



INDONESIA ENERGY SUBSIDY BRIEFING

A bi-monthly review of developments in Indonesian energy subsidy policy and energy markets

SEPTEMBER 2014

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.

Highlights

- President Yudhoyono turns down proposal to share fuel price increase with incoming Widodo administration.
- The proposed State Budget 2015 would increase expenditure on fuel subsidies to IDR 291.1 trillion (US\$ 25 billion) and electricity subsidies to IDR 72.4 trillion (US\$ 6.2 billion). This means 26.4 per cent of the 2015 budget would be allocated to energy subsidies.
- Attempts to reduce fuel consumption in August 2014 resulted in long queues and panic buying as rumours of fuel shortages spread. The measures were therefore withdrawn at the end of August. Although the consumption of subsidized fuel did reduce to some extent, the impact was too small to make a significant contribution towards Indonesia's quota for subsidized fuel consumption in 2014.

Widodo Proposal to Share Fuel Price Increases is Turned Down

The proposal to share a fuel price increase between the outgoing and incoming administrations in Indonesia has been turned down by current president Susilo Bambang Yudhoyono. The economic team of the newly elected president, Joko Widodo, had proposed to increase Indonesia's fuel prices by 20 per cent within Yudhoyono's remaining two months, on the agreement that the Widodo administration would then raise prices a further 20 per cent after taking office.

The taskforce to manage the transition from Yudhoyono's to Widodo's administration—called the Jokowi-Kalla Transition House, and led by the former minister of industry and trade, Rini Soemarno—was established when the Electoral Commission (KPU) declared the electoral victory of Widodo. On fuel subsidies, the initial proposal from the transition team was to split equally the task to increase the fuel price with Yudhoyono's administration. Since Indonesia's expenditure on fuel subsidies is decided by the 2015 State Budget, which is

proposed by the Yudhoyono administration and then negotiated by parliament, the discussion was focused on the design of the budget proposal (GSI - IISD, 2014a).

The talks were able to begin in earnest after 21 August, when the Constitutional Court ruled out a legal suit from presidential candidate Prabowo Subianto and upheld the election result in favor of Widodo. This automatically validated Widodo as the new president of Indonesia for a 2014 to 2019 term. A private meeting between Yudhoyono and Widodo took place in Bali on August 27 (Voice of America, 2014).

Although the talk between the two leaders was presented as a more general discussion around the political transition and the upcoming State Budget, much of Indonesia's media has given heavy emphasis to the fuel price issue, almost on a daily basis. It is well-known to the public that Widodo is firmly in favour of reducing the fuel subsidy, but that this must be negotiated with Yudhoyono, since he will govern under a state budget made by Yudhoyono's administration for the first year of his term.

Yudhoyono diplomatically explained his decision to shut down the negotiation with Widodo through his YouTube account (Yudhoyono, 2014),

“...There is still a space for changes if the new government see that as necessity. There is an open possibility and it can be done. However, the State Budget Proposal 2015 shall be the definitive State Budget 2015 at the end of September this year. Therefore, if there are changes, they will be accommodated through a State Budget Revision 2015, just like we did in 2005, when we revised the budget that was set by Ms. Megawati in the previous year. So it is not true, that there is no chance for changes or adjustments...”

Specifically on the subsidy issue, Yudhoyono explained,

“...The subsidy has been the problem of Indonesian governments from time to time, not only the current government. Indeed, for a country that adopts a strong capitalistic system, or what is widely known as “neolib” [neo liberal, ed.], the subsidy system is despised. But I have a different opinion for Indonesia, taking into account that there are still many of our brothers living in poverty and with weak purchasing power, if the subsidy is genuinely to help the people, the amount is not exaggerated, and it can be directed accurately to the targets, I think it is not wrong... But I agree that in the future, the subsidy must be reduced...”

Yudhoyono added,

“...The pressure on my government to increase the fuel price can be said to be extraordinarily strong... As far as I can remember, in 2004 I did not push the previous government like that... If the objective is to secure the targeted budget deficit, then we actually have taken the necessary steps: we increased the fuel price last year, and this year we increased the electricity tariff, gas price and cut other parts of the budget. Please do not forget, I frequently asked for a fuel price increase throughout my term, but the parliament never approved it [sic]¹... Why are we suddenly under pressure to increase it now? Should not we think about the poor, should we not think to avoid putting more burden on the people? But if, within the next seven weeks, there is a dramatic

1. The Indonesian parliament did in fact approve price increases three times during President Yudhoyono's term: in 2005, 2008 and 2013. However, it is true that fuel price increases have always been hotly contested and debated by parliamentarians in the House of Representatives, and that an attempt to increase fuel subsidies in 2012 was not approved by parliament.

change—a sharp increase in international oil prices for instance—and it endangers our state budget, then I definitely will have to increase the fuel price.”

From this, it can be concluded that a fuel price increase is unlikely to happen under the remaining weeks of Yudhoyono's term. It also suggests that the upcoming State Budget 2015 will not accommodate any maneuver that enables the new administration to alter the fuel price, at least until the state budget revision window opens in 2015.

The possibility that Widodo will institute a price increase in the short term is not completely eliminated. The nearest window to put the reform agenda within the State Budget is currently taking place in the ongoing negotiations of State Budget 2015 by parliament. However the new political configuration in the parliament may not side in favor of Widodo, since he has indicated a preference to maintain a tight coalition, rather than accommodating a wider spectrum of political parties in Indonesia. The core of the new ruling coalition led by PDI-P only occupies 37 per cent, far short of the simple majority needed to secure parliamentary approval.

Table 1. Result of Indonesia's Legislative Election 2014

Political party	Seats	Share of seats
Ruling coalition		37.0
Indonesian Democratic - Struggle (PDI-P)	109	19.5
National Democrat (Nasdem)	35	6.3
National Awakening Party (PKB)	47	8.4
People's Conscience (Hanura)	16	2.9
Neutral		
Democrat (PD)	61	10.9
Outside the ruling coalition		52.1
Greater Indonesian People Movement (Gerindra)	73	13.0
Functional Groups (Golkar)	91	16.3
Justice Welfare (PKS)	40	7.1
National Mandate (PAN)	49	8.8
United Development (PPP)	39	7.0
Total	560	100.0

Source: General Election Commission (2014).

State Budget Proposal: Indonesia's 2015 Fuel Subsidy

The proposed allocation of expenditure to fuel subsidies in 2015 has been set at 38 per cent higher than agreed in the initial State Budget 2014, or 18 per cent higher than the Revised State Budget 2014. The fuel subsidy value rises from IDR 210.7 trillion (US\$ 18.1 billion) in State Budget 2014 to IDR 291.1 trillion (US\$ 25.0 billion) in the 2015 proposal. Increased fuel subsidy expenditure is a trend that has continued since 2009. The value of the proposed fuel subsidy in 2015 is equal to 21.1 per cent of total central government spending.

The proposed allocation of expenditure to electricity subsidies has been set at 1.5 per cent higher than agreed in the initial State Budget 2014, or 30 per cent lower than the Revised State Budget 2014. The electricity subsidy rises from IDR 71.4 trillion (US\$ 6.1 billion) in the State Budget 2014 to IDR 72.4 trillion (US\$ 6.2 billion) in 2015. The smaller gap in electricity subsidy is made possible by an ongoing effort to adjust tariffs and to eliminate subsidies for several tariff classes in the past two years. The value of the proposed electricity subsidy in 2015 is equal to 5.3 per cent of all total central government spending.

Indonesia's state budgets are normally revised in the first semester of each year to allow fiscal adjustments

based on an analysis of the first quarter of economic performance. Although it is not mandatory, the negotiation between the government and the parliament over the state budget adjustment has become a regular feature every year, which in most cases has resulted in a higher fuel subsidy value.

Chatib Basri, the current Minister of Finance, explained that the higher fuel subsidy value in 2015 is made based on an assumption that there will be no price adjustment during the year. Of the total fuel subsidy value, IDR 44.6 trillion is allocated to cover subsidy costs unpaid from the previous year, leaving around IDR 246 trillion to cover a consumption quota of 48 million kiloliters of subsidized fuel (Detik, 2014a). In 2014, the government allocated 46 million kiloliters of subsidized fuel, costing a total of IDR 246.49 trillion. Taking into account that the government estimates a weaker rupiah against the US dollar in 2015, the value of fuel subsidy may need to be revisited next year.

Widodo is working to negotiate a State Budget that will support his vision to reduce the fuel subsidy. One day after the State Budget Proposal 2015 was announced, he took a jab at the huge fuel subsidy in the State Budget Proposal, stating that he did not like the size of it and that he hoped it could be reduced (Detik, 2014b). Widodo and his team questioned the alignment of the state budget

Table 2. Energy Subsidy Breakdown in State Budget Proposal 2015

	IDR trillion			US\$ billion		
	State Budget 2014	Revised State Budget 2014	State Budget Proposal 2015	State Budget 2014	Revised State Budget 2014	State Budget Proposal 2015
Fuel subsidy	210.7	246.5	291.1	18.1	21.2	25.0
Electricity subsidy	71.4	103.8	72.4	6.1	8.9	6.2
Total	282.1	350.3	363.5	24.3	30.1	31.3

Source: State Budget Proposal 2015

Table 3. Macroeconomic Assumptions of Indonesia's State Budget 2015

Description	Revised State Budget 2014	State Budget Proposal 2015
Growth (%)	5.5	5.6
Inflation (% yoy)	5.3	4.4
IDR/USD exchange rate (Rp/US\$)	11,600	11,900
Interests rate (%)	6.0	6.2
Indonesian crude price (US\$/bl)	105	105
Crude oil production (thousand barrels per day)	818	845
Natural gas production (thousand barrels of oil equivalent per day)	1,224	1,248

Source: State Budget Proposal 2015

proposal with the policy trajectory that will be taken by the new administration (Solo Pos, 2014). Yudhoyono openly refuted the accusation of obstructing the new administration, while at the same time defending his decision by stating “every administration has its own challenge”.

The table below summarizes statements from nine existing political factions in the Indonesian parliament towards the fuel subsidy clause in State Budget Proposal 2015. The identification of a party as “for” or “against” the subsidy is inferred, based on the content of the statement itself. There are only two factions, Hanura and PPP, that have called for reducing the fuel subsidy, while Gerindra called for significant changes to the fuel subsidy system. The other political factions, except PAN, showed support towards the continuation of the fuel subsidy, with additional comments that its mechanism should be improved. Interestingly, the position of PDI-P—Widodo’s party and the prime opposition towards fuel subsidy

removal during the ten years of Yudhoyono’s presidential term—supported an improved fuel subsidy, in contrast to Widodo’s objective to remove it gradually. Maruarar Sirait, the Chairman of PDI-P, dismissed the idea that the failure to reduce fuel consumption through improved efficiency means that it is necessary to increase the fuel price. He argued there are still many ways to increase the government’s revenue from mining and tax, and if those can be done in Widodo-Kalla’s term, the fuel price increase can be avoided (Republika, 2014).

Written statements from Indonesian political parties may not be indicative of how parties will actually act when it comes to a decisive moment to determine fuel subsidy policy (GSI-IISD, 2012). Nonetheless, although the responses were delivered in general wording and lack an in-depth technical argument, they suggest that many political actors in Indonesia feel that the fuel subsidy is still relevant to supporting the country’s people and economy.

Table 4. Political Factions’ Responses to Fuel Subsidy Issue in State Budget Proposal 2015

Party	Stance on fuel subsidy		Notes from Political Factions’ Response to State Budget Proposal 2015
	For	Against	
Indonesian Democratic - Struggle (PDI-P)	X		The government needs to have clear criteria to decide who should receive the subsidy. The government’s spending on SKK Migas [the upstream oil and gas regulator] has to be provided through state budget mechanism. All parties involved in the oil and gas business need to comply with cost recovery and taxation regulations.
National Awakening (PKB)	X		The amount of fuel subsidy shows that the government is consistently paying attention to the poor. The fuel subsidy mechanism needs to improve its accuracy and should be supported by a transparent oil and gas industry database.
People’s Conscience (Hanura)		X	The government needs to reduce the fuel subsidy.
Democrat (PD)	X		Fuel subsidy system needs to be changed from a general price subsidy to a targeted subsidy. The subsidy should be used to protect the poor and to support business.
Greater Indonesian People Movement (Gerindra)		X	It is a pity that the budget deficit, which is financed by debt, is burned on the road. The government needs to totally restructure the fuel subsidy system.
Functional Groups (Golkar)	X		The fuel subsidy is a fiscal instrument to help the people, but it needs to be improved in order to accomplish its goal.
Justice Welfare (PKS)	X		The government needs to make sure that fuel subsidy will not exceed the quota.
National Mandate (PAN)	-	-	PAN did not provide a response on the fuel subsidy issue.
United Development (PPP)	-	-	PPP did not indicate a clear position on fuel subsidy issue, but noted that there is still no significant step towards reducing the subsidy bill, which is dominated by fuel and electricity subsidies.

Source: Political Factions’ Responses to State Budget Proposals 2015.

Government Withdraws Policy to Restrict Subsidized Fuel Supplies

On 27 August, Hanung Budya, Director of Marketing and Trading of PT Pertamina, held a press conference to announce the normalization of subsidized fuel supply amidst growing public anxiety in many regions in Indonesia (Liputan6, 2014). The decision was taken in accordance with the government's instruction to lift the limitations on access to subsidized fuel that have been taking place since early August (see GS-IISD, 2014a).

As explained in the July edition of this news briefing (GSI-IISD, 2014b), the commitment to reduce the consumption of subsidized fuel was taken because the Indonesian government did not consider it viable to increase fuel prices in its 2014 State Budget Revision. As a consequence, the government initiated several programs aimed at restricting subsidized fuel consumption. Those programs are:

- The reduced availability of gasoline pumps selling subsidized fuel, commonly referred to as “nozzle reduction”;
- Preventing the sale of subsidized fuel in 26 gas stations in Central Jakarta and all gas stations within toll routes;
- Introducing a time limit (between 8am to 6pm) for the sale of subsidized fuel in areas considered to be prone to illegal distribution.

In the implementation these programs, early in August, PT Pertamina cut the supply of subsidized gasoline by 5 per cent and the sale of subsidized diesel by 15 to 20 per cent in all gas stations, a move that was immediately followed by long queues in many areas in Indonesia. In the North Coast route (Pantura), the main backbone of Java's logistics and transport, the lines reached a kilometer in length and stayed for hours in several places. Some customers even stayed overnight at gas stations to maintain their turn to buy the fuel. (Republika, 2014b; Merdeka, 2014; MetroTV, 2014). Cases were reported in several areas of people fainting while queuing for fuel, while in Wates, a man died from heart failure after waiting in the line for hours (Bangka Pos, 2014). In Yogyakarta, a motorcyclist became a media sensation for sparking ethnic discontent after being denied service by gas station's staff because she queued in the line for cars to avoid a longer line for motorcycles (The Jakarta Globe, 2014; Tempo, 2014).

Contrary to widespread belief that the restrictions have had no effect on fuel consumption, M. Iskandar, the Vice President of Fuel Marketing of PT PERTAMINA, reported that between 18 to 25 August the policy had reduced subsidized diesel consumption by 13 per cent and subsidized gasoline by 5 per cent, and increased the consumption of non-subsidized gasoline from 2,800 kiloliters to 3,300 kiloliters per day (Katadata, 2014). However, this was considered insignificant in terms of achieving the annual quota target.

During the implementation of these limitation policies, the government was struggling to counter widespread anxiety and rumors of fuel scarcity. Officials from related line ministries and PT Pertamina made statements to counter these fears, and clarified that although the subsidized fuel was reduced, the supply of non-subsidized fuel was widely available and the supply was running without any problem (MOEMR, 2014; Okezone, 2014).

For Indonesia, this was a test of the idea that “people are willing to pay a higher price of fuel as long as it can be easily acquired and it has a stable supply” (Okezone, 2012; Merdeka, 2014; Liputan6, 2014). This notion came into prominence based on actual cases, especially in remote areas, where prices are significantly higher than average in Indonesia, but people nonetheless continue to purchase fuel products.

This is not the first time that the government has withdrawn policies attempting to control the country's fuel subsidy. Previously, in February 2014, a policy to reduce subsidies for the fishery sector was withdrawn due to conflict with other regulation (GSI-IISD, 2014). In the previous year, a dual-pricing system—which was intended to set two different prices for the same grade of gasoline, one subsidized and the other non-subsidized—was withdrawn before it was even introduced, despite the readiness of some gas stations to implement the policy (GSI-IISD, 2013).

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Published by the International Institute for Sustainable Development.

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