I. Introduction and Context

Country Context
1. Over the past decade, Indonesia has sustained strong economic growth year on year. Despite the global and domestic economic challenges in recent times, such as the 2008-9 global recession, the current euro sovereign debt crisis, the effects of the Japanese earthquake and tsunami, and the increases in international commodity prices and domestic food prices, Indonesia is on course for 2011 to maintain its strong growth performance currently projected at 6.4%, which is even higher than the 6.1% growth in GDP it achieved in 2010. At the same time Indonesia has transformed this growth into substantial poverty reduction and has already achieved the target MDG of halving the incidence of extreme poverty from 20.6% of its population in 1990 to 5.9% in 2008.

2. Notwithstanding such solid economic performance, Indonesia continues to face significant challenges in developing its infrastructure for the 21st century and is now at a critical point where its relatively poor levels of infrastructure development are holding back its growth potential and further poverty reduction efforts. For example, Indonesia’s quality of infrastructure in general and access to improved sanitation in particular, continuously rank at the lower end when compared to similar middle income countries in the region.

3. Recognizing these issues and backed with its sustained strong economic performance, the Government of Indonesia is committed to addressing its infrastructure challenges as one of its priorities. This commitment is demonstrated in the current medium term development plan (RPJMN) for 2010-2014 which sets a range of infrastructure development targets to be achieved by 2014 that include targets to improve access to higher quality sanitation to meet the MDG targets. In addition, improving infrastructure is also at the center of the Master Plan for the Acceleration and Expansion of Indonesia’s Economic Development 2011-2025.

4. The prioritization of infrastructure spending is also seen in recent budget allocations. For instance in 2011, the budget allocation to capital expenditure was increased by 40% relative to the revised 2010 budget. However, overall levels of investment in infrastructure as a percentage of GDP have not risen to the pre-1997/1998 crisis levels of 8% of GDP, but were around 4% of GDP in the 2007-2009 period.

Sectoral and Institutional Context
5. The solid waste management sector in Indonesia today is under extreme stress mostly due to population pressure in urban areas and is in a state of crisis. For instance, there are approximately 110 million Indonesians (nearly half of the population) living and working in urban centers today who collectively generate some 85,000 tonnes/day of solid waste, out of which only 34,000 tonnes/day are collected and disposed in landfills. This means that 51,000 tonnes/day of solid waste remains uncollected in urban areas in Indonesia today. This uncollected waste ends up either on city sidewalks where it is openly burned contributing to local air population problems, or in the storm drainage and sewer systems where it causes significant blockage and flooding. These poor sanitary conditions serve as ideal breeding grounds for disease vectors thereby creating additional public health challenges for the cities to deal with, and further reduce quality of life for the urban population.

6. These issues have contributed to the urban populations demand for improved solid waste management services from their municipal governments whose responsibility it is to provide these services. However, service delivery and revenue generation and collection have not kept pace with increasing quantities of waste that have resulted from large urban population and economic growth. As a result, cities are unable to cope and most landfills in Indonesia follow the practice of open dumping. The poor design
and management practices of these open dump landfills result in unending leachate flows and uncontrolled emissions of methane, a greenhouse gas (GHG) that is generated through the anaerobic degradation of organic matter.

7. The demand for improved services has put significant political pressure on local elected officials which, in turn, has led to a number of significant policy changes to help address these challenges. For instance, the Ministry of Public Works (PU) in 2006 issued regulation (21/Prt/M/2006) outlining a number of policy and strategy measures for improving solid waste management systems during the planning period 2006-2015. The 2006 regulation set out a number of measures which include a target for increasing collection from 40% to 70% by 2015 and a five year time horizon for closing all open dump landfills or upgrading them to more controlled conditions.

8. In 2008, a new Waste Management Act (No.18/2008) was passed and signed into law outlining the responsibility of local governments. The 2006 regulation is completely aligned with the 2008 Act and is now the main regulation that outlines the government's strategy to implement the 2008 act. The 2008 act, inter alia, requires that all landfills be operated under sanitary conditions. Furthermore, the Ministry of Public Works (PU) maintains a budget line to provide block grants to the cities to help them implement the requirements of the 2008 law.

9. The municipal governments are also fully engaged in a number of initiatives aimed at improving solid waste management services in their cities, partly in an attempt to demonstrate that they are also leading this effort to improve quality of service ahead of their respective municipal elections. Most of these initiatives have included Clean Development Mechanism (CDM) projects and/or other market mechanisms as part of a broader approach to privatize landfill operations and to increase operational revenues.

10. These regulatory, policy and budgetary reforms confirm the Government's commitment to a sustainable approach to help resolve these challenges and have created the enabling environment and space for a sustainable program for which they have requested World Bank support.

11. Despite these gains that Indonesia has made in the regulatory and policy front, most of the on the ground operational responses in individual cities remains fragmented, unsustainable and not sufficiently large to adequately address the current crisis.

12. The private sector is keen to partner with the public institutions to address these challenges, but a lack of confidence in the areas of public governance and management capacity are significant barriers for a broader and deeper involvement by the private sector. This has lead to the unavailability of much needed private capital inflows for investment in the sector.

Relationship to CAS

13. The proposed project is consistent and aligned with the current Indonesia Country Partnership Strategy (2009-2012), investing in Indonesia's Institutions by continuing the core engagement in Environmental Sustainability and Disaster Risk Mitigation with Central Government Institutions (PU in this project) and implementing through Local Government Institutions (which will be the participating municipalities).

14. The World Bank has also been actively and broadly supporting the urban sector in Indonesia for decades now. More recently, with respect to solid waste, in June 2001 the World Bank approved the West Java Environmental Management Project (WJEMP) comprising a blended package of instruments, which were a loan, credit and GEF grant. The loan was structured into a three phase APL. The rationale for the three phased APL approach was as follows, APL1 was to establish the Environmental Framework and Preparation of designs; while APL2 was for Implementation of Environmental Programs; and APL3 was for Consolidation of Service Delivery. The WJEMP did prepare a number of relevant and useful studies and plans, including the Provincial Environmental Strategies, National Environmental Strategy, a number of waste management plans and the Drainage Master Plan for Jakarta.

15. In January 2012, the Bank approved the Jakarta Urgent Flood Mitigation Project (JUFMP) for FY12Q2 delivery, which inter alia, will be dredging canals and drainage systems in the DKI Jakarta area that are in part blocked by solid waste deposits. The JUFMP project is benefiting from some of the studies done under the WJEMP.

16. Lastly, the Infrastructure Development Policy Lending (I-DPL) series that ended in 2010 included solid waste management prior actions.

II. Proposed Development Objective(s)

Proposed Development Objective(s)

17. The project development objective is to support improvements to solid waste management in participating municipalities through selective interventions in waste minimization, collection, transfer, separation and disposal.

Key Results

18. The PDO will be measured by a combination of output and outcome indicators such as (i) completion of engineered sanitary landfills and supporting infrastructure in participating municipalities, (ii) Operations and Maintenance contracts (O&M) in place, (iii) adoption and implementation of operational and maintenance manuals and systems in participating municipalities, (iv)
increased collection and disposal rates and (v) adoption and implementation of pricing and collection strategies in each participating municipality.

III. Preliminary Description

Concept Description

19. The PDO will be achieved through the implementation of these four components, namely,

Component A: Improvements in Solid Waste Management Systems ($122.5m), these funds would be on-granted to the participating municipalities and would finance the re-engineering and/or rehabilitation and/or closure of existing landfill/disposal sites, construction of new state of the art sanitary landfills (equipped with leachate treatment plants, heavy equipment such as compactors and bulldozers, facilities for staff/operator), waste treatment systems (such as sorting and composting plants, landfill gas to energy/flaring plants, and or other treatment systems as appropriate) and transfer stations. The 3 R approach (reduce, re-cycle, re-use) will be incorporated in the design and infrastructure works to minimize waste generation rates at the household level and local markets, and subsequently lowering collection, transfer and disposal costs, and extending the life of the landfills.

The selection criteria for participating provinces and municipalities which will include financial and technical considerations, will be agreed upon as part of project preparation and will also be aligned with Indonesia's Master Plan 2011-2025. This component will be rolled out in two phases. Phase 1 investments will be ready for implementation soon after project effectiveness and Phase 2 investments will be prepared, appraised and implemented in subsequent years during project implementation. The potential Phase 1 and 2 groups of municipalities under consideration are the Cities of Semarang, Yogyakarta, Medan, Bekasi and Tangerang.

The proposed investments are presently subject to a feasibility study to ascertain their commercial, economic and technical viability. Both phases will be completed within the five year life cycle of the project as the proposed lending instrument will be a specific investment loan (SIL). The proceeds of the loan would be on-granted to the participating municipalities depending on the institutional and implementation arrangements agreed upon, the relevant national regulations and other considerations.

Component B: Implementation Support ($10m). This component is expected to be co-financed or parallel financed as a donor grant. The source of financing will be confirmed during project preparation and will finance the technical assistance required to support the institutional framework needed to sustainably operate and maintain the effective management of these systems. The government and potential participating municipalities, given the past experiences in the sector, have suggested a partnership approach between the national and participating municipal governments as the institutional framework to manage each provincial waste management system. The BLU approach (Badan Layanan Usaha, as it is known under Indonesia regulations) involves establishing service units (in the Dinas Kebersihan, which is the cleaning services department of the participating municipalities). The established BLU's would be set up with a clear and pre-defined benchmarks. These benchmarks could include the completion of O&M contacts after a number of years to demonstrate how the improved systems are to be managed, as well as the cost recovery measures and the allocation of operation budgets by the local parliament (DPRD).

This component will also provide support to establish a country wide carbon/climate finance activity for the solid waste management sector as a whole to coordinate market based carbon revenue generation opportunities. This component will also include funding for setting up publically accessible information based National Solid Waste Benchmarking System (NSWBS). Details of this system will be agreed upon during project preparation but will include an incentive based mechanism to improve management of these operations.

Component C: Social Development Component ($5m). The funding source for this component will be confirmed during project preparation. This component will address the social needs of waste pickers and affected host community members, particularly owners of livestock. Challenges related to resettlement/land acquisition and the potential loss of livelihood for waste pickers and livestock owners will be comprehensively addressed to help improve their social development outcomes. This component will not finance any physical investments or works associated with landfill workers or livestock, as these need to be integrated into the landfill operations as a whole and are thus included in Component A. This component will finance training, continuous consultations with affected households, participation activities and potentially a fund to address major social concerns during preparation.

Component D: Advisory Services ($5m) will finance high level strategic and analytical studies to underpin advice to GoI and municipalities on potential sector policy reform options going forward.

IV. Safeguard Policies that might apply

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V. Tentative financing

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