



Indonesia Energy Subsidy Briefing

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AS PART OF ITS WORK ON ENERGY POLICY AND SUSTAINABLE DEVELOPMENT IN INDONESIA, THE GLOBAL SUBSIDIES INITIATIVE (GSI) OF THE INTERNATIONAL INSTITUTE FOR SUSTAINABLE DEVELOPMENT (IISD) PUBLISHES A REGULAR BRIEFING ON ISSUES RELATED TO ENERGY SUBSIDIES. FOR MORE INFORMATION, CONTACT LUCKY LONTOH AT LUCKY.LONTOH@IISD.ORG AND CHRISTOPHER BEATON AT CBEATON@IISD.ORG.

Next Step for Indonesia: A Fixed Fuel Subsidy?

The new Minister of Finance, Chatib Basri, has announced that the government of Indonesia is considering a “fixed fuel subsidy system”—a new system where the overall cost of the fuel subsidy would be less affected by external factors such as fluctuations in international oil prices and the exchange rate.ⁱ

The announcement comes after July talks with the Budget Body (Badan Anggaran) and the parliamentary commission responsible for the state budget, development plan and banking (Commission XI).

The initiative was confirmed by Hatta Radjasa, the Coordinating Minister of Economic Affairs, who added that the inclusion of the plan in the 2014 state budget will be discussed with parliament this year.ⁱⁱ

Basri and Radjasa further explained that the new system would still provide the fuel subsidy, but that the retail fuel price would fluctuate in accordance with the changing market price for fuel.ⁱⁱⁱ

Until now, Indonesia has been subsidizing the gap between international market prices and the domestic subsidized price on several fuel products, which, in the midst of soaring international oil prices, has resulted in a fiscally unsustainable fuel subsidy.

Inflation, Exchange Rates and Foreign Exchange in the Wake of July Price Rises

Although it is too early to evaluate the impact of price increases in gasoline and diesel that took place in June 2013, Indonesia’s central bank, Bank Indonesia, has claimed that inflationary impacts appear to be in line with levels that were expected.

Inflation across June remained within central bank predictions, at 1.03 per cent, contributing to 5.9 per cent overall inflation so far this year.^{iv} The average price of foodstuffs and goods in Indonesia was already increasing prior to the announcement of higher fuel prices, mainly because of increasing seasonal demand in anticipation of Ramadan fasting from July to August.^v

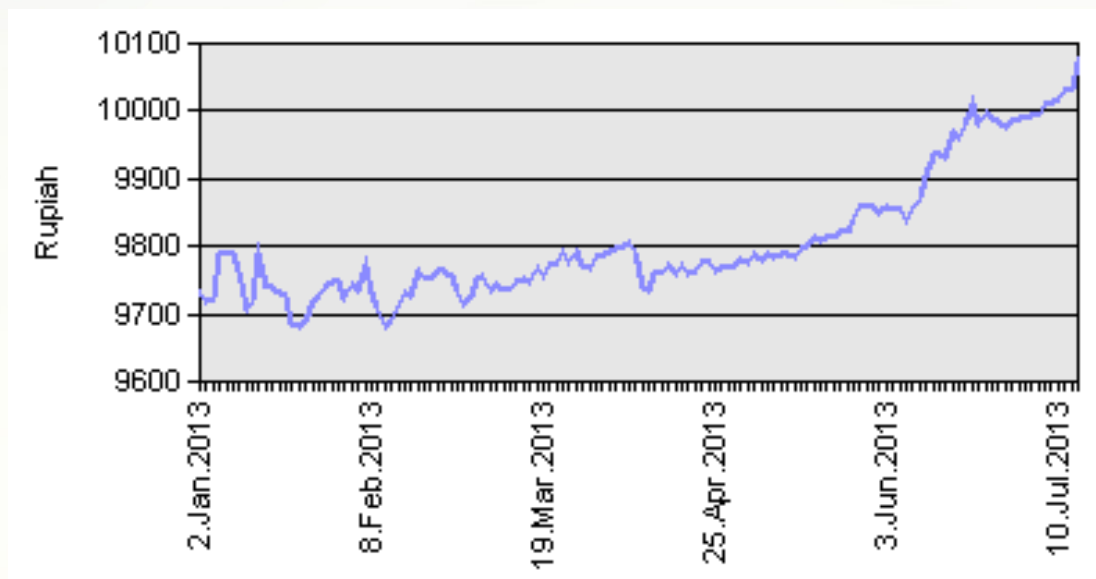
The Central Statistics Agency (Badan Pusat Statistik, BPS) warned the government to take necessary steps in order to keep total inflation across 2013 at around 7.2 per cent.^{vi} Steep inflation is expected to take place in July 2013, as the impact of fuel price increases is combined with spending related to Ramadan.



Bank Indonesia's Head of Public Relations, Difi A. Johansyah, explained that the inflationary effect of the fuel price increase is expected to last for three months. The peak is expected to happen in July, and then slow down over the next two months.^{vi,vii} Inflationary impacts are at least expected to slow after the end of Eid al-Fitr, which falls on 8 August.^{viii,ix}

Similarly, it is too early to assess the extent to which fuel price changes may go on to affect the value of Indonesian currency. Through July, the rupiah exchange rate towards the US dollar has continued to weaken. This trend began around late April, when the government abruptly cancelled a previous proposal for changing the fuel pricing mechanism, the 'dual pricing system'. On 26 July, US\$ 1 exceeded Rp10.300,^x the lowest point for the Rupiah this year.^{xi} Bank Indonesia has responded to the weakening exchange rate by increasing the interest rate on two occasions: from 5.75 per cent to 6 per cent on 13 June; and then on 11 July to 6.5 per cent.

Figure 1. Rupiah/USD exchange rates



Source: Bank Indonesia (2013).^{xii}

From the end of May 2013 until the end of June 2013, Indonesia's foreign exchange reserve has dropped from US\$ 105 billion to US\$ 98 billion. It was primarily caused by the state debt payment, state-owned companies' raw material imports and central bank intervention to support the Rupiah.^{xiii, xiv}

In relation to the fuel subsidy, Minister of Finance Chatib Basri explained that investors may not be fully informed about the new fuel price policy in Indonesia. He hopes that the new fuel price policy can tame the fall of Indonesian currency, and that with less demand for fuel imports in the future the Rupiah can regain its strength.^{xv, xvi} Bank Indonesia's Governor, Agus Martowardojo, stated a similar message. He welcomed the fuel price policy, expressing hopes that it can reduce the fuel imports and so reduce the demand for US dollar.^{xvii}

Views on Subsidy Reform Compensation Packages

On June 22, the government of Indonesia decided to increase the subsidized fuel price of gasoline (Premium, RON 88) from Rp 4,500 to Rp 6,500 and automotive diesel (Solar) from Rp 4,500 to Rp 5,500. The government also launched five aid programs aimed to mitigate the impact of fuel price increase, namely: BLSM (unconditional cash transfer), P4I (basic infrastructure support), BSM (financial support for poor students), PKH (conditional cash transfer) and Raskin (food aid), amounting to approximately US\$2.9 billion.^{xviii}

The implementation of the compensation packages has been subject to monitoring and considerable political and public debate.

The biggest opposition party, the Indonesia Democratic Party – Struggle (PDI-P), has been giving specific attention to the BLSM program. The BLSM receives the largest share of funding among the compensation programs, US\$ 968.75 million. PDI-P has been highly critical of the BLSM, mainly with respect to inaccuracies in the database used to target poor households, and asynchronous delivery of cash transfers to some areas.^{xix} The official PDI-P social media account (@PDI_Perjuangan)^{xx} has reported numerous complaints and problems in its implementation. In part, the stance of the PDI-P reflects a concern that the cash aid can be used to increase the popularity of ruling coalition parties, especially the Democrat Party (PD).

Online and print media from all over Indonesia have also played a major role in reporting the implementation of the BLSM, largely focused on the period when cash was distributed. Most of the reporting on implementation has taken place at the local level. The news varies from disseminating government information about the scheme to explaining the distribution schedule and how to find the locations where cash will be disbursed, as well as reporting on problems and feedback from the households targeted by the program.

Many of the criticisms surrounding the BLSM have focused on the first round of distributing cash, which was supposed to take place on the same day as the change in subsidized fuel prices, through post offices nationwide.^{xxi,xxii} In practice, the schedule in some regions varied, due to technical issues such as the adjustment of the list of recipients, the distribution of identification cards (KPS, Social Protection Card) and communication network problems.^{xxiii,xxiv} This should not, however, prevent households from accessing funds once the problems are resolved. Recipients are allowed to acquire the cash aid until the end of 2013.^{xxv}

The National Team for the Acceleration of Poverty Reduction (TNP2K)—the government body supervising the implementation of the poverty reduction programs—reported that by 26 July, the BLSM had been distributed to 89.23 per cent of the targeted 15.5 million households.

The TNP2K explained that dissatisfactions with the BLSM derive from four main factors. First, the list of recipients of the unconditional cash transfer has changed since similar interventions in 2005 and 2008, due to an improvement in the methodology used to determine the poor households that need support. Second, there could be inaccuracies in the new data, due to survey staff making errors in the process to determine eligible recipients. In this case, there is the possibility that ineligible individuals may have been included on the list of recipients, or, vice versa, that eligible households may not have been included. Third, the difference between

the poorest group and the group slightly above them is small, creating the impression that there are poor households excluded from the list of recipients. Fourth, since the list of recipients is based on data from 2011, there could be errors because of changes in households' economic status, mortality and residential movement.

xxvi

The government acknowledged the weaknesses in the BLSM program, and has promised that improvements will be made.^{xxvii}

Radio Frequency Identification Device

The plan to install radio frequency identification (RFID) devices at gas stations has been postponed to 1 August. The device is intended to monitor the purchase of fuel products by individual motor vehicles at the gas stations.

A telecommunications company, the Indonesian Telecommunications Industry (PT INTI), is expected to begin installing the devices in 276 gas stations in Jakarta, while the installation on vehicles is still waiting for further instruction and regulation from the government.^{xxviii} The President Director of PT INTI, Tikno Sutisna, explained that in the first phase the RFID will be installed on government vehicles, until further clarification from the government to start installing it on private vehicles.^{xxviii}

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GSI is an initiative of the International Institute for Sustainable Development (IISD). GSI puts a spotlight on subsidies—transfers of public money to private interests—and how they impact efforts to put the world economy on a path toward sustainable development. In cooperation with a growing international network of research and media partners, GSI seeks to lay bare just what good or harm public subsidies are doing; to encourage public debate and awareness of the options that are available for reform; and to provide policy-makers with the tools they need to secure sustainable outcomes for our societies and our planet.

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