



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.

Fuel Subsidy 2013 Recap: Over the Limit, Again

Indonesia's Ministry of Finance has estimated that actual total fuel subsidy expenditure in 2013 will, again, exceed the amount allocated in the 2013 budget. Indonesia allocated US\$ 16.32 billion¹ to fuel subsidy expenditure in 2013, but data released in January 2014 suggests actual expenditure was US\$ 20.41 trillion, an increase of 25 per cent above the allocated amount. While targets for the total volume of subsidized fuel sold (of 48 million kiloliters) have largely been met, the depreciation of the rupiah (which has fallen from IDR 9,760/US\$ in May 2013 to IDR 12,245/US\$ in 20 December 2013), combined with higher international oil prices, has driven significantly higher the subsidy per unit of fuel sold (Detik.com, 2013; Bank of Indonesia, n.a.).

Between January and November 2013, Indonesia imported 14.74 billion tons of crude oil, worth US\$ 12.51 billion, a rise of 25 per cent from the same period in 2012. Import volumes of gasoline varieties reached 13.40 billion tons (with a value of US\$13.58 billion) in the same period in 2013, 5.2 per cent higher than in 2012, while jet fuel imports were 38.4 per cent higher between January and November 2013 compared to the same period in 2012. (BPS, n.a.a.).

In 2014, Indonesia plans to allocate IDR 194.83 trillion to fuel subsidies covering gasoline RON 88, automotive diesel, 3kg LPG cylinders, and liquefied gas for vehicles (LGV). The government also plans to allocate IDR 89.8 trillion to electricity subsidies for tariff and voltage classes below 900VA. The combination of fuel and electricity subsidies in 2014 comprises 85 percent of Indonesia's total subsidy allocation, equivalent to 23 percent of total central government expenditure (Fiscal Note and State Budget Proposal 2014, p. lampiran I—4, 11).

Jakarta's government proposes a trade-off between fuel subsidy and mass transportation

The provincial government of Jakarta continues to articulate its desire to reduce subsidized fuel distribution within its jurisdiction, with a plan to reallocate the finances saved to one of the city's flagship programs, the development of Jakarta's mass transportation system. Joko Widodo, the highly popular governor of Jakarta, announced that talks were underway with Indonesia's Ministry of Energy and Mineral Resources regarding this proposal. He added that the first step to limiting subsidized fuel consumption would be to apply market rates for

¹ This briefing uses Bank of Indonesia's foreign exchange rate on 3 February 2014, at IDR12,251/US\$.

cars' consumption of fuel (Kompas, 2013). Basuki Tjahaja Purnama, the vice governor of Jakarta also added that the provincial government of Jakarta is looking to test public opinion regarding the plan (Tempo, 2013a). A final decision on this issue will depend on the deliberations of the Indonesian Government, relevant ministries and the downstream oil and gas regulator (BPH Migas).

Very heavy traffic in Jakarta is one of the main motivations behind this initiative, with traffic becoming a key developmental policy issue for the Greater Jakarta area², the centre of Indonesia's business and administration. According Tigor Nainggolan, the Chairperson of Jakarta Transportation Council, traffic has worsened significantly in the past few years, with the average car speed on Jakarta roads now reduced to 12km per hour (Tempo, 2013b).

According to Metro Jaya Police, in 2013 there were 16 million registered vehicles in the Greater Jakarta area, which consisted of: 11.93 million motorcycles; 3 million cars; 360,022 buses; 617,635 commercial vehicles; and 133,430 special vehicles (Detik.com, 2014). Police authorities have stated that they issue an average of 4,000 new motorcycle licenses and 1,000 new car licenses every day (Vivanews, 2014a). The vehicles in the Greater Jakarta area make up roughly 15.49 percent of the total number of vehicles in Indonesia, which, according to BPS (n.a.b), reached 94.3 million vehicles in 2012. The huge growth in motor vehicle usage in Indonesia has been bolstered, among other factors, by the current cheap fuel policy.

The provincial government's proposal has been supported by several groups, such as Indonesia's Chamber of Commerce (KADIN), whose chairman, Suryo Bambang Sulisto, sees the plan as a key part of the solution to Jakarta's traffic problem, with implications for productivity and business development (Vivanews, 2014b). Jusuf Kalla, Indonesia's former Vice-President and one of the running candidates for Presidential post, also weighed into the debate, saying that the city's capacity to best respond to flooding, another major issue for Jakarta, would be far stronger if the fuel subsidy budget could be reallocated to assist the victims in periods of flooding and to improve the city's infrastructure and landscape to reduce the impact of persistent floods (Liputan6, 2014a).

Pertamina acquisition of PGN or PGN merger with Pertagas?

A plan to overhaul two of Indonesia's energy-sector state-owned enterprises (SOEs), PT Pertamina and PT PGN, has been a feature of the Indonesian energy policy debate in recent months. Talk of a potential acquisition or merger between the two companies has put PT PGN's stock under pressure, which has fallen from US\$ 0.41 per share before November 2013 to as low as US\$ 0.37 per share as of 30 December 2013 (Indonesia Stock Index, n.a.).

PT PGN's core business is to operate Indonesia's downstream gas system, including gas pipeline transmission and distribution. There were two proposals for SOE restructuring: first, a direct acquisition of PGN by PT Pertamina; and second, an initial merger between PT PGN and PT Pertagas, a subsidiary of PT Pertamina which operates in the gas market, followed by PT Pertamina's final acquisition of PGN. The Ministry of Finance has expressed its support for restructuring of this kind (Inilah.com, 2014). The acquisition plans may offer an opportunity to cut

2 Greater Jakarta territory encompasses the Jakarta area and its surrounding cities, namely Bogor, Depok, Tangerang, and Bekasi.

the transaction costs in pipeline rental for gas transmission and distribution, which currently has to be organized between PT Pertamina and PT PGN and therefore to potentially enhance PT Pertamina's capacity to support the government's strategy to expand the conversion of gasoline usage to gas in the domestic market.

The plan for energy sector restructuring has received mixed reactions from commentators and the public. Analysts from PT Investa Saran Mandiri, PT Panin Sekuritas and Trust Securities all expressed concern that the plan had flaws, especially by putting downward pressure on PT PGN's stock (The Jakarta Post, 2014a). Similar criticisms also came from members of parliament. The Chairperson of the House of Representatives, Marzuki Ali, said that the Minister of State Enterprises' decision to support the plan was imprudent given the way that the process had put pressure on PT PGN's stock (Kompas, 2014a).

Gas Price Changes, Government Intervenes

Indonesia's price for 12kg -cylinder LPG was revised twice in the first week of January 2014. PT Pertamina announced the new price for the large-cylinder LPG, which is widely used for daily household activities, on 1 January 2014. The revised price was US\$ 0.32 per kg higher than the previous price, an increase of 67 per cent. This was the first change in prices since 2009, when 12kg-cylinder prices were set at US\$ 0.48 per kg. PT Pertamina announced that it had been making a loss of US\$ 1.75 billion between 2008-2013 in the distribution of the cylinders (The Jakarta Post, 2014b), and would continue to make a loss of US\$ 0.17 per kg under the new price (Kompas, 2014b).

PT Pertamina's position was supported by the assessment of the National Audit (Badan Pemeriksa Keuangan (BPK)) which quantified Pertamina's losses in 2011 and 2012 at around IDR 7.7 trillion (US\$ 628.52 million), resulting largely from the distribution of 12kg-cylinder LPG, sold below its production cost (Liputan6, 2014b; The Jakarta Post, 2014c).

In Indonesia, 12kg-cylinder LPG is typically referred to as being "non-subsidized", because the government does not compensate Pertamina for selling its product at the fixed below-market price, as it does in the case of 3kg-cylinder LPG, the price of which was fixed at US\$ 0.35 per kg in 2007 (IISD-GSI, 2012). By international definitions, however, the price of 12kg-cylinder LPG does indeed represent a subsidy, as the product is not sold at its market-price as a result of government intervention.

On 5 January 2014, following considerable public opposition to Pertamina's 12kg LPG price increase announcement, Indonesian President Susilo Bambang Yudhoyono intervened in the debate, instructing PT Pertamina and associated ministers to review the decision within twenty-four hours. The next day, PT Pertamina dramatically scaled back the proposed price increase to US\$ 0.8 per kg (a quarter of the original increase), setting the retail price of 12kg-cylinder LPG to around US\$ 0.56 per kg, and citing the public reaction to higher prices as its reason for revising the initial decision.

At the same time, in response to the reduction in prices, PT Pertamina revised down its profit growth projections for 2014, from 13.17 per cent to 5.65 per cent. According to Hanung Budaya, PT Pertamina's Director of Marketing and Trade, 59 percent of LPG marketed by Pertamina is imported, while Indonesia's consumption of LPG in 2013

reached 5.6 million tons, of which 4.4 million ton was subsidized (Kompas, 2014c).

The inflationary impact of LPG price changes was considered to be minor by several government agencies and experts. The Deputy Governor of Bank of Indonesia, Perry Warjoyo, commented that the initial price increase on 1 January would add 0.13 per cent to annual inflation (Tribunnews, 2014), while Tony Prasentiantono, an economist from University of Gadjah Mada, warned the government that the revised price would put total annual inflation at 5.5-6.5 per cent, which is one percent higher than the central bank's annual inflation target for 2014. Prasentiantono argued that the weakening rupiah would be a key factor in driving inflationary pressures in 2014 (Kontan, 2014). The latest report from National Statistics (Badan Pusat Statistik (BPS)) on 3 February 2014 showed that grocery price indices rose by 1.81 per cent from December 2013 (BPS, 2014).

An Emerging Alternative for Fuel Pricing System in Indonesia

On 15 January 2014, Minister of Finance, Chatib Basri argued that the government had not ruled out the possibility of fuel subsidy reform in 2014, although this would be a risky decision for politicians facing re-election starting in April 2014. He added that the Ministry of Energy and Mineral Resources is currently preparing a 'closed-distribution mechanism' for subsidy targeting, while the government has also been working on 'fixed subsidy' scheme (Ministry of Finance, 2014).

The closed-distribution system—which aims to increase the accuracy of subsidy distribution to qualifying recipients—has been progressing slowly thus far. The flagship program to take this forward, the Radio Frequency Identification (RFID) scheme, aims to reach 4 million vehicles in Jakarta by March 2014. Under this scheme, consumption control instruments, designed to identify the vehicle and determine fuel consumption, are offered for free in selected gas stations. PT INTI, the contractor responsible for installing the RFID, reported that by January 2014 there were 200,000 vehicles equipped with RFID (Detik.com, 2014). Furthermore, the Director of PT INTI explained that it has been difficult and will likely be impossible for the company to meet its tender obligation to provide 100 million RFID consoles by July 2014.

A potential fixed fuel subsidy system, as described by the Minister of Finance, would represent a return to subsidy policies of the past. During Megawati Soekarnoputri's Presidency, who reigned between July 2001 and October 2004, Indonesia implemented and subsequently revoked a fixed fuel subsidy scheme that at various times capped fuel prices at 50 per cent and 75 per cent of market prices.

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