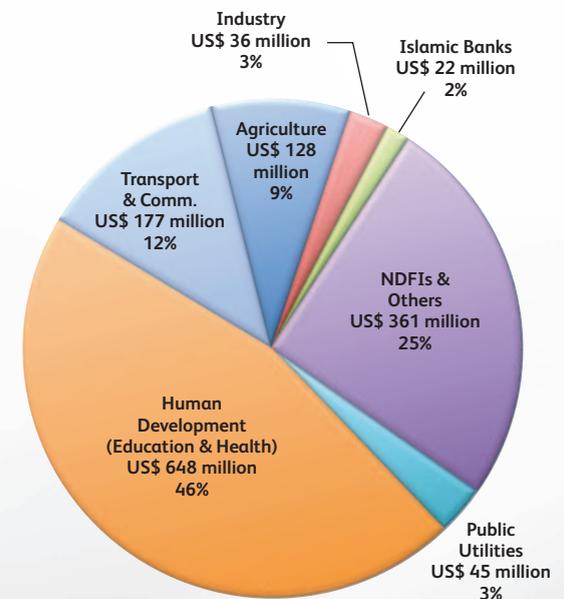
As of end of March 2011, the Bank's OCR approvals for Indonesia amounted to a total value of US\$1.4 billion for 101 ordinary operations of which 41 operations (US\$ 869.3 million), are active while 58 operations (US\$ 635.0 million) have been completed.

Financing from IDB-OCR is heavily tilted, in regional terms, towards Java & Bali and Sumatra regions, and, in sectoral terms, towards tertiary education.

As depicted in the following chart, most of the IDB financing has been concentrated in Human Development (support for Higher Education), Infrastructure for Public Utilities and in Agriculture reflecting the strategic priorities of the Government of Indonesia.



Chart: Sector-wise Breakdown of IDB-OCR Operations in Indonesia



IDB-OCR Operations by Mode of Finance

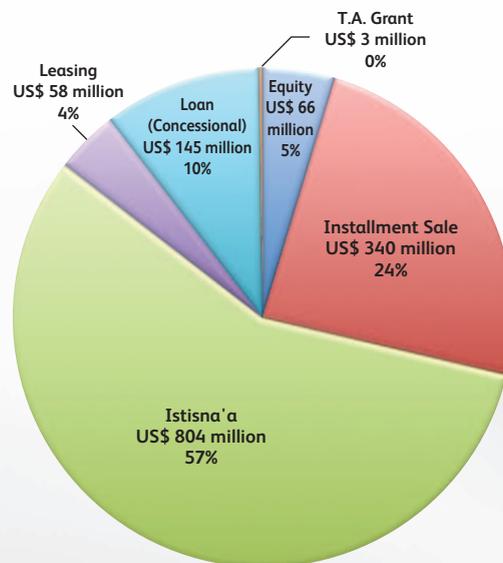
IDB-OCR operations by mode of financing is presented in the following chart. Around 57% of the IDB operations have been financed through Istisna'a while around 24% are through Installment sale reflecting the fit and flexibility of Islamic financial instruments with regard to IDB's areas of assistance.

In terms of partnership with other donors in Indonesia, IDB has leveraged co-financing in the ratio of \$1:\$3.3. About 59 percent of the education sector approvals were committed to Islamic education institutions under the Ministry of Religious Affairs whilst 41 percent was committed to institutions under the Ministry of National Education.

Since inception, IDB's special assistance to Indonesia accounted for US\$ 4.4 million. This comprised of 44 scholarships given to

students amounting to US\$ 1 million, and support for relief operations in earthquakes of 2004, 2005, and 2006 amounting to US\$ 3.4 million.

Chart: Mode-wise Breakdown of IDB-OCR Operations in Indonesia



1). Private Sector Operations

Since their inception, various private sector arms of the IDB Group have also played an active role in Indonesia. **Islamic Corporation for the Development of Private Sector (ICD)** has been active in Indonesia since 1428H and has approved a total of six operations, of which one has been completed and five are on-going. Total financing for these operations amounted to US\$26.8 million. These operations have been for telecom and energy sectors and line of financing for the SMEs. **Islamic Corporation for the Insurance of Investment and Export Credit (ICIEC)** has issued approvals for insurance cover for Indonesian imports and exports amounting to US\$33.98 million. **International Islamic Trade and Finance Corporation (ITFC)** has also been active in Indonesia since its inception. Trade financing amounting to US\$949 million, or 39 percent of total Group portfolio, was approved for Indonesia.

Strategic Shift in IDB Partnership with Indonesia

With the adoption by IDB Group of “Strategic Agenda for the Medium Term” in 1994, a three-year rolling operations plan based on Country Assistance Strategy Studies (CASS) – a comprehensive diagnosis of the development challenges facing the country – was formulated. The CASS selected a set of projects linked to the country’s development strategy and



based on the Bank’s possible areas of interventions.

During the early years of its engagement with the country, IDB focused its support on public sector projects and trade financing. Prior to the Asian financial crisis of 1997 - 1998, the Indonesian economy was experiencing rapid economic growth funded by oil/gas and forestry revenues, loans from MDBs, and foreign direct investment. IDB was one of the main donors during the period preceding the Asian financial crisis. During the two decades before the Asian financial crisis (i.e. 1976 - 1996), IDB approvals in Indonesia were dominated by trade financing, accounting for 41 percent of total approvals. The project portfolio,

on the other hand, was dominated by social sector (education & health), which accounted for 18 percent of total approvals, followed by transport and communications (14 percent), agriculture and rural development (10 percent), industry & mining (9 percent), public utilities (5 percent), and NDFIs/Islamic banks (3percent).

The bulk of IDB committed funds to Indonesia was approved during the post-crisis period, 1998 - 2011.

This trend clearly highlights the structural transformation of IDB operations in



Indonesia. The post-crisis period is characterized by increased financing to all sectors, except industry and mining which did not receive any financing. In particular, approvals to social sector increased from 16 percent to 46 percent of total approval. The bulk of funding for social sector went to education. On the other hand, support to health, agriculture, and transport & communication also increased in absolute value but decreased in relative term.

The trade financing operations increased from US\$162 million in 1998 to US\$949 million in 2011.

The post-crisis period is also characterized by IDB's relief support to the people affected by the Tsunami that struck Aceh and Sumatra in December 2004. The Tsunami package targeted the Housing & Urban Development sector, focusing on construction and rehabilitation of infrastructure devastated by the Tsunami.



Member Country partnership Strategy for the Republic of Indonesia 2011 - 2014: Harnessing the Regional Potential

In the post-reform IDB, the 'Member Country Partnership Strategy (MCPS)' has been adopted as the IDB Group's principal engagement tool with member countries.

The MCPS aims to achieve alignment between the medium term strategic priorities under IDB Vision 1440H and the member countries' development priorities. The MCPS for Indonesia was endorsed



by the IDB BED and the Government of Indonesia at the end of 2010. In the context of achieving "balanced and inclusive growth" as set out in the country's mid-term development plan, and based on in-depth country and sectoral diagnostics, the strategy focuses on harnessing the regional potential of Indonesia through four core engagement areas (Multi Sector Work Program): (i) addressing agriculture and rural development needs, (ii) addressing education and skill development constraints, (iii) addressing infrastructure constraints, and (iv) addressing private sector development needs. In addition, IDB support will include area focused programs selected on the basis of (i) poverty incidence, (ii) HDI ranking, (iii) investment climate, and (iv) cost of doing business. The IDB work

in Indonesia will encompass Cross Cutting Pillars of (i) Islamic finance, (ii) Partnerships, (iii) Capacity development, and (iv) Reverse linkages.

The overall MCPS Program sought alignment and selectivity with 'Regional Strategies and Priorities' of the Second Plan. It covers Java-Bali region (termed as the National-level Programs) and Sumatra, Kalimantan and Sulawesi (termed as the Regional-level Programs). Achieving focus was guided by four sets of inter-related considerations: (i) spread of geography and the sheer volume of required investments; (ii) identification of binding constraints, based on diagnostic studies, in Core Engagement Areas; (iii) identification of knowledge-, financing-, and partnership-based delivery mechanisms;

and (iv) consultations process at different levels and stakeholders.

Diagnostics on growth, poverty and sector level challenges and priorities for Sumatra, Kalimantan and Sulawesi regions were carried out. A key insight of the diagnostics was that interregional disparities in Indonesia cannot be addressed by only basing economic activities on regions' natural resources. In fact, supportive policies and adequate public investments are required to provide low cost access to critical inputs, such as electricity and skilled labor, and building a highly efficient interregional connectivity to attract new industries.

On the basis of the diagnostics of binding constraints, mapping between the Regional Priorities of the Second Plan and the IDB Group Strategic Priorities, the four Pillars together with four Cross-Cutting Areas are expected to help accelerate growth drivers at the regional level.

The MCPS Program supports emerging

developmental opportunities at the regional level in critical areas such as building of highly efficient interregional connectivity; urban development particularly focusing on well organized urban land markets, water supply / distribution networks; achieving food security through agriculture and rural development; and assisting the private sector development, particularly the SMEs, through low cost access to critical inputs such as skills development of the workforce, electricity and investment / trade financing.

Building on past successes and lessons learnt, the MCPS Program is expected to be further augmented by knowledge and financial resources under the two major Cross-Cutting Areas: (i) leveraging Islamic finance, and (ii) mobilizing Partnerships. In particular, IDB Group will optimize its institutional knowledge to support accelerated growth of Islamic financial industry in Indonesia through the development of an Islamic financial architecture, including augmenting efforts to further deepen the Islamic capital market.

The indicative (notional) financing envelope for the MCPS period 2011 - 2014 has been estimated in the range of US\$ 3 - 3.3 billion. In line with sectoral strategy, the distribution of the indicative envelope is planned as follows: the private sector development is expected to receive maximum share of 34.7%, followed by infrastructure at 26.3%, education and skills development at 19.8%, and agriculture and rural development at 17.5%. The regional distribution of the indicative envelope is 64% for financing programs in the three selected regions viz. Sumatra, Kalimantan and Sulawesi. About one-third of the total indicative financing is expected to be provided by the private sector financing Entities of IDB Group.



Private Sector Development

International Islamic Trade Finance Corporation (ITFC)

As trade plays an increasingly significant role in Indonesia's economic success, the IDB Group continues to support strengthening the competitiveness and marketability of this sector. This is reflected in the diversity of the trade financing portfolio which has covered agriculture, petroleum, petrochemical, marine and financial sectors. The total trade finance portfolio of the IDB Group has grown to US\$949 million as of end of March 2011.

Before the establishment and commencement of business activities by

ITFC at the beginning of 1429H/2008, Trade Finance and Promotion Department, under the IDB Group, approved a total of US\$662 million of trade financing for Indonesian public and private sector entities. Some of the notable projects include:

- Trade financing for Pertamina for US\$100 million; and
- Fives Lines of Financing amounting to US\$92.0 million for banks including Bank Mandiri, Bank Syariah Mandiri, Bank Eskpor, Bank Negara Indonesia and Bank Rakyat Indonesia.

IDB's trade financing has also played a significant role in promoting the growth of Islamic banking in Indonesia. The trade

financing for Pertamina is considered one of the first Islamic financing structure in Indonesia. Since early 2000s, IDB has introduced and promoted Islamic banking products and principles to the banks in Indonesia through Lines of Financing thus enhancing their skills, capabilities and product range.

ITFC Focus on Business Competitiveness

ITFC has a renewed focus on enhancing the business competitiveness of trade finance in Indonesia. One of the key sectors is the agriculture given its export potential and beneficial impact on rural employment and poverty alleviation. This focus in line with the drive towards boosting intra-OIC trade volumes in pursuance of targets set under the Makkah Declaration.

Being a major commodities producer among IDB member countries, Indonesia continues to support growth in the ITFC trade finance portfolio. ITFC is gradually building up its portfolio in the commodities sector in Indonesia.

In 2009, ITFC financed a sugar refinery for its imports of raw sugar under a Structured Murabaha Trade Financing. This deal was widely recognized as one of the ground breaking deals in Indonesia for its innovative structure in Islamic finance and it was also awarded as one of the “Deals of the Year” by 3 globally reputable Trade Finance Magazines. This deal has also paved the way for the Islamic banks in Indonesia to finance the commodities sector and compete on an equal footing with the conventional banks in Indonesia.

In 2011, ITFC extended financing to the cooperatives and exporters in the coffee growing region of Takegon, Aceh. Six Coffee Cooperatives working together with the exporters are benefiting from

this tailored made financing. This is part of ITFC’s effort to directly impact the lives of the farmers in the export oriented agricultural sector and this is in line with the MCPS for Indonesia to reduce regional disparity by supporting their trade finance needs.

Photos with Coffee farmers



Raw Sugar financing in Indonesia



Islamic Corporation for the Development of the Private Sector (ICD)

ICD has approved a US\$50 million line of financing for targeting SMEs in member countries of Southeast Asia region. Indonesia is expected to absorb the bulk of this line of finance channeled through banks and finance companies. ICD line of finance is intended to remove critical constrains in access to credit for SMEs as they are increasingly becoming the driver

for economic growth. The strategy of supporting SMEs development is in line with ICD's current focus on providing investment and advisory services to financial institutions such as banks, ijarah and investment companies and takaful providers.

As of end of March 2011, US\$8 million of line of financing has been disbursed and serviced by PT Mandala Multifinance while US\$10 million for PT Mandala has been approved. The ICD is syndicating a further US\$20 million to other financial institutions.

In order to support the development of critical infrastructure as part of the IDB Group's strategy for Indonesia, the ICD has signed MOUs with PT Jamsostek and PT SMI to establish Islamic Investment Fund and Islamic Infrastructure Investment Company. The ICD has also allocated US\$13 million to PT Powertel to develop backbone telecommunication infrastructure. Further, the ICD has provided facilities for PT Dimas in a geothermal project in North Sulawesi.

ICD is currently in the process of arranging a major Islamic Syndication Facility for a rayon plant that would support the development of textile industry. While continuing to reach out to more SMEs through lines of finance, the ICD will be involved in providing advisory services in Indonesia to banks and companies that are soliciting investments and those that are planning to expand abroad especially in 48 ICD member countries.



The Islamic Corporation for the Insurance of Investment and Export Credit (ICIEC)

Since inception, the Corporation has issued approvals for insurance cover in favor of 9 exporters from Saudi Arabia, Kuwait, Tunisia and Malaysia amounting to around US\$36 million to cover their exports to Indonesia.

ICIEC is also considering 8 applications for investors from Kuwait Bahrain, Japan, Saudi Arabia, United Kingdom and Singapore totaling US\$832 million to cover their investment in Indonesia.



Knowledge Delivery

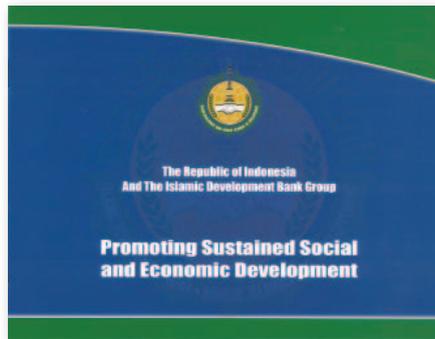
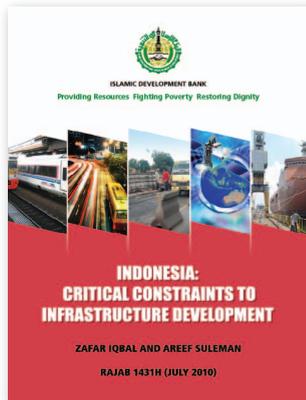
In addition to its assistance in the form of OCR funding and private sector development, IDB Group has been active in delivering knowledge products to Indonesia. In this regard, Islamic Research and Training Institute (IRTI) has carried out a number of research and training activities during last three decades. The first ever activity of IRTI in Indonesia was a training program on 'project implementation and supervision' that was held in 1989. Altogether, a total of 12 training activities have been organized by IRTI in Indonesia, in close collaboration with government agencies, universities, and partners in the banking sector. Majority of these trainings, held during 1999 - 2008, were focused on Islamic banking and Financial sector.

Research activities of IRTI mainly comprised of conferences, seminars, forums, and roundtable discussions. The first research activity was a seminar on Islamic Banking and Finance in 2003. Since then, a total of nine research activities have been conducted. As part of these research activities, International Conference on Islamic Capital Markets was held in Indonesia in 2010, in collaboration with Securities Exchange Commission of Indonesia and Malaysia.

Some examples of other knowledge products that IDB Group has delivered to Indonesia include a recent study on critical development constraints, which was jointly carried out by IDB, Asian Development Bank, and International Labour Organization.



Knowledge Products of IDB Group for Indonesia



Special Initiatives and Humanitarian Relief

Asian Financial Crisis

During the Asian financial crisis which occurred in 1997 - 1998 and severely affected the Indonesian economy, IDB played an important role, especially when other multilateral and bilateral financial institutions were hesitant to invest in Indonesian capital market given the uncertain environment. IDB approved two facilities: Mudaraba facility of US\$25 million, of which half was actually disbursed, and Murabaha facility of US\$75 million. Investments were made through DANAREKSA for the purpose of investing in shares quoted in Jakarta Stock Exchange. These timely investments by IDB helped to sent a positive signal to the local and foreign

investors about the medium term economic prospects of the Indonesian corporate sector.

Relief and Reconstruction Package after Tsunami

IDB stood shoulder to shoulder with Indonesian people in the aftermath of Tsunami in 2004. It quickly responded to the emergency and launched its relief operations to cope with the severe impact of the Tsunami, in both urban and rural areas of Nangroe Aceh Darussalam. In addition to an urgent relief of US\$3 million, six OCR operations (amounting to US\$97.73 million) and two trade operations (amounting to US\$40 million) were approved. OCR

approvals in the Tsunami relief package were in the sectors of education, agriculture, and transportation. In addition, IDB is also managing the Saudi Charity Campaign Fund for Tsunami, amounting to US\$44.65 million allocated for 7 projects.

Kafala Program

In the aftermath of the Tsunami in 2004, the OIC and the IDB launched a campaign to pool resources from member countries for safeguarding children victims of the Tsunami.

OIC Alliance Field Office was subsequently established in May 2006 in Banda Aceh for overall coordination and implementation of the «Tsunami Orphan Kafala Program» in particular to provide necessary care for the orphans.

The financial and humanitarian support for the Kafala program has been provided by a number of IDB Member countries,

NGOs and philanthropists. This program is planned to run over fifteen years in order to benefit a total of 25,000 orphans. The implementation partner is Baitulmaal Muamlaat (BMM).

This is a pioneering program which plans to meet the overall needs of the orphans until they grow up to become self reliant and useful members of society.



IDB & OIC Mission Team visiting to Krueng Seumiden region project YTM-0002 Pidie on 2 October 2010

West Sumatra Earthquake in 2009: IDB provided US\$1.2 million. The QRCS in partnership with Indonesian Red Crescent, and Islamic Relief Indonesia, with UNICEF, UN OCHA are implementing the assistance program in the Province of West Sumatra, Indonesia.

2010 Tsunami in West Sumatra-Indonesia: The Bank has approved, in October 2010, an emergency grant amounting US\$ 200,000 for the relief efforts. Project is under implementation by the QRCS which will also provide additional US\$ 100,000.



Vocational Training in Indonesia

In 1995, IDB approved a vocational training project in Indonesia. The project aimed at reducing poverty among the families of the Madrassah students who were predominantly poor, by preparing graduates to seek gainful employment in public and private sector industries. The students studying in Madrassahs were from the poor families who could not afford to send their children to the academic institutions and schools of the Ministry of National Education, and had very limited chances of receiving higher education or good jobs. The IDB's assistance was for the establishment of vocational training workshops in 82 Madrassah Aliyah in 27 provinces. The project was financed by IDB leasing and instalment sale financing of US\$18.2 million (76 percent) and Government of Indonesia (GoI) financing of US\$5.6 million (24 percent).

The project facilitated the construction of vocational workshops equipped with necessary tools and machinery for vocational training. It was completed in December 2001 and became fully operational in the beginning of the 2002 - 2003 academic year. The project was able to significantly improve both student enrolment and generate employment opportunities for the Madrassah Aliyah graduates. It contributed to increasing the total enrolment in the vocational training program from 550 students in 1995 to 82,333 in 2003 for all 575 public Madrassah Aliyah in 30 provinces. The introduction of the vocational component in Madrassah education system has led to a significant reduction in the drop-out rate for the last two years, and in the 12 Madrassahs Aliyah the drop-out ratio reached almost zero of the enrolled students. The project has enabled Madrassah Aliyah graduates to seek employment in the private or public sectors or become self-employed. The track record of students after graduation shows that almost 72 percent of Madrassah

Aliyah graduates are either employed or got enrolled for higher education.

An IDB post-evaluation study, undertaken in May 2004, rated the project as successful in terms of achieving its objectives.



IDB's Role in Strengthening the Performance of Bank Muamalaat Indonesia (BMI)

BMI was established in 1991 at the initiative of the Indonesian Council of Ulema and later supported by a group of local entrepreneurs and Muslim intellectuals. It started its operations in May 1992 with a paid-up capital of IDR89.8 billion. The BMI focused on the provision of Shari'ah-compliant financing facilities. The BMI customer base comprised of small and medium size enterprises (SMEs) and retail consumers.

During the Asian financial crisis, BMI suffered a major increase in its non-performing loans, leading to a substantial write-down of its paid-up capital. At this critical juncture, IDB was invited to participate in the equity capital of BMI. In June 1999, IDB acquired



a stake in BMI with an initial investment of US\$2.7 million with a view to strengthening the financial position of the BMI at a critical time. The main aim of IDB's participation in the capital of BMI was firstly, to ensure continued survival of the Bank during the Asian financial crisis and, secondly, to stabilize the fundamentals in order to lay foundations for future growth.

In 2003, IDB acquired additional equity stock in BMI equivalent to \$6.3 million, which increased its stake to one third in the paid-up capital. IDB supported upgrading of the BMI's Strategic Business Plan as well as to conform to the prudential framework

of the Bank Indonesia (the central bank). The key BMI business initiative was to enter into an alliance with the Indonesian postal network to offer banking facilities at the retail level. Over a short period, BMI succeeded in attracting new domestic investors, depositors and clients which helped the Bank grow its operations significantly and to become a profitable entity.



In 2005, IDB invested a further US\$4.9 million for a total stake of US\$13.9 million. IDB also invited Boubyan Bank (based in Kuwait) and SEDCO (a private wealth management based in Jeddah, Saudi Arabia) to participate in the capital of BMI to further enhance the shareholder base. As of end-2009, IDB held 28 percent of the BMI's Paid-up Capital.

BMI rapidly expanded a network of branches, sub-branches and cash offices through which it offers its clients a wide range of products and services such as retail and corporate financing, foreign trade, debit cards, demand and time deposit accounts,



FX trading, local and international money transfer etc.

BMI has now successfully established itself as a solid reputation as one of the premier Islamic banks in Indonesia. Its target is to not only become the leading Islamic bank but also to grow to rank among the top Islamic banks in the South East Asian region.

IDB's participation in the paid-up capital is in line with its strategic thrust to establish and expand the Islamic financial services industry by supporting establishment of well-capitalized Islamic financial institutions. IDB's support to BMI is a successful example of rehabilitating Islamic financial institutions facing operational difficulties. Through proper diagnostic assessment and demonstrated support by way of making available equity investments at the appropriate time, it is indeed possible to revive fledging Islamic financing institutions even in a highly competitive banking environment.



Community Driven Development

IDB is supporting the Government of Indonesia (GOI) in the National Program for Community Empowerment ('PNPM-Mandiri') in 14 Provinces across Indonesia. It is one of Indonesia's flagship poverty reduction programs.



The overall objectives of the project are to:

- (i) improve the socio-economic conditions of communities in the targeted areas, especially women and the poorest, through physical, social and economic interventions, and (ii) build capacities & skills of communities and local institutions.

IDB was requested to cover 4871 urban villages (Kelurahan) in 111 districts of 14 provinces across the whole of Sumatra, West Java and West Kalimantan.

Community Driven Development

PNPM-Mandiri adopts a highly successful approach to poverty reduction called

Community Driven Development (CDD), which gives direct control of decisions and resources to the communities themselves. CDD (largely pioneered & promoted by the World Bank), treats poor people as assets & partners in the development process, rather than mere recipients, and builds on their institutions & resources.

Integrated Community Driven Development

Moving beyond the basic CDD concept, the Integrated CDD (ICDD) model, adopts a more holistic approach pro-

actively targeting the poor and women in particular. ICDD places greater emphasis and effort on developing the economic and livelihood sectors of the community, through enhanced community capacity building, vocational/ skills training,

facilitation on developing market and trade linkages, and micro-finance support.



