
POLICY BRIEF

**Inequality in Aceh:
dimensions and policy issues**

Summary

This brief calls for urgent government action on inequality. The issue has always been important elsewhere, but this is even more so in the case Aceh. Growth was not spread evenly, poverty remains high and inequality has increased overtime. There are cases where the contrast between the populations is quite dramatic. For instance, highest incidence of poverty was found in resource rich districts, inter ethnic disparity in agricultural land holding increased, both inflation and wages shot up rapidly during the post tsunami era (especially in Banda Aceh).

What raises serious concern is that the above trend is set within the fragile social, political and economic background. The consolidation of peace, democracy and development in Aceh is still in flux and therefore it cannot and should not be taken for granted. The challenge is to mitigate various forces of social division in Aceh such as between the have and the have-nots, the GAM leaders and the ex combatants, the GAM and the rest, the Acehnese and the Javanese, the resource rich regions and the rest, those that support the sharia and those who do not, and so on.

Reducing inequality within this context is then crucial; it would sustain development by simultaneously promoting social and political stability.

The case is urgent, the stake is high but opportunities are also plenty. The consequence of the special autonomy law in Aceh, later also the LOGA, is that there is a massive central government transfers to various levels of local government. The revenues will continue for a considerable period of time and the amount is relatively large and would be more than compensate the dwindling oil and gas revenues.

But local government policy needs to change. Recent trend in government expenditure has not been encouraging. Most of the extra resources for Aceh were spent on public consumption and the creation of new districts and less on public goods. More public goods are needed for the Acehnese so that they are capable to participate more meaningfully in the economic, social and political processes. So is also with employment creation and poverty reduction.

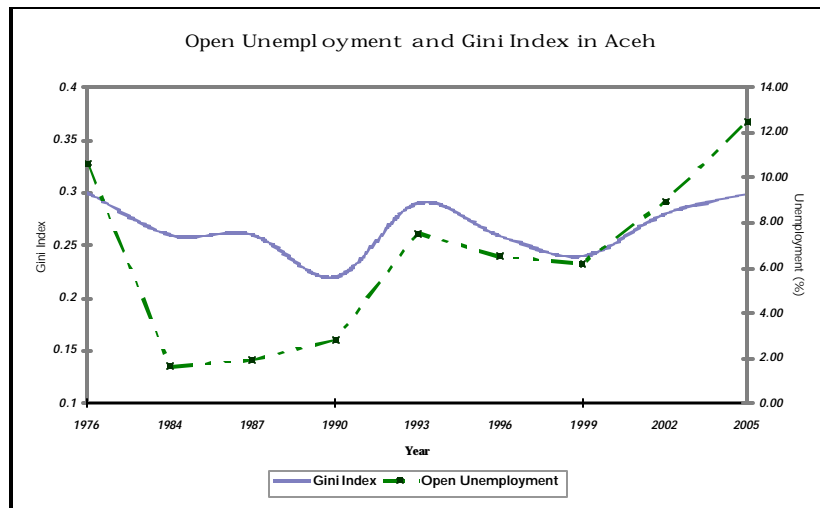
Above all, since inequality has so far been largely ignored in government policy, there is a need for Aceh to formulate new and comprehensive long term development strategy wherein equity is integrated into the fostering of peace, democracy and development. This framework which should reflect broad consensus among stakeholders would provide a united vision of the future as well as framework for development strategy, policy and its implementation modalities.

General trends in inequality

In the last thirty years there was a clear, rising trend in income per capita in Aceh. But a different pattern occurred in inequality.¹ First it declined sharply from mid 1970s to 1990 along with growth then it started to increase (also quite sharply) since early 1990s. Employment pattern could explain the inequality trend, both largely moved in the same direction. As unemployment dropped so was also inequality and vice versa.

In the years prior to 1990, employment was significantly expanded. The green revolution, where rice yield per hectare increased by more than one half, generated increases in rural income as well as employment. Also, massive rural infrastructure development scheme played an important role. Coincidentally, the onset of natural resource boom affected positively on the economy especially when at initial stage large construction of building and infrastructure was done, which had some positive effects on employment and income. As well, security condition in the region was relatively good. The armed conflict was still at its infancy.

¹ Gini index of 0 indicates perfect equality and 1, perfect inequality. It should be noted that the calculation of Gini coefficient is based on personal expenditure data. The usual caveats apply. These include the equality biased in expenditure data compared to income data (where the rich saves more compared to the poor (which spends most of their income), the tendency to exclude the rich in the expenditure survey, the changing composition of consumption basket between the rich and the poor which tends to be ignored in the expenditure survey. However, the only complete data available so far is the household expenditure survey.

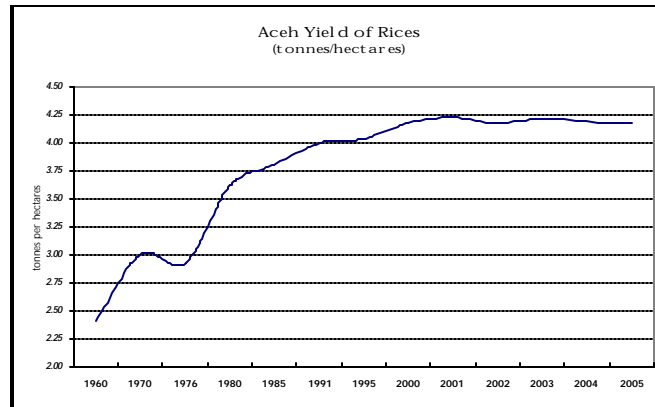


Source: *Pembangunan daerah dalam angka 2001, Bappenas Selected Socio economic indicators of Indonesia, 2007 BPS, Supas various years*

Notes: *Open Unemployment was percent to labour force Unemployment data 1971 represent 1976, 1980 represent 1984, 1985 represent 1987, 1995 represent 1993, 1998 represent 1999 and 2003 represent 2002*

Situation changed dramatically since 1990s when inequality and unemployment show an increasing tendency. A number of factors were responsible. In the first place, increases in rural income became smaller as gains in rice production slowed down and rural development schemes were also reduced. To some extent this is inevitable as rice yield per hectare was already close to its technical possibility in early 1990s, output increases has been marginal since then.² To make matter worse, while rice production growth slowed down the overall agricultural sector growth dropped rapidly since 1992. At the same time, government’s rural infrastructure programme virtually ended among others because most infrastructure has been repaired or built so that the opportunity of constructing new schemes was also limited.

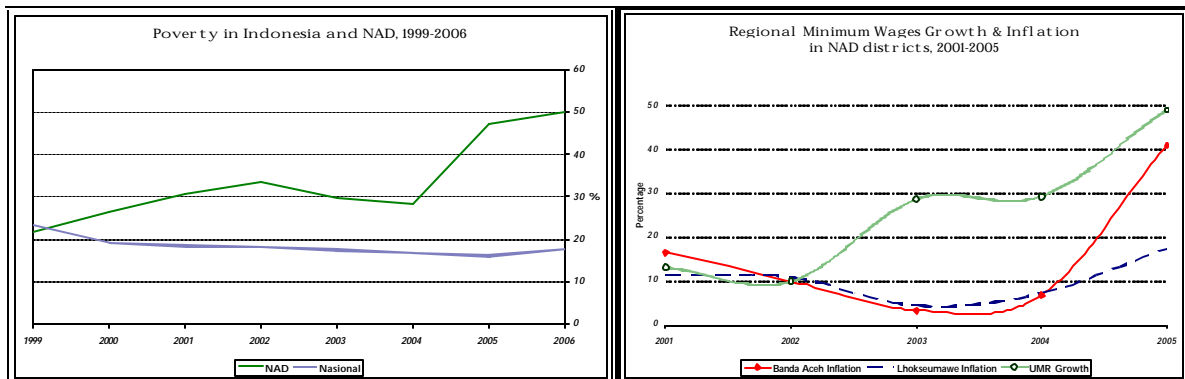
² This is the classic Ricardian case of “diminishing returns”, where expansion of land results in declining extra output as less and less fertile land is cultivated. Indeed, the rice harvested area in Aceh continue to expand until very recently.



Source: Data were constructed from BPS, *Aceh dalam Angka 2005*, *Statistik Indonesia 1990 & 1995* and Dayan Dawood and Sjafrizal, "Aceh: The LNG Boom and Enclave Development" in Hal Hill, *Unity and Diversity: Regional Economic Development in Indonesia since 1970*

Meanwhile, the stagnant economic condition in rural areas, particularly in districts North Aceh, Pidie, Bireun, was exacerbated by the escalation of armed conflict throughout the 1990s. The decline in agricultural output was a direct impact of the armed conflict. Oil and gas production has also been affected, its output dropped due partly to the worsening security condition in North Aceh district, where GAM movement gained strength. Of course, the depleting natural reserves also played a part in it.

The increase in inequality in Aceh was also associated with the poverty level, which also showed an increasing tendency since 1999. This deviates from the national pattern. Again, the worsening security condition was largely to blame.



Source: BPS and BPS NAD

A marked increase in inequality and poverty occurred after the tsunami. The disaster itself put millions of people displaced, deprived of their productive assets and jobless. Hence

unemployment increased during this period. However, there are other forces at work that push up the inequality further. Massive resource transfer into the region within a short period of time inevitably created inflation to shoot up as the supply of non-tradables is limited.³ A jump in construction and services activities following the tsunami reconstruction is a case in point. As is well known, inflation tends to be unequalising. The minimum wage, which also rose steeply, is in practice only applicable in urban areas. As most workers are still employed in agricultural, informal sectors such regulation is not operative hence widening rural-urban inequality in addition to the one between the tradables and non-tradables.

Urban and rural inequality

The urban-rural inequality is high and shows a tendency to increase. As discussed above, the recent post-tsunami reconstruction played an important role.

Meanwhile, the gap between the agricultural sector and non agricultural, which also essentially means between rural and urban areas, has been phenomenal. For instance, in 2005 the average per capita household expenditure in agriculture in South East Aceh District was Rp 939 thousand per year whereas in non agriculture was Rp 8 million per year. In Gayo Lues District, the contrast is even more striking, Rp 833 thousands as against Rp 15 million per year.

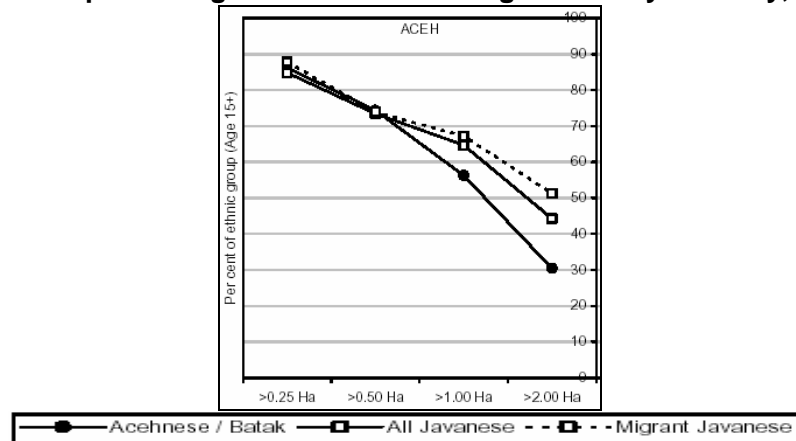
Changes in the composition of population, mainly due to government transmigration programme, as well as government recruitment policy, were partly responsible for the increased inequality. This has generated not only urban-rural inequality but also inter ethnic inequality.

In general, migrants from Java and Bali who comprised only about 5 percent of total Aceh population in 1995, have a much better economic performance than the Achenese. For instance, more than on half of the relatively high paying jobs in government officials, professionals and technicians were occupied by them. Their unemployment rate is also much lower, about 5 per cent in 1990 as compared to 10 per cent for the Acehnese.

³ This is a classic case of the Dutch disease phenomenon whereby a massive resource flow into an area disturbs inter sectoral equilibrium with the non-tradables gain and the tradables lose. Hence, massive reconstruction activities favours the services and construction sectors at the cost of the agriculture and manufacturing. Non-tradable prices jumped in Banda Aceh including wages and services. *Kompas* daily, 8 December 2005, reported that house rent increased at least ten times in Banda Aceh.

The transmigration programme seemed to have also increased inequality in productive assets in the rural areas. The Acehese average land holding was much lower than the Javanese. The figure below shows 1990 data on landholding.

Rural Inequalities agricultural land holding in Aceh by ethnicity, 1990



Source: *Horizontal Inequalities, Ethnic Separatism and Violent Conflict: The Case of Aceh, Indonesia.* Graham Brown, 2005

Inter district inequality

There is not much information about inter district inequality in Aceh. The fact that population distribution is unevenly spread, where a large part of the population lives in Kota Banda Aceh, Sabang, Langsa dan Lhokseumawe, it should be expected that inter district inequality in Aceh is relatively high. This is not to mention the existence of enclave oil and gas industries in Aceh Utara.

Using the human development indicators (HDI), Banda Aceh always has the highest HDI in the province, whereas in southern and western part of Aceh HDI are the worst. The overtime pattern showed a fluctuation in the inter district HDI, it declined first then it increased again.

Comparison between district with highest and lowest HDI 1993-2005

	Highest HDI		Lowest HDI		Difference
	District	HDI	District	HDI	
1993	Banda Aceh	74.8	Southeast Aceh	61.8	13
1996	Banda Aceh	74.2	South Aceh	64.2	10
1999	Banda Aceh	70.5	South Aceh	62.1	8.4
2002	Banda Aceh	71.8	Simeulue	61.8	10
2005	Banda Aceh	74.7	Sim eulue	65.2	9.5

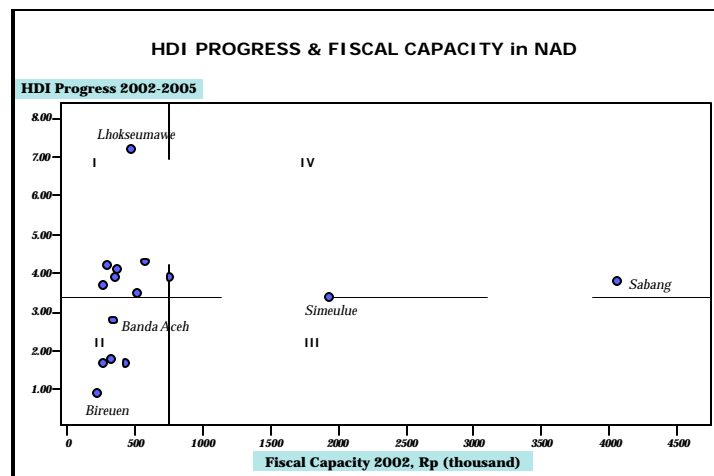
Source: BPS & NHDR Indonesia 2005

Geographic and topographic condition partly explain inter district inequality. Simeulue separated from Sumatera mainland and have the lowest HDI district in 2002 & 2005. Gayo Lues and Southeast Aceh location is part of Taman Nasional Bukit Barisan, are isolated from other part of Aceh.

In fact, the State Ministry for Development of Disadvantaged Regions has included 16 out of 21 districts in Aceh underdeveloped regions in 2004.

The role of local government is critical in increasing HDI. The figure below shows the HDI progress between 2002-2005 and fiscal capacity in 15 districts. There are 6 districts which had below or equal to average HDI progress 2002-2005 (average was 3.4)-they are located in West Aceh, Banda Aceh, Simeulue East Aceh, Bireuen, Pidie. The first three districts are the tsunami affected areas whereas the last three, GAM based districts.

Districts included in Quadrant II need fiscal assistance from the central government (through DAK) whereas districts in quadrant III already had high fiscal capacity per capita. Their problems are related to the low local government capacity.



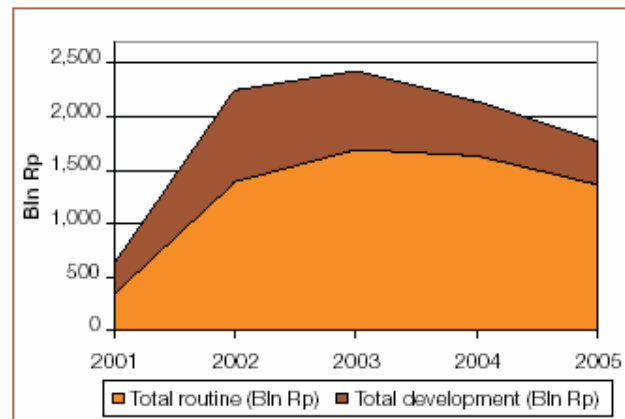
Source: Data constructed from BPS source

Notes:

- Samples not included Aceh Barat Daya, Gayo Lues, Aceh Tamiang, Nagan Raya, Aceh Jaya dan Bener Meriah.
- The line shows the average fiscal capacity per cap 2002 (vertical) and average HDI progress 2002-2005 for 15 districts sample (horizontal). The average fiscal capacity percapita 2005 was Rp. 747.000,-
- Quadrant I: district with high pogram in HDI 2002-2005 and have low fiscal capacity, i.e.: Lhokseumawe
- Quadrant II: district with low HDI progress 2002-2005 and have low capacity, i.e.: Bireuen
- Quadrant III: district with low HDI progress 2002-2005 but have high fiscal capacity percapita in 2005, i.e.: Simeulue
- Quadrant IV: district with high HDI progress 2002-2005 and also have high fiscal capacity percapita in 2005, i.e.: Sabang
- See statistical annex for information

The low capacity of local government to promote human development, which in other words is a high quality growth, is related to its expenditure priority. Figure below shows that most of the extra financial resources were spent on public consumption. This does not bode well for the provision of public goods and services such as infrastructure, health, education and so on.

**District government routine and development expenditures
(billion Rp, constant 2006 prices)**



Source: World Bank staff calculations, *Aceh Public Expenditure Analysis*, World Bank 2007

Policy implications

The rise of unemployment, poverty and inequality since 1990 in Aceh is worrying. These divisive forces need to be managed. It is clear that employment creation, and poverty reduction, should be the top priority in Aceh. The challenge is enormous. Economic condition is quite difficult. Unlike in the past, the traditional agriculture and natural resource based industries (oil and gas, forestry) could not be the leading sectors to pull growth with equity. New growth centres have to be identified and developed. See separate Policy Brief on “Aceh: growth and resources for the future”.

Specifically, government policies should focus on:

- Employment creation in non-rice agriculture such as soya beans, palm oil etc. as well as infrastructure
- Re-developing enclaves in the declining resource industries into new growth centres, perhaps to serve as centres for agro based industries;
- Redefining local government spending priorities to reflect more concern for human development as well as productivity increase;

- Special attention to undeveloped regions, some are former GAM based areas;
- As a sizeable portion of the extra resources accrued to provincial government, there is an opportunity for the provincial government to take more active approach to redress the imbalances, promote competitiveness as well as to lead the local government capacity building

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Statistical Annex

HDI Progress among district in Aceh

Province and Districts		HDI 1993	HDI 1996	HDI Progress 1993-1996	HDI 1999	HDI Progress 1996-1999	HDI 2002	HDI Progress 1999-2002	HDI 2005	HDI Progress 2002-2005
NANGGROE ACEH DARUSSALAM		68.4	69.4	0.9	65.3	(4.1)	66.0	0.7	69.0	3.0
1	SIMEULUE						61.8		65.2	3.4
2	ACEH SINGKIL						62.2	0.1	66.5	4.3
3	ACEH SELATAN	63.6	64.2	0.6	62.1	(2.1)	63.8	1.8	67.7	3.9
4	ACEH TENGGARA	61.8	67.7	5.9	63.9	(3.7)	66.8	2.8	70.2	3.5
5	ACEH TIMUR	69.7	69.5	(0.2)	65.4	(4.1)	66.7	1.3	68.4	1.7
6	ACEH TENGAH	68.8	68.3	(0.5)	66.0	(2.4)	66.7	0.7	70.8	4.2
7	ACEH BARAT	65.3	67.1	1.8	64.3	(2.8)	65.6	1.3	67.4	1.8
8	ACEH BESAR	69.1	68.4	(0.7)	66.8	(1.6)	67.2	0.4	71.4	4.1
9	PIDIE	66.8	67.8	1.1	64.1	(3.7)	67.8	3.7	69.5	1.7
10	BIREUEN						70.6	7.5	71.5	0.9
11	ACEH UTARA	69.1	69.5	0.4	63.1	(6.4)	65.9	2.8	69.7	3.9
12	ACEH BARAT DAYA								66.9	3.0
13	GAYO LUES								66.1	(0.7)
14	ACEH TAMIANG								68.3	1.6
15	NAGAN RAYA								66.3	0.8
16	ACEH JAYA								66.8	1.2
17	BENER MERIAH								67.4	0.7
18	KOTA BANDA ACEH	74.8	74.2	(0.5)	70.5	(3.7)	71.8	1.3	74.7	2.8
19	KOTA SABANG	72.3	70.1	(2.2)	63.7	(6.4)	69.4	5.8	73.3	3.8
20	KOTA LANGSA								70.4	3.7
21	KOTA LHOKSUMAWA								73.1	7.2