# INDONESIA ENERGY SUBSIDY BRIEFING

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

## June 2016

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 Lasse Toft at ltchristensen@iisd.org.

## Highlights

- In anticipation of Ramadan it is unlikely the government will adjust fuel prices in July.
- With international oil price developments and the performance of the Indonesian Rupiah (IDR) in mind, the government may be facing a fuel price increase in the coming months.
- On June 2, 2016, during state budget revision talks with the parliament, the government proposed to reduce the subsidy on automotive diesel from IDR 1000 to IDR 350 per litre.
- Minister of Finance, Bambang Brodjonegoro, recently announced that implementation of electricity subsidy reform will be subject to another postponement.

### The Impact of Ramadan on Indonesian Fuel Prices

The arrival of Ramadan is normally seen to increase inflation on a range of commodities, including fuel prices, one of two such periods per year. The other period is year-end, which sees stronger demand for goods and services, similar to the month of Ramadan which in 2016 is from June 6 to July 6. This poses a challenge to the government's newly adopted fuel price system where price adjustments are expected no later than July 1.

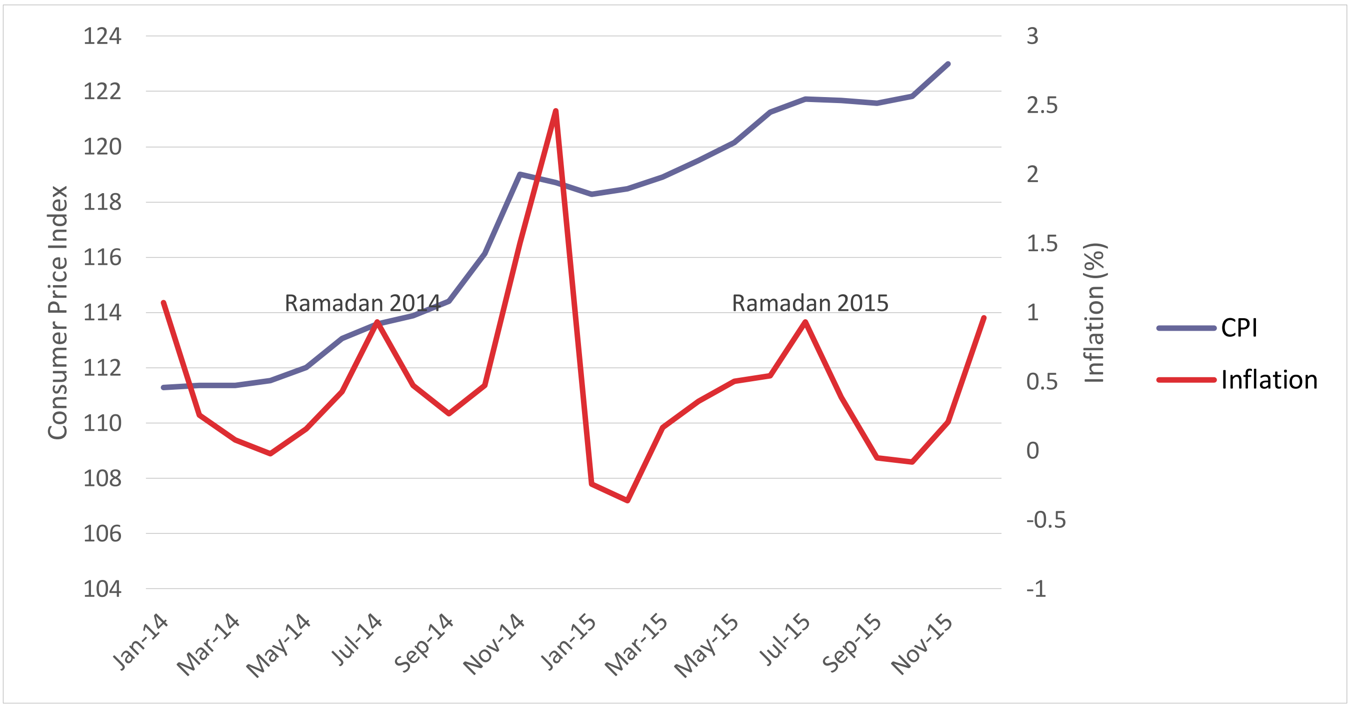
Indonesia introduced a new fuel pricing system in November 2015, aiming to revisit subsidized fuel prices every three months (GSI, 2016). Although Minister of Energy and Natural Resources (MEMR) Sudirman Said is mandated to change prices more frequently if necessary, the government has so far chosen to follow the three month period for price adjustments. Thus, the first price adjustment was implemented in January 2016, followed by a second, planned adjustment in April 2016. In both January and April, the government reduced the price of subsidized fuel in line with declining international fuel prices. In order to continue fuel price evaluations every three months, the next round of adjustments should be implemented in July 2016, colliding with the final week of Ramadan and the celebration of Eid.

In anticipation of Ramadan, however, it is unlikely the government will actually adjust prices in July. On May 31, Ahmad Bambang, Marketing Director of PT Pertamina (Indonesia's state-owned oil company), announced that the company will not increase fuel prices during Ramadan (Merdeka, 2016). IGN Wiratmadja, Director General of Oil and Gas, MEMR, echoed this statement by announcing that fuel prices would remain at current levels until after Eid, and indicated that the government is not too concerned with short-term oil price fluctuations. He further added that the government would examine prices again in September (Ministry of Energy and Mineral Resources [MEMR], 2016).

With international oil price developments and the performance of the Indonesian Rupiah (IDR) in mind, the government may be facing a price increase for the next round of adjustments. Since April 2016, international oil prices have been climbing toward USD 50 per barrel, up from USD 36.79 per barrel in April.

At the same time, the IDR has devaluated from IDR 13,134 per USD in April to IDR 13,547 per USD on May 31.

Figure 1 – Inflationary Cycle during Ramadan in Indonesia




Source: BPS, n.d..

A price increase would be the first upward adjustment of subsidized fuel prices since March 28, 2015 when the price of both subsidized diesel and gasoline was raised by IDR 500 per litre.

## Indonesia's Energy Security Fund

In April 2016, Minister Said announced that MEMR had received Presidential approval to bring the issue of Indonesia's energy security fund (Dana Ketahanan Energi, DKE) into the annual state budget revision talks with the parliament (Amelia, 2016).

The plan to establish the DKE has been discussed since 2015, but in January 2016 the government decided to postpone its establishment due to lack of legal support, and considerable opposition from various stakeholders, including the National Energy Council and a range of civil society groups. The initial design of DKE aimed to channel funds toward the deployment of renewable energy by adding a levy to the price of subsidized gasoline and diesel. The government will now be looking to further engage with the parliament on the issue and explore ways of establishing the fund.

While the energy security fund is up for discussion at the national level, it should be noted that a similar oil fund scheme is already in function at the subnational level in the oil-rich regency of Bojonegoro, East Java. As part of the agreement between the central government and Indonesia's regions, each oil and gas producing region is entitled to a certain percentage of total revenue. For oil production, the region is entitled to 15.5 per cent of total revenue, of which 0.5 per cent is locked for educational support with the remaining share being distributed to provinces, regencies and cities respectively. For this revenue, the regency of Bojonegoro has set up a fund to further invest in transportation and infrastructure as well as education (Tempo, 2016a). Bojonegoro's revenue comes from a number of oil fields in its area, including the Banyu Urip (180,000 barrels per day), Sukowati (16,000 barrels per day), Tiung Biru and Wonocolo (2,000 barrels per day each).

With an international oil price of USD 40 per barrel, the regency of Bojonegoro would be expected to bring in IDR 800 billion (USD 59.66 million) per year from the oil revenue-sharing agreement with the central government.

## Plan to Reduce Diesel Subsidy

On June 2, 2016, during state budget revision talks with the parliament, the government proposed to reduce the subsidy on automotive diesel. The proposal intends to reduce the subsidy on automotive diesel from its current levels at IDR 1,000 (USD 0.07) to IDR 350 (USD 0.03) per litre.

If the plan is approved by parliament, the total fuel subsidy allocation will drop from IDR 63.7 trillion (USD 4.75 billion) to IDR 40.6 trillion (USD 3.03 billion) (Primadhyta, 2016a). The state budget revision talks between Indonesian the government and the parliament are expected to be concluded by the end of June.

### Merger of PT Pertamina and PT PGN

Following a review investigating the opportunities to establish a state energy holding company, the government has decided to move ahead with plans to merge PT Pertamina and PT PGN (a state-owned company controlling a considerable share of gas transmission and distribution throughout the country). According to the government's plan, PT Pertamina will become the parent company, with PT PNG its subsidiary (Hermansyah, 2016a). The merger is part of a broader process to create holding companies for state-owned enterprises engaged in areas such as mining, banking, housing and construction and engineering (Tempo, 2016b).

The plan to create an energy holding company originated from a dispute over gas distribution and poor coordination around gas infrastructure development, leading to higher end-prices for consumers. The government has also previously expressed concerns about the lack of coordination and synergies between the two state-owned companies, compromising the progress of the highly profiled 35 GW plan that aims to increase electricity capacity (Inilah.com, 2015).

Huge efficiency savings are expected to be gained from the merger, and according to PT Pertamina the merger will lead to savings of around USD 1.6 billion in investments and also result in better coordination on gas distribution and operations. Likewise, for customers, the price of gas is expected to decrease (Hermansyah, 2016a).

### Electricity Subsidy Reform is Postponed

As part of recent budgetary discussions with parliament, Minister of Finance, Bambang Brodjonegoro, revealed that implementation of electricity subsidy reform will be subject to another postponement.

This is second delay of electricity subsidy reform this year, initially planned for implementation in early 2016, but since being delayed due to technical reasons around the ability to target recipients.

In parliament, Minister Brodjonegoro noted that the government will be asking for an additional electricity subsidy allocation of IDR 18.8 trillion (USD 1.40 billion) to cover the costs of prolonging the subsidy scheme (Primadhyta, 2016b).

For background, the plan to reduce electricity subsidies follows a process initiated in 2014, aiming to better align electricity tariffs with production costs. The current electricity market in Indonesia is divided into 12 non-subsidized tariff classes and two subsidized tariff classes, the 900VA and 450VA classes. Recent political discussions, however, have seen electricity subsidy reform move closer to implementation, and comments from PT PLN, Indonesia's state-owned electricity company, recently suggested that reform was imminent.

On April 9, 2016, the Head of the Commercial Division of PT PLN, Benny Marbun, announced that PT PLN would remove subsidies to all non-eligible 900VA connections, equal to 18 million customers. Marbun's statement was based on an evaluation conducted by the Indonesian National Team for the Acceleration of Poverty Reduction (TNP2K) which found that only 4 million out of 22 million consumers in the 900VA tariff class are categorized as poor households and should be entitled to receive subsidized electricity tariffs (KOMPAS, 2016).

PT PLN also indicated how electricity subsidy would be implemented, stating that tariffs for 900VA connections would be increased gradually from April levels at IDR 585/kWh (USD 0.04/kWh) to IDR 1,352/kWh (USD 0.10/kWh) in order to reach market levels (Fajriah, 2016).

Due to the fact that a minority of consumers with 900VA connections still need to receive subsidized electricity post-reform, it is likely that upcoming reform will lead to a dual pricing system within the 900VA connection class; one subsidized price for the 4 million eligible consumers and one market-based price for the remaining 18 million. Those consumers who will no longer be eligible to receive subsidized electricity via their 900VA connections will be offered to move to the higher, and also non-subsidized, 1,3000VA connection for free (Liputan6, 2016).

### Update on 35 Gigawatt Project

Indonesia's ambition to add 35 GW of power to its electricity capacity by 2019 continues to face hurdles. Recently, a main point of focus has been the slow tendering process, affecting the development of around 16 GW of power capacity.

Since the launch of the 35 GW plan in May 2015, increased power capacity has only reached 223 MW or 0.6 per cent of the overall target. These (three) projects include the Gorontalo gas power plant (4x25 MW), Taludaa mini-hydro power plant (3 MW), and Amurang gas power plant (125 MW) (Beritagar.id, 2016).

According to Minister Said, the problem originates from the slow process of expediting PT PLN's General Plan of Electricity Provisioning (Rencana Umum Penyediaan Ketenagalistrikan, RUPTL) which should be the base for the company to carry out public tenders for power capacity development (Sirait, 2016). Minister Said's statement, however, was rebutted by the CEO of PT PLN, Sofyan Basyir, claiming that the RUPTL had already been submitted to the government, and that PT PLN was actually waiting for the government's decision. As the result of the debate, Minister Said reportedly plans to let MEMR take over the tender process for 35 GW power plan project (Detik, 2016).

Nevertheless, according to Director General of Electricity, MEMR, Jarman, the 35 GW project is still on track. Thus, as of May 2016, 12,227 MW (34.4 per cent) out of 35 GW is already in the planning phase, 8,378 MW (23.6 per cent) is under procurement, and 3,742 MW (10.5 per cent) is being constructed.

## Coal Update

As reported in April 2016, the Indonesian Coal Mining Association (APBI-ICMA) called for the introduction of an artificial high domestic coal price, i.e., coal subsidies, to ensure supply for the 35 GW plan (GSI, 2016).

The call for subsidies from APBI-ICMA has since become more detailed, developing into a so-called cost-plus scheme in which the coal price is based on the cost of production and a 15–25 per cent profit margin.

Furthermore, the chairperson of APBI-ICMA, Pandu Sjahrir, underlined that the demand for a cost-plus scheme should not only be applied to mine-mouth power plants (related to the 35 GW power plant project), but to all domestic coal used for power production (BeritaSatu, 2016).

However, by early June, the government stated that it has still to evaluate the price proposal from APBI-ICMA and on June 8, PLN CEO, Basyir reported that neither the government nor PLN had decided on a pricing formula for purchasing coal as part of the 35 GW plan. He also underlined that the cost-plus pricing system was unlikely to be implemented this year or the next (Hermansyah, 2016b).

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