



INDONESIA ENERGY SUBSIDY REVIEW

A biannual survey of energy subsidy policies



Highlights

- On December 31, 2014, Indonesian President Joko Widodo announced the removal of subsidies on Premium gasoline and the introduction of a “fixed” subsidy that would set the price of Solar diesel at IDR1,000 (US\$0.08) below the market price. Due to low world oil prices, the immediate impact of this decision was to decrease gasoline and diesel prices on January 1 and then again on January 19, 2015. Kerosene prices remain unchanged.
- The reforms, in combination with low world oil prices, are expected to yield budgetary savings of around IDR195 trillion (US\$15.6 billion) from the State Budget 2015’s original allocation of IDR276.0 trillion (US\$22.1 billion) for petroleum subsidies. The savings are equal to over 9 per cent of total planned government expenditure. The Revised State Budget 2015 has been quickly prepared and finalized, increasing the budget for infrastructure from IDR190 trillion to IDR290 trillion (US\$15.2 billion to US\$23.2 billion).
- Because of falling world oil prices, no compensation mechanisms have been required, although a number of new systems to provide compensation were introduced before an earlier set of price increases in November 2014. They include a new health card and cash transfer systems that can deliver funds directly to individual savings accounts.
- A number of other price reforms have also taken place, with PT Pertamina increasing the price of a 12-kilogram (kg) cylinder of liquefied petroleum gas (LPG) as part of a pre-announced roadmap of increases, and PT Perusahaan Listrik Negara (PT PLN), Indonesia’s state-owned electricity company, introducing a number of scheduled increases in electricity tariffs for certain groups.
- The rationale for these reforms is starkly illustrated by experiences in 2014. Due to a variety of factors, subsidy costs were higher than planned, such that the Revised State Budget 2014 allocated a total of IDR246.5 trillion (US\$19.7 billion)¹ for petroleum subsidies and IDR103.8 trillion (US\$8.3 billion) for electricity subsidies. This amounted to a total of IDR350.3 trillion (US\$28.0 billion) for energy subsidies—24.1 per cent higher than originally budgeted, and equal to around 18.7 per cent of total central government expenditure and 3.8 per cent of anticipated GDP. In order to sustain this expenditure, a number of reductions were made in the budgets of ministries and government programs in the Revised State Budget 2014.

¹ Unless otherwise stated, all exchange conversions have been made at of IDR 12,500 per US\$.

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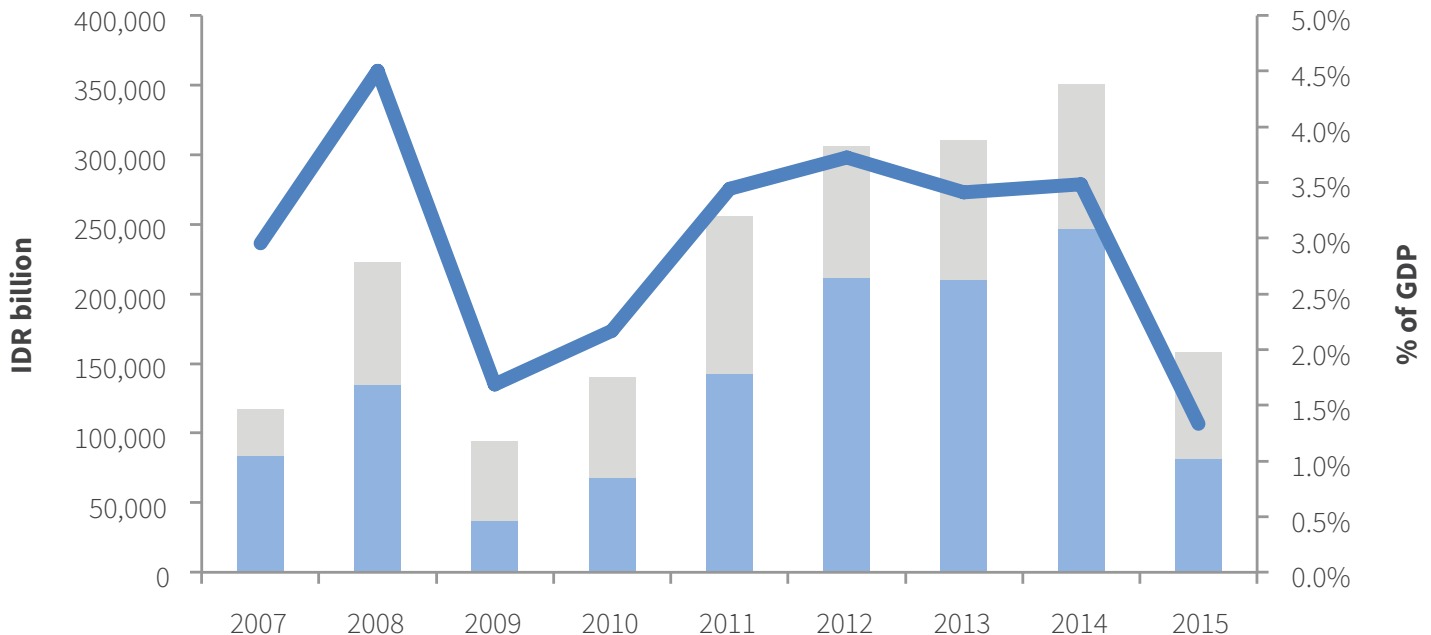
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Introduction

For a long time, energy subsidies have represented a significant fiscal burden for the Government of Indonesia. On average, payments related to consumer subsidies alone have amounted to around 3.1 per cent of annual GDP since fiscal year (FY) 2010—a cost that has led to intermittent macroeconomic instability and tends to crowd out core development expenditure. Despite being widely perceived as a form of social assistance, many of Indonesia’s energy subsidies are regressive, benefiting higher income groups disproportionately, due to a lack of targeting to the poorest. At the same time, the pricing system has encouraged wasteful energy consumption, providing little incentive to improve energy efficiency or to reduce domestic greenhouse gas emissions, and contributes to the deterioration of Indonesia’s trade balance. For these reasons, Indonesia’s fuel pricing policy merits attention.

This second edition of the *Indonesia Energy Subsidy Review* outlines the latest economic and policy developments that have affected Indonesia’s subsidized energy markets. Part One features a roundup of information on fuel subsidy expenditure and policy, including State Budget Revision 2014, the impacts that the Indonesian electoral cycle has had upon policy and the dramatic policy changes that have taken place in November 2014 and January 2015. Part Two features analysis by guest author Rahimah Abdulrahim, Executive Director of the Habibie Center, on the politics of subsidy policy; and an interview with Lembaga Survei Indonesia (LSI) on their recent work about public opinion toward reform. This edition concludes with a commentary by Professor Mohamad Ikhsan, Special Advisor to the Vice President at the Office of the Vice President of Indonesia, and Professor of Economics at the University of Indonesia.

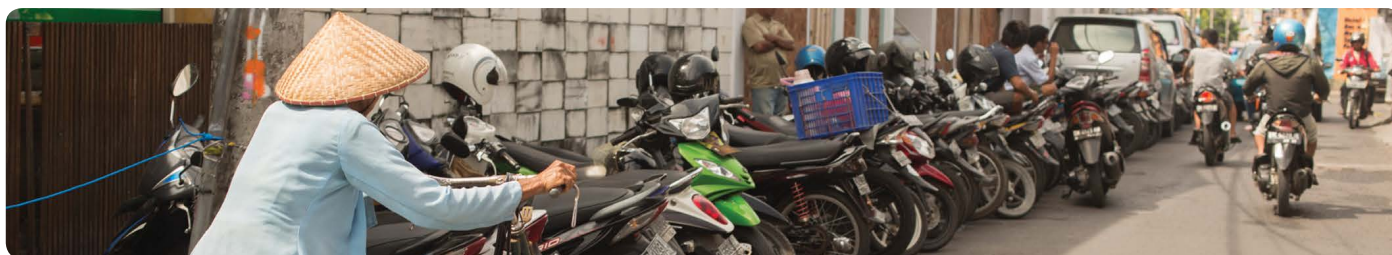
Figure 1: Total Energy Subsidy Expenditure in IDR Billion and as a Share of GDP



Note: 2013 data differs from Issue 1 Volume 1 as audited data has since been released. The share of GDP for 2014 and 2015 has been calculated based on the total GDP anticipated by the Revised State Budgets for 2014 and 2015.

Source: Ministry of Finance (2014a; 2015); Bank of Indonesia (n.d.b).

Part One: Recent trends in fossil-fuel pricing policy



(a) Overview of current fuel subsidy expenditure, 2013

Up until the end of 2014, energy subsidies (both for liquid fuels and electricity) continued to make up the largest single item of state expenditure in Indonesia. Following a revision to State Budget 2014, the total expenditure allocated to fuel subsidies for gasoline, diesel, kerosene and LPG was IDR246.5 trillion (US\$19.7 billion), just over 13 per cent of total planned expenditure. The revised 2014 budget also allocated IDR103.8 trillion (US\$8.3 billion) for electricity subsidies and IDR4.2 trillion (US\$0.3 billion) to subsidize the consumption of LGV (liquid gas for vehicles), amounting to a further additional 5.5 per cent of total planned expenditure. This saw energy subsidies make up 18.7 per cent of all planned government expenditure in 2014.

State Budget 2015 allocated IDR276.0 trillion (US\$22.1 billion) for petroleum subsidies and IDR68.7 trillion (US\$5.5 billion) for electricity subsidies, amounting to a total energy subsidy commitment of IDR344.7 trillion (US\$27.6 billion). Following reforms in November 2014 and January 2015, the Revised State Budget 2015 has dramatically reduced the allocation for petroleum subsidies to IDR81.8 trillion (US\$6.5 billion) and slightly increased the electricity subsidy allocation to IDR76.6 trillion (US\$6.1 billion).

Table 1: Assumptions and Energy Subsidy Allocations in Indonesia State Budgets, 2013 to 2015

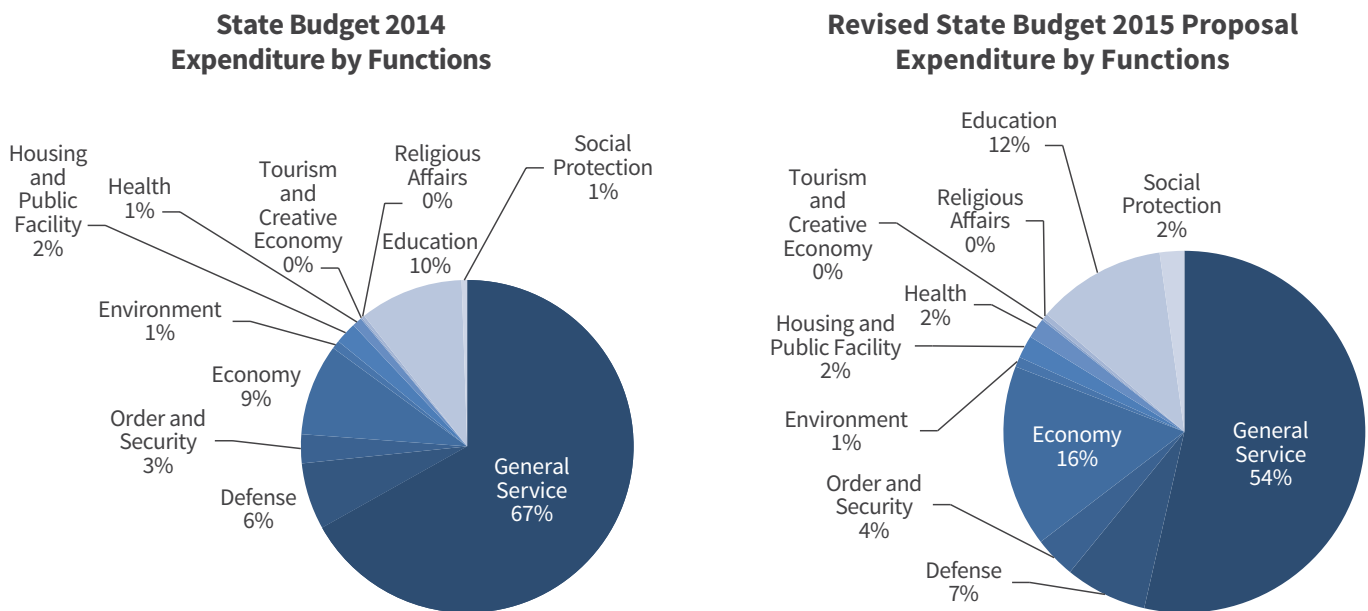
No	Indicators	State Budget 2013	Revised State Budget 2013	State Budget 2013 (Audited)	State Budget 2014	Revised State Budget 2014	State Budget 2015	Revised State Budget 2015
Macroeconomic Indicators								
1	Inflation year-on-year	4.9%	6.3%	8.38%	5.5%	5.3%	4.4%	5.0%
2	Growth	6.8%	7.2%	5.78%	6.0%	5.5%	5.8%	5.7%
3	Government's bond interest rate (3-mth)	5%	5%	4.5%	5.5%	6.0%	6.0%	6.2%
4	Oil production	0.9 mbd ¹	0.84 mbd	0.82 mbd	0.87 mbd	0.82 mbd	0.90 mbd	0.82 mbd
5	Gas production	1.36 mboed ²	1.24 mboed	1.21 mboed	1.24 mboed	1.22 mboed	1.25 mboed	1.22 mboed
6	Modelled exchange rate (IDR/US\$)	9,300	9,600	10,451	10,500	11,600	11,900	12,500
7	Indonesia crude price (ICP)	US\$100/bbl	US\$108/bbl	US\$105.87/bbl	US\$105/bbl	US\$105/bbl	US\$105/bbl	US\$60/bbl
Fuel Subsidy Expenditure								
8	Fuel subsidy spending ³	IDR193.8 trn (US\$18.5 bn)	IDR199.0 trn (US\$19.0 bn)	IDR210.0 trn (US\$20.1 bn)	IDR210.7 trn (US\$16.9 bn)	IDR246.5 trn (US\$19.7 bn)	IDR276.0 trn (US\$22.1 bn)	IDR81.8 trn (US\$6.5 bn)
	Quota of subsidized Premium, Solar & kerosene combined	46 mkl ⁴	48 mkl	48 mkl*	48 mkl	46 mkl	46 mkl	17.9 mkl
	Quota of subsidized LPG 3 kg	3.7 million ton	4.4 million ton	4.4 million ton	4.8 million ton	5.1 million ton	5.8 million ton	5.8 million ton
Electricity Subsidy Expenditure								
9	Electricity subsidy	IDR81.0 trn (US\$7.8 bn)	IDR100.0 trn (US\$9.6 bn)	IDR100.0 trn (US\$9.6 bn)	IDR71.4 trn (US\$5.7 bn)	IDR103.8 trn (US\$8.3 bn)	IDR68.7 trn (US\$5.5 bn)	IDR76.6 trn (US\$6.1 bn)
Fiscal Balances								
10	State revenue	IDR1,530 trn (US\$146.4 bn)	IDR1,502 trn (US\$143.7 bn)	IDR1,439 trn (US\$138.0 bn)	IDR1,667 trn (US\$133.4 bn)	IDR1,635 trillion (US\$130.8 bn)	IDR1,794 trn (US\$143.5 bn)	IDR1,769 trn (US\$141.5 bn)
11	State expenditure (including Transfer to Regions)	IDR1,683 trn (US\$161.0 bn)	IDR1,726 trn (US\$165.2 bn)	IDR1,650 trn (US\$157.9 bn)	IDR1,843 trn (US\$147.4 bn)	IDR1,877 trn (US\$150.2 bn)	IDR2,040 trn (US\$163.2 bn)	IDR1,995 trn (US\$159.6 bn)
12	Budget deficit	IDR153.3 trn (US\$14.7 bn)	IDR224.2 trn (US\$21.6 bn)	IDR211.7 trn (US\$20.3 bn)	IDR175.3 trn (US\$14.0 bn)	IDR241.5 trn (US\$19.3 bn)	IDR245.9 trn (US\$19.7 bn)	IDR225.9 trn (US\$18.1 bn)
13	Deficit to GDP ratio	1.65%	2.38%	2.33%	1.69%	2.40%	2.21%	1.90%

Notes: All figures rounded. All exchange conversions for 2013 are at the official audited rate for the period, IDR10,451 per U.S. dollar. All exchange conversion for 2014 and 2015 are made assuming a rate of IDR12,500 per US\$.

¹ Million barrels per day. ² Million barrels of oil per day equivalent. ³ Includes Premium, Solar, kerosene and LPG 3-kg combined. ⁴ Million kilolitres.

Source: Ministry of Finance (2012; 2013a); (National Audit Board, 2014); Ministry of Finance (2013b; 2014a); Ministry of Finance (2014b; 2015).

Figure 2: Government Expenditure by Function in 2014 and State Budget 2015 Proposal



Source: Ministry of Finance (2013b; 2015).

It is worth noting that, as a proportion of central government spending, total budgeted energy subsidy expenditure for 2014 was close to double capital expenditure, a key driver of long-term economic growth. Further, a high proportion of inflexible fixed expenditure items within the national budget (fuel subsidies, personnel expenditure, interest payments on debt etc.) have in previous years reduced the discretionary spending power of the government, limiting its ability to invest where necessary as the need arises. Following recent reforms, it has been possible for the government to increase the budget for infrastructure in Revised State Budget 2015 by more than 50 per cent, from IDR190 trillion to IDR290 trillion (US\$15.2 billion to US\$23.2 billion).

In previous years, total energy subsidy expenditure has always exceeded the amount allocated in the budget, so expenditure in 2014 may yet exceed the amount allocated in the Revised State Budget 2014. Audited data on 2013 found that spending on energy subsidies was IDR35 trillion (US\$2.9 billion) higher than initially budgeted and IDR11 trillion (US\$0.9 billion) higher than even the revised budget. This was partly due to fuel consumption being 4 per cent higher than anticipated; partly due to the rupiah depreciating dramatically in 2013, averaging at IDR10,500 per US dollar, instead of the assumed IDR9,300 per U.S. dollar; and partly due to international oil prices being on average US\$5 above the originally assumed rate. The government's inability to control these exogenous factors is what has made fossil-fuel subsidies a fiscal liability that draws away expenditure from other government priorities.

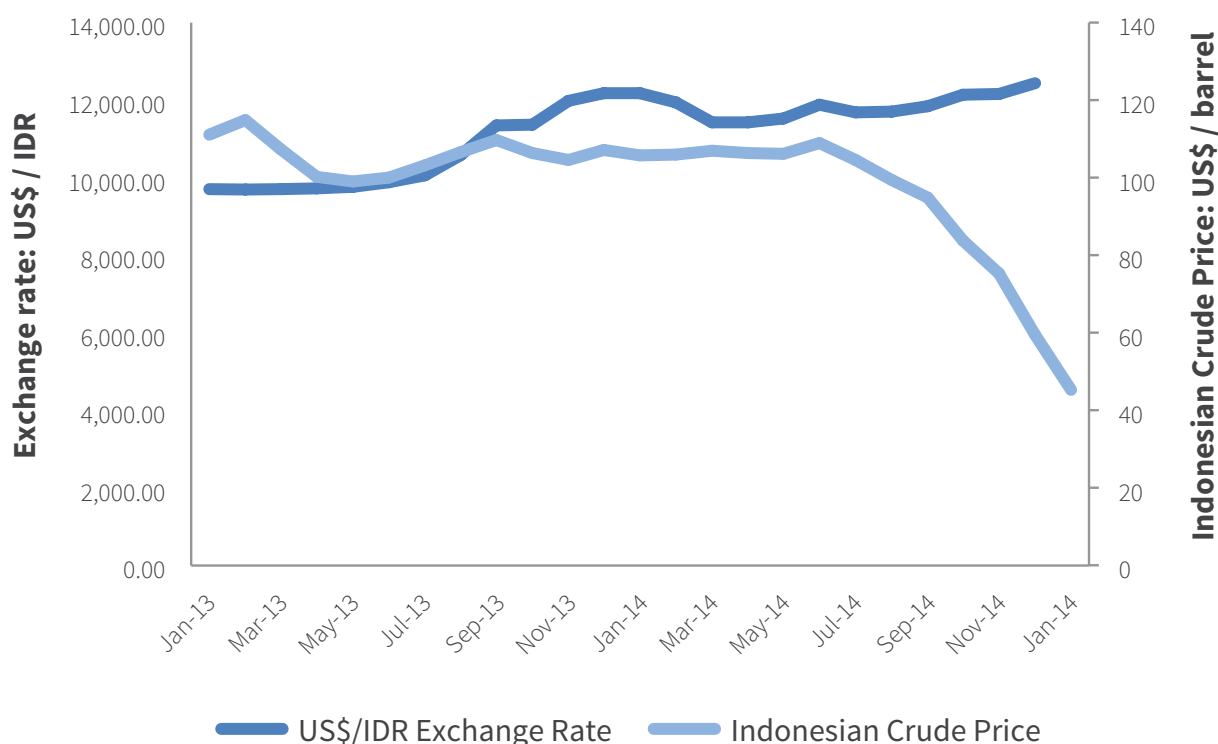
Some of these conditions continued to prevail in 2014. As illustrated in Table 2, the consumption of subsidized gasoline, diesel and kerosene in the first quarter of 2014 was higher than the previous year, despite there being a smaller volume of subsidized fuel allowed for in the revised budget. In addition to this, the average exchange rate in the first six months of 2014—IDR11,745 per dollar—was significantly weaker than the IDR10,500 per dollar assumed in the budget (Figure 2). In addition, lower-than-anticipated production of domestic crude increased reliance on imports: the targeted level of oil and gas production for 2014 had to be reduced from 870,000 barrels per day to 818,000 barrels per day (Okezone, 2014a). The factor that remains hard to define for 2014 is crude oil import prices. Since October 2014, prices of international crude oil and Indonesian Crude have fallen significantly (see Figure 2), compared to the anticipated price of US\$105 per barrel. It remains to be seen how this decline will affect total expenditure once the budget has been audited, in combination with the other above-mentioned factors.

Table 2: Subsidized Fuel Consumption, 2013, 2014 and 2015 (in million kilolitres)

Fuel Type	2013	2013 Q1	Revised Budget 2014	2014 Q1	2015	Revised Budget 2015
Gasoline	30.8	6.98	29.43	7.1	29.6	0
Diesel	16.0	3.7	15.67	3.85	16.2	17.05
Kerosene	1.2	NA	0.90	0.25	0.9	0.85
Total	48.0		46.0		46.7	5.77

Source: Ministry of Finance (2012, 2015); MetroTVNews (2014); National Audit Board (2014); CNN Indonesia (2015).

Figure 3: Monthly IDR/US\$ exchange rate vs. Indonesian basket crude (IDR price, i.e., month-to-month IDR-US\$ rate x oil prices), 2013



Sources: OECD (n.d.); Bank of Indonesia (n.d.a); MEMR (n.d.); Tempo (2014c; 2014d); RambuEnergy (2014b; 2014c); AntaraNews (2015a; 2015b).

Fuel subsidy reforms announced on December 31, 2014 and implemented as of January 2015 ought to restrict the extent to which fossil-fuel subsidies represent a liability in future budgets. This is because the reforms have attempted to entirely remove the subsidy on Premium gasoline and to introduce a “fixed” subsidy for Solar diesel, whereby the price of Solar will be allowed to fluctuate with market conditions, and a fixed gap of IDR1,000 (US\$0.08) will be maintained between its price and international market prices. This means that no fiscal liability ought to be associated with gasoline prices and that the subsidy costs for diesel will not be forced to change due to fluctuations in international crude prices. Given that these reforms have been introduced during a period of low oil prices, however, it remains to be seen if the government will be able to maintain the new pricing system. When world oil prices increase once again, there will be significant political pressure to prevent domestic prices from increasing as well.

Box 1: A Tale of Two Budgets: The Opportunity Costs of Fossil-Fuel Subsidies

In 2014, the mid-year revision to the State Budget increased overall expenditure by IDR34.4 trillion (US\$2.8 billion) to a total of IDR1,877 trillion (US\$156.2 billion). Combined with lower-than-anticipated revenues, the budget deficit increased from IDR175.5 trillion (US\$14.0 billion, 1.69 per cent of GDP) to IDR241.5 trillion (US\$19.3 billion, 2.4 percent of GDP).

There were two main causes of the overall increase in state expenditure: first, the increase in debt interest payments, from IDR121.3 trillion (US\$9.7 billion) to IDR135.5 trillion (US\$10.8 billion), caused by the increase of government securities (SBN, *Surat Berharga Negara*) to cushion the overall budget deficit; and second, the increase in energy subsidies from IDR282.1 trillion (US\$22.6 billion) to IDR350.3 trillion (US\$28.0 billion), primarily caused by the prolonged depreciation of the rupiah.

If total subsidies increased by IDR68.2 trillion (US\$5.5 billion) and overall expenditure only by IDR34.4 trillion (US\$2.8 billion), what budget items were cut in order to allow for this increased subsidy bill? Efforts were made to contain expenditure by cutting the budgets of government ministries and other institutions. Chatib Basri, Minister of Finance at the time, explained that the initial proposal was to source around IDR100 trillion (US\$8.0 billion) in this way, but that following internal challenges this was revised down to IDR43 trillion (US\$3.4 billion) (AntaraNews, 2014c). There is no simple direct relationship between increased expenditure on subsidies and decreased expenditure in other areas, because many adjustments upwards and downwards are made in a budgetary revision for a variety of reasons. Nonetheless, the essential nature of the trade-off is clear, as illustrated in Tables 4 and 5, which summarize some of the adjustments that were made to keep state expenditure within acceptable limits during 2014.

Table 3: Selection of Budgetary Revisions by Purpose, 2014

No	Function	State Budget 2014 (IDR bn)	Revised State Budget 2014 (IDR bn)	Changes (IDR bn)
Areas of increased spending				
1	Energy subsidy	282.1	350.3	68.2
2	Debt interest payments	121.3	135.5	14.2
Areas of decreased spending				
Economic Infrastructure				
Inter-regional connectivity				
	Ministry of General Works	84.1	61.6*	-22.5
	Ministry of Transportation	40.4	30.2*	-10.2
1	Energy infrastructure			
	Ministry of Energy & Mineral Resources	16.3	11.8*	-4.5
Housing				
	Ministry of Housing	4.6	3.2*	-1.4
Social Protection and Welfare				
Education				
	Ministry of Education	80.7	76.5	-4.2
	Ministry of Religion	42.6	44.6	2
	Education budget through other Ministries	7.1	7.1	0
	Education budget through transfer to region	238.6	238.8	0.2
Poverty Reduction				
2	Ministry of Internal Affairs	14.9	11.0*	-3.9
	Ministry of Social Affairs	7.7	5.4*	-2.3
	Ministry of Cooperatives and SMEs	1.6	1.1*	-0.5
Affordable Healthcare				
	Ministry of Health	46.5	41.0*	-5.5
	National Agency of Drug and Food Control	1.1	0.8*	-0.3
Food Supply and Price Stabilization				
	Ministry of Agriculture	15.5	11.8	-3.7
	Ministry of Maritime and Fishery	6.5	4.7*	-1.8
Social and Political Stability				
General Election 2014				
	Election Committee	15.4	16.8*	1.4
	Election Supervisory Body	3.3	4.0*	0.7
3	Defense			
	Ministry of Defense	86.4	77.2*	-9.2
National Security				
	National Police	45.0	40.3*	-4.7
Total				12.0

* Temporary figures from State Budget 2014 Revision Proposal.

Source: The categories of expenditure in this table are created by the author, based on budget breakdowns for different programs within Ministries as set out in the State Budget 2014 Revision Proposal (Ministry of Finance, 2014c), the Revised State Budget 2014 (Ministry of Finance, 2014a) and the summary infographic of State Budget 2014 (Ministry of Finance, 2014d). Due to data availability, it has not been possible to update some of the figures from the State Budget 2014 Revision Proposal, so these should be taken as indicative only.

Table 4: Selection of Budgetary Revisions by Institution, 2014

Description	State Budget 2014 (IDR bn)	Revised State Budget 2014 (IDR bn)	Changes (IDR bn)
Economy and Governance			
Anti-Corruption Commission (KPK)	616.9	483.5	-133.4
Center of Financial Transaction Report and Analysis	65.0	51.3	-13.7
National Audit (BPK)	2,895.7	2,196.7	-699.0
Supervisory Agency on Financial and Development (BPKP)	1,233.4	1,075.9	-157.5
Supervisory Committee of Business Competition (KPPU)	95.0	69.5	-25.5
National Commission of Human Rights	68.7	54.6	-14.1
Development and social assistance			
Ministry of Underdeveloped Regions	2,801.3	1,975.4	-825.9
Ministry of Women Empowerment and Children Protection	214.7	151.6	-63.1
National Commission for the Placement and Protection of Indonesian Migrant Workers	429.1	303.4	-125.7
Public services			
National Agency of Sidoarjo Mud Disaster Management	845.1	590.7	-254.4
National Agency of Terrorism Prevention	302.8	211.6	-91.2
National Archive	125.6	105.7	-19.9
National Library	435.1	405.7	-29.4
National Narcotics Agency	792.8	584.3	-208.5
Radio of Republic of Indonesia Broadcasting Agency	998.5	820.1	-178.4
Search and Rescue Agency (SAR)	2,188.8	1,523.8	-665.0
Television of Republic of Indonesia Broadcasting Agency	1,075.6	824.6	-251.0
Science, education and information			
Agency for the Assessment and Application of Technology (BPPT)	822.0	688.5	-133.5
Agency of Meteorology, Climatology & Geophysics	1,617.9	1,187.8	-430.1
Indonesia Institute of Science (LIPI)	1,072.7	883.9	-188.8
National Statistics (BPS)	3578.7	3,251.0	-9.2

Source: The categories of expenditure in this table are created by the author, based on budget breakdowns for different programs within Ministries as set out in Revised State Budget 2014 (Ministry of Finance, 2014a) and the summary infographic of State Budget 2014 (Ministry of Finance, 2014d).

In 2015, the same principle is illustrated but from the other direction. The fiscal space created by subsidy savings has allowed the government to significantly increase spending in a number of areas that are priorities for economic development and social welfare. As with 2014, not all fluctuations are attributable to energy subsidies; for example, efforts to tighten spending on official travel and meetings has also created significant fiscal space. But the general scale of opportunity costs incurred year-on-year by subsidies is clear. In the Revised State Budget 2015, Indonesia has been able to increase funding for state owned enterprises—in areas such as financing, construction, agriculture, and transportation sectors (see Table 5 for details). The Village Fund has also seen its budget allocation soar from IDR9 trillion (US\$0.7 billion) to IDR20.8 trillion (US\$1.7 billion). The Village Fund is a direct budget allocation to the lowest government administrative branches at subnational level, distributed to 74,093 villages across the country (Bisnis, 2015).

Table 5: Capital Injection to State-Owned Enterprises

No	State-Owned Enterprises	Sectors	Capital Injection	
			IDR trillion	US\$ billion
1	PT Dirgantara Indonesia (PTDI)	Aeronautics	0.4	0.03
2	PT Sang Hyang Seri	Agriculture	0.4	0.03
3	PT Pertani	Agriculture	0.47	0.04
4	PT Angkasa Pura	Airport	2	0.16
5	PT Utama Karya	Construction	3.6	0.28
6	PT Waskita Karya Tbk	Construction	3.5	0.27
7	PT Adhi Karya	Construction	1.4	0.11
9	PT Askrindo	Finance, Collateral Substitution Institution	0.5	0.04
10	PT Jamkrindo	Finance, Collateral Substitution Institution	0.5	0.04
11	PT Sarana Multigriya Finansial (SMF)	Finance, housing credit	1	0.08
12	PT Penjaminan Infrastruktur Indonesia (PII)	Finance, Infrastructure Collateral	1.5	0.12
8	PT Permodalan Nasional Madani	Finance, SME and Cooperatives	1	0.08
13	PT BPUI	Finance, SME and Cooperatives	0.25	0.02
14	Perum Perikanan Indonesia	Fishery	0.3	0.02
15	PT Perikanan Nusantara	Fishery	0.2	0.02
16	PT Geo Dipa Energi	Geothermal, Energy	0.6073	0.05
17	Perum Perumnas	Housing	1	0.08
18	PT SMI	Infrastructure financing	20.35	1.58
19	PT ASDP Indonesia Ferry	Marine transport and logistic	1	0.08
20	PT Djakarta Lloyd	Marine transport and logistic	0.35	0.03
21	PT Pelni	Marine transport, logistics, ports	0.5	0.04
22	PT Aneka Tambang Tbk	Mining	3.5	0.27
23	PT Perkebunan Nusantara III (PTPN III)	Plantation	3.15	0.25
24	PT Perkebunan Nusantara VII (PTPN VII)	Plantation	0.0175	0.00
25	PT Perkebunan Nusantara IX (PTPN IX)	Plantation	0.1	0.01
26	PT Perkebunan Nusantara X (PTPN X)	Plantation	0.0975	0.01
27	PT Perkebunan Nusantara XI (PTPN XI)	Plantation	0.065	0.01
28	PT Perkebunan Nusantara XII (PTPN XII)	Plantation	0.07	0.01
29	PT Pelindo IV	Port	2	0.16
30	PT PLN	Power / Electricity	5	0.39
31	PT Kereta Api Indonesia (PT KAI)	Railroad	2	0.16
32	PT Garam	Salt	0.3	0.02
33	PT Pindad	Security, strategic defense, weaponry	0.7	0.05
34	PT Dok Perkapalan Nusantara Surabaya	Ship	0.2	0.02
35	PT Dok Kodja Bahari	Ship	0.9	0.07
36	PT Industri Kapal Indonesia	Ship	0.2	0.02
37	PT PAL	Ship	1.5	0.12
38	PT Perusahaan Pengelola Aset	State Treasury	1	0.08
39	Perum Bulog	Strategic Food	3	0.23
40	PT Pengembangan Pariwisata	Tourism	0.25	0.02
Total			64.8773	5.05

Source: Ministry of Finance, (2015); SindoNews, (2015).

(b) Indonesia's Efforts to Address the Energy Subsidy Burden, 2014.

During the first nine months of calendar year 2014, there were relatively few policy changes attempting to address energy subsidies, in large part due to concerns around the political sensitivity of energy price changes in the run-up to parliamentary elections in April and the presidential election in July. Notable pricing policy changes during this time included:

- **January 1—attempt to raise price of 12-kg cylinder LPG; partially reversed.** PT Pertamina announced that 12kg-cylinder LPG would increase in price from IDR5,850 (US\$0.53) per kg to IDR9,809 (US\$0.88) per kg, a 67 percent rise. This was the first change in prices since 2009. PT Pertamina announced that it had suffered losses of IDR21.8 trillion (US\$2.0 billion) from distributing 12-kg cylinder LPG in 2008-2013 (The Jakarta Post, 2014a), and would continue to make a loss of IDR2,100 (US\$0.19) per kg under the new price (Kompas, 2014). PT Pertamina's position was supported by the National Audit Board (*Badan Pemeriksa Keuangan* [BPK]), which quantified Pertamina's losses in 2011 and 2012 at around IDR7.7 trillion (US\$0.69 billion), resulting largely from under-pricing 12kg-cylinder LPG (Liputan6, 2014a; The Jakarta Post, 2014a). On January 5, following considerable public opposition, Indonesian President Susilo Bambang Yudhoyono intervened, instructing PT Pertamina and associated ministers to review the initial decision within 24 hours (The Jakarta Post, 2014b). The next day, PT Pertamina scaled the price increase back to a quarter of the original size, setting 12kg-LPG's retail price at IDR6,850 (US\$0.62) per kg (Kompas, 2014).
- **January 15—attempt to restrict diesel subsidies for fisheries; fully reversed.** BPH Migas, Indonesia's regulator of downstream oil and gas, started implementing Presidential Decree No. 15/2012, which ruled that only two consumer groups in the fishery sector would be eligible for diesel subsidies: fishing boats with gross tonnage below 30 gross tonnes; and small aquaculture businesses. BPH Migas Circular No. 29/07/Ka.BPH/2014 prohibited distributors PT Pertamina, PT AKR Corporindo, and PT Surya Parna Niaga from selling subsidized fuel to any boats above 30 gross tonnes (Okezone, 2014b). Various groups immediately opposed BPH Migas's decision. After a meeting between the Coordinating Ministry of Economic Affairs, the Ministry of Fisheries, and the Ministry of Energy and Mineral Resources, the government responded by instructing BPH Migas to revise the policy (AntaraNews, 2014a; Tempo, 2014b). Indonesia therefore continued to provide diesel subsidies to fishermen in 2014.
- **June—biofuel subsidies reduced.** Although no change was made to gasoline, diesel, LGV, LPG or kerosene subsidies in the State Budget Revision, the government and parliament did agree to reduce the subsidy for bioethanol from IDR3,500 per litre to IDR2,000 per litre (US\$0.29 per litre to US\$0.17 per litre), and for biodiesel from IDR3,000 per litre to IDR1,500 per litre (US\$0.25 per litre to US\$0.13 per litre) (VivaNews, 2014).

Rather than price reforms, the first eight months of 2014 saw the government place an emphasis on “non-pricing” policies. This resulted from parliament's decision to reduce the annual quota for subsidized fuel in State Budget Revision 2014, effectively requiring the government to reduce consumption in order to avoid over-spending. In August, policies were introduced to reduce the number of petrol pumps selling subsidized fuel, to restrict the areas where subsidized fuel can be purchased and to stop selling subsidized fuel on the weekend. Despite long-standing plans to introduce radio frequency identification devices (RFID) to monitor and potentially control consumer fuel usage, RFIDs were not used. No formal evaluation of the non-pricing policies has been identified by this Review, but reported impacts on consumption indicate that their results did not appear large enough to justify the surrounding political fallout. Widespread public opposition and panic buying due to fear of fuel shortages led to the reversal of these policies the following month. For more information, see Box 2.

Box 2: Short- and Long-Term Efforts to Reduce Fuel Consumption

Early in August, a number of short-term policies were introduced in an attempt to reduce the consumption of subsidized fuel in Indonesia. This included:

- Reducing the availability of gasoline pumps selling subsidized fuel, commonly referred to as “nozzle reduction.” Early plans envisioned its implementation in 59 cities in Indonesia (AntaraNews, 2014b). By inconveniencing subsidized fuel buyers, and causing longer queues, it aimed to reduce consumption and promote the use of non-subsidized fuel.
- 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 8:00 a.m. to 6:00 p.m.) for the sale of subsidized fuel in areas considered to be prone to illegal distribution.

The immediate result of the programs was to cause long queues and social unrest in many areas in Indonesia. On the North Coast route (Pantura), the main backbone of Java's logistics and transport, lines reached a kilometer in length and stayed for hours in several places. Reports came in of customers staying overnight at gas stations, suffering health problems while waiting, and most notably, in Yogyakarta, a motorcyclist sparking ethnic discontent after being denied service for having queued in the wrong line (Lontoh & Beaton, 2014). The government struggled to counter widespread anxiety amid rumours of fuel scarcity, and on August 27, Hanung Budya, Director of Marketing and Trading of PT Pertamina, held a press conference to announce that the supply of subsidized fuel would return to normal (Liputan6, 2014b).

Although the policies did not prove to be politically successful, the Vice President of Fuel Marketing of PT Pertamina reported that between August 18 and 25 the consumption of subsidized diesel had reduced by 13 per cent and gasoline by 5 per cent, with consumption of non-subsidized gasoline increasing from 2,800 kilolitres to 3,300 kilolitres per day (Katadata, 2014).

Over the longer term, the government has also invested in a number of policies to reduce the consumption of petroleum fuels. However, to date, they have yet to have much impact on the downstream market. The most notable of these are:

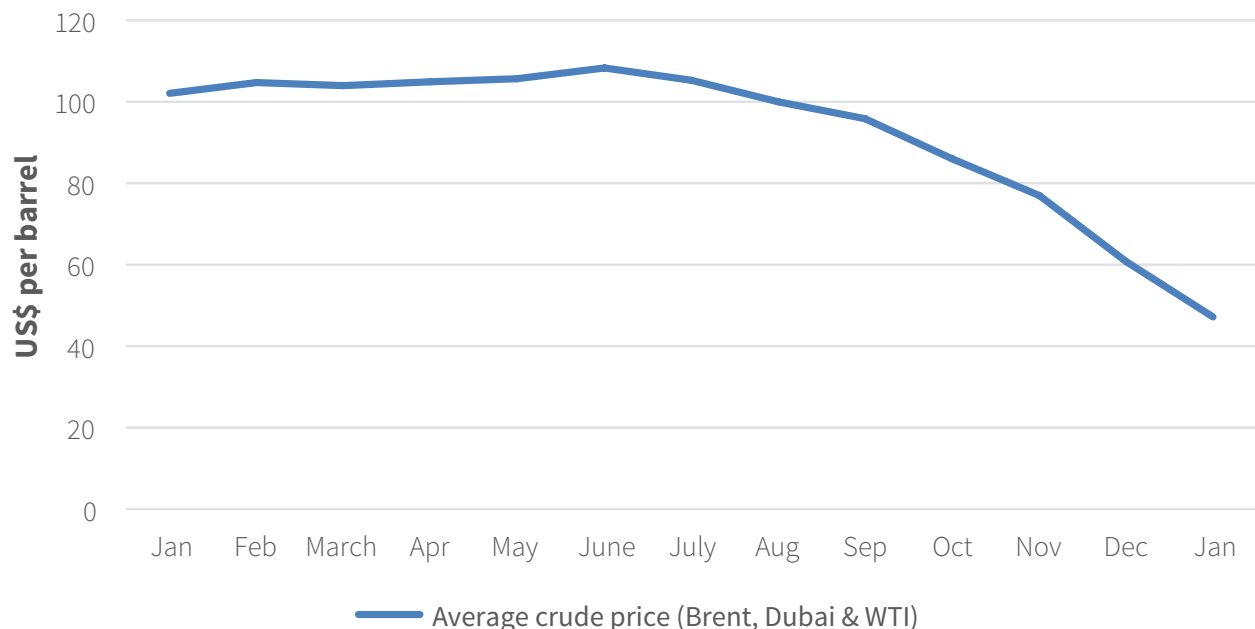
- For several years, statements have been made about introducing RFID technology to monitor and ultimately to limit the consumption of subsidized fuel. In theory, RFID equipment would be able to scan vehicles that are eligible to purchase subsidized fuel, to determine how much they have consumed and to enforce a quota for different kinds of buyer. However, there have been a number of technical problems in importing and installing the equipment; announced timelines have been pushed back on several occasions; and PT INTI, which won the tender for the five-year project, has had difficulties in obtaining financial support, as it was seen unattractive by the banking sector. PT INTI stated that in 2014 the project was expected to install the equipment at 5,027 gas stations and 100 million vehicles, but, as of end-February 2014, RFID devices were installed on only 270,000 vehicles (Bisnis, 2014). To put this in perspective: sales of new vehicles alone in 2014 were anticipated to be around 1.3 million (Indonesia Investments, 2014a).
- The program Conversion of Fuel to Gas in the Transportation Sector (*Program Konversi BBM ke BBG*) aims to diversify the market for transport fuels by promoting the expansion of infrastructure for compressed natural gas (CNG) for vehicles. The plan was revived by President Yudhoyono in a cabinet meeting in 2012 (Ministry of Energy and Mineral Resources, 2012), slightly before the government's attempt to increase fuel prices in 2012. The idea is not new, however, with Indonesia having experimented with the use of CNG in the transportation sector for decades. During Yudhoyono's administration, several programs have been related to this initiative, such as converter kit programs, gas-fired public buses and the installment of CNG dispensers in some gas stations.

In stark contrast, the final four months of 2014 and the first months of 2015 have seen the most dramatic changes to Indonesia's fossil-fuel subsidy policies in over a decade, following the inauguration of new President, Joko Widodo, who made clear his ambition to reduce fuel subsidies in numerous public statements both during and after his electoral campaign.

- **September 10—Increase in price of 12kg-cylinder LPG.** PT Pertamina develops a price adjustment scheme to take 12kg-cylinder LPG to market prices by 2016 and the first increase is implemented in September 2014, taking the price from IDR92,800 to IDR114,300 per cylinder (US\$7.42 to US\$9.14 per cylinder) (Indonesia Investments, 2014b).
- **November 17—Price increases for Premium gasoline and Solar diesel.** After much speculation, the government announced that price hikes for subsidized gasoline and diesel would take effect from November 18. The price of Premium gasoline rose from IDR6,500 to IDR8,500 per litre (US\$0.52 to US\$0.7 per litre) and Solar from IDR5,500 to IDR7,500 per litre (US\$0.44 to US\$0.62 per litre). In his announcement, President Widodo explained that the government intended to use the funds for infrastructure, education and healthcare. He further stated that recently introduced delivery mechanisms for social assistance—the Prosperous Family Card, the Indonesia Healthy Card and the Indonesia Smart Card—would be used to support the vulnerable and promote economic activity (Sekretariat Kabinet RI YouTube Channel, 2015).
- **December 24, 2014—New law provisions monthly electricity tariff adjustments.** Sudirman Said, the new Minister of Energy and Mineral Resources, explains that the new law—in force as of January 1—will see the electricity tariff determined by PT PLN, with tariff adjustments on a monthly basis, based on an evaluation on the IDR—US\$ exchange rate, the Indonesian Crude Price and the inflation rate.
- **December 31—Announcement that subsidies for Premium gasoline will be largely removed and subsidies for Solar diesel will be reduced, resulting in immediate price reductions.** Following a sharp and continued decline of world oil prices since mid-2014, a suite of Ministers announced that Indonesia's fuel prices would be lowered as of January 1, 2015. The price of Premium (gasoline RON 88) was decreased from IDR8,500 to IDR7,600 per litre (US\$0.68 to US\$0.61 per litre), while the price of Solar-brand automotive diesel was lowered from IDR7,500 to IDR7,250 per litre (US\$0.6 to US\$0.58 per litre). The price of kerosene was untouched, remaining at IDR2,500 per litre. At the same time, the government announced that going forward there would be no subsidies for gasoline, except for subsidizing distribution costs outside the Java-Madura-Bali, and that diesel would be subject to a “fixed” subsidy of IDR1,000 (US\$0.08) below market prices. The government intends to announce price changes every two to four weeks (Lontoh & Beaton, 2015).
- **January 1—Increase in price of 12kg-cylinder LPG.** PT Pertamina implements its next scheduled price increase of 12kg-cylinder LPG, increasing prices to IDR134,700 (US\$10.78) per cylinder (The Jakarta Post, 2015).
- **January 16—Decrease in price of gasoline and diesel.** In the first of its regular price announcements, the government announced that the price of automotive fuels would decrease once more, as world oil prices continued to fall. From Monday, January 19, the price of Premium fuel was lowered from IDR7,600 to IDR6,600 per litre (US\$0.61 to US\$0.53 per litre) and the price of Solar-brand diesel from IDR7,250 to IDR6,400 (US\$0.58 to US\$0.51 per litre).
- **January 19 —Decrease in price of 12kg-cylinder LPG.** PT Pertamina adjusts prices for 12kg-cylinder LPG again, this time reducing prices to IDR129,000 (US\$10.32) per cylinder.
- **February 13 —Revised State Budget 2015 is agreed, reallocating subsidy savings. Increase to biofuel subsidies is considered by not accepted.** Parliament passes a proposal to increase the subsidy for biodiesel from IDR1,500 to IDR4,000 per litre (US\$0.12 to US\$0.32 per litre) and bioethanol from IDR2,000 to IDR3,000 (US\$0.16 to US\$0.24). This is however subsequently rejected by a parliamentary budgetary body and the policy change does not take place. (Mongabay, 2015).

- **March 1—Increase in price of gasoline.** The government announces that the price of Premium gasoline will increase to IDR6,900 (US\$ 0.55) per litre. The price of diesel is not changed.
- **March 28—Increase in price of gasoline and diesel.** The government announces that the price of Premium gasoline is increased to IDR7,900 (US\$ 0.59) per litre and the price of diesel is increased to IDR6,900 (US\$0.55) per litre.

Figure 4: Average International Crude Oil Price, 2014–2015



Source: World Bank (2015). Nominal US\$.

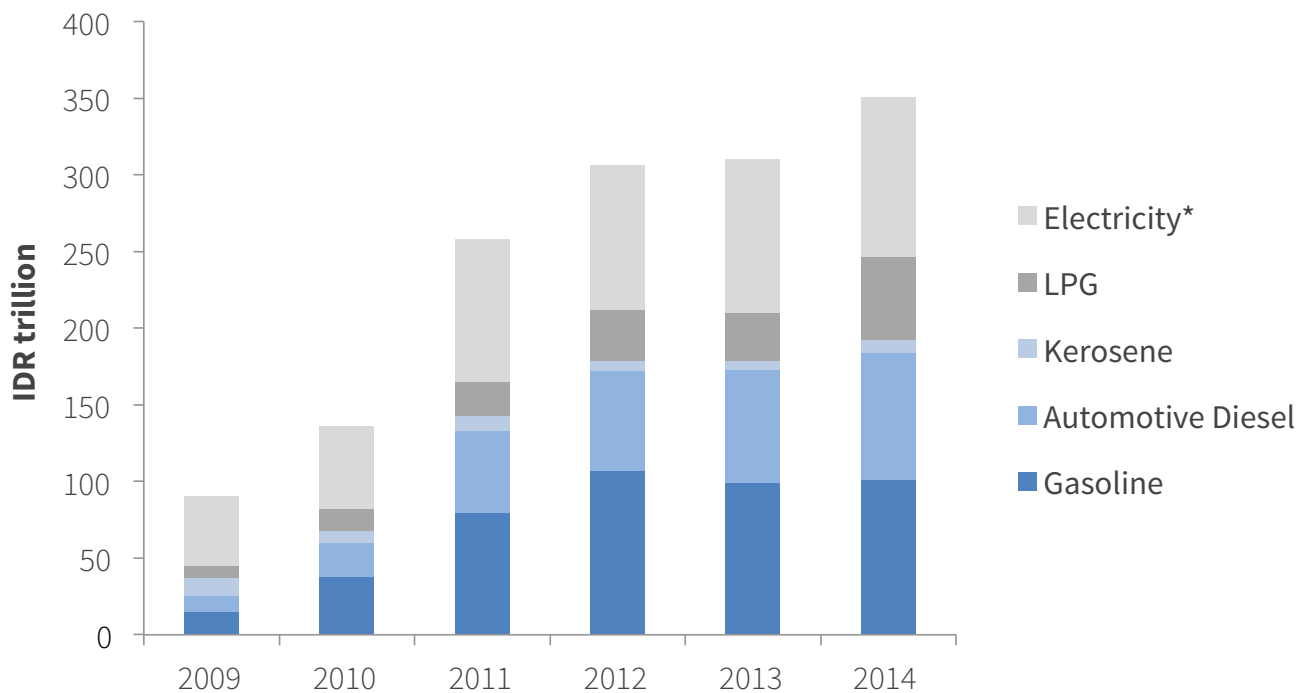
c) Looking Forward – Reallocation of savings and entrenching reforms

Recent changes in Indonesian subsidy policy have been dramatic and make it difficult to predict what should be expected in subsequent months. Key issues that are likely to dominate energy pricing debates in month to come include:

- **How should subsidy savings be spent?** Revised State Budget 2015 has reduced the allocation of state funds to fuel subsidies by just over IDR211 trillion (US\$16.9 billion), equal to over 10 per cent of all originally planned government expenditure in 2015. This scale of funding is a huge opportunity for Indonesia to invest in its core development priorities but much attention will be paid to how it has been reallocated and whether spending has been effective.
- **What will be the environmental impacts of reallocating savings to the energy sector?** Subsidy reform is generally welcomed on environmental grounds, because low-cost fuel tends to cause people to buy more fuel, which in turn worsens local and global environmental problems. However, it is likely that the reallocation of subsidies will be a subject of debate in two respects: first, whether subsidy savings have contributed toward the support of coal-fired power generation in Indonesia, given analysis by the International Energy Agency (IEA) and others that Indonesia’s ambitions to expand coal-fired power generation are at odds with its stated goal on the reduction of greenhouse gas emissions (Darby, 2015); and second, the ways in which subsidy savings could promote the construction of low-carbon infrastructure in Indonesia, particularly in the development of distributed renewable energy generation.
- **How will the government make sure that the new energy pricing system is not reversed in future?** It is relatively easy to announce the removal of subsidies when this can be achieved by reducing the price of gasoline and diesel. The government is likely to experience significantly more push-back when world oil prices begin to climb again and the prices of gasoline and diesel must be adjusted to levels that domestic consumers have not faced before. It is unclear what plans the government has to ensure that it can help assist the vulnerable with the impact of energy price volatility and resist political pressure without resorting to fuel-price intervention.
- **How will the government reshape oil and gas governance, which has been crippled by various legal attacks and political interventions?** The government has commissioned a special team to assess the situation and build recommendations for a new act on oil and gas management. One primary issue to be addressed is the architecture of Indonesian oil and gas governance that includes the arrangement of the market regulator, operator and policy-makers. The government–parliament talk on the new Oil and Gas Act will be the main feature in the next parliament session starting from 23 March 2015.

Beyond these near-term questions, it is unclear what stance the Widodo government has on the country's major remaining energy subsidies: for diesel (through the new "fixed" subsidy mechanism), kerosene, LPG and electricity. It is possible that the government may wish to harness the momentum of recent reforms to cut energy subsidies more broadly as 2015 continues. Alternatively, the government may judge that the short-term political cost of cutting Indonesia's remaining subsidies—smaller than the recently reformed fuel subsidies, but still significant—outweighs the long-term benefits.

Figure 5: Fuel and Electricity Subsidy Expenditure, by fuel, 2009–2014 (est., in IDR trillion)



Note:

* No breakdown of subsidy expenditure by fuel was made available in Revised State Budget 2014. In this figure, it has therefore been assumed that fuel subsidies in 2014 are divided between different fuels according to the same proportions as 2013. Note also that this figure indicates planned rather than actual expenditure for 2014, i.e., the impact of declining oil prices and subsidy reforms in November is not reflected in the bar for 2014.

Source: Ministry of Finance (2012; 2013) and National Audit Board (2014).

(d) Current dynamics in subsidized fuel markets

Gasoline (Premium-branded)—Gasoline prices remained fixed throughout most of 2014, until November 18, when prices were increased from IDR6,500 to IDR8,500 per litre (US\$0.52 to US\$0.7 per litre). On December 31, 2014, it was announced that prices would change again, this time being decreased, to IDR7,600 per litre (US\$0.61 per litre). It was announced at the same time that Premium gasoline would no longer be subsidized in Indonesia, categorized from now on as a "general fuel." The only exception to this was a subcategory of Premium gasoline called "special designated fuel," defined as Premium gasoline that is distributed outside the Java-Madura-Bali areas of Indonesia. This is also to be sold at market prices, with the exception that its distribution costs will remain subsidized. On Monday January 19, the price of Premium gasoline was decreased again to IDR6,600 per litre (US\$0.53 per litre) (Lontoh & Beaton, 2015). The first price increases took place in March.

Table 6: Changes in Premium Gasoline Price (IDR per litre), 2014–2015

	Pre-reform	18 November 2014	1 January 2015	19 January 2015	1 March 2015	28 March 2015
Premium gasoline	6,500	8,500	7,500	6,500	6,900	7,400

Source: Lontoh & Beaton (2015).

BPH Migas, Indonesia's downstream oil and gas regulator, declared that the task of distributing Premium in 2015 will be carried out by two companies, PT Pertamina and PT Aneka Kimia Raya (AKR) Corporindo Tbk. Initially, the two companies were allocated quotas of 29.46 million kilolitres and 20,000 kilolitres of Premium, respectively (RambuEnergy, 2014a). However, in recognition of subsequent changes to the fuel subsidy policy, downstream regulator BPH Migas has proposed reducing the volume of subsidized gasoline and automotive diesel from 46 million kilolitres to 17.9 million kilolitres (Liputan6, 2015), with only Pertamina distributing the remaining supplies of Premium fuel.

The new pricing formula for special designated gasoline states that prices will be determined by a base market price plus taxes (value added tax and a motor fuel tax) and minus a 2 per cent subsidy, to compensate distribution costs, paid to the distributor. The exact retail price is to be decided by individual marketing companies, with a profit margin pegged at between 5 to 10 per

cent of the base market price used by the government. The government's base price will be derived from an average international oil price index (Indonesia currently uses the Mean of Platts Singapore [MOPS]) and the central bank's US\$ buying rate from day 25 to day 24 in the previous month (Lontoh & Beaton, 2015). The concept of a base price in the fuel pricing formula is intended to articulate and preserve the core principle that the state controls the domestic fuel price (Ministry of Energy and Mineral Resources, 2014). According to recent reports, fuel retailers in Java-Madura-Bali are allowed to have a 5 to 10 per cent profit margin, while the profit margin for the retailers outside Java-Madura-Bali is uniform at 5 per cent (Merdeka, 2015).

Diesel (Solar-branded)—Like Premium gasoline, Solar diesel prices remained fixed throughout most of 2014, until November 18, when prices were increased from IDR5,500 to IDR7,500 per litre (US\$0.44 to US\$0.62 per litre). On December 31, 2014, it was announced that prices would change again, this time being decreased, IDR7,250 per litre (US\$0.6 to US\$0.58 per litre). It was announced at the same that from January 1 onwards Solar diesel would receive a “fixed” subsidy. This means that the price of Solar should vary in 2015, but with a fixed gap between domestic and market prices, set at IDR1,000 (US\$0.08). On Monday, January 19, the price of Solar diesel was decreased again to IDR6,400 (US\$0.6 to US\$0.51 per litre) (Lontoh & Beaton, 2015). The first price increases took place in March.

Solar diesel will also be distributed in 2015 by two companies, PT Pertamina and PT Aneka Kimia Raya (AKR) Corporindo Tbk, with quotas of 15.045 million kilolitres and 625,000 kilolitres of Solar, respectively (RambuEnergy, 2014a).

Table 7: Changes in Indonesian Fuel Prices (IDR per litre), 2014–2015

	Pre-reform	18 November 2014	1 January 2015	19 January 2015	28 March 2015
Solar diesel	5,500	7,500	7,250	6,400	6,900

Source: Lontoh & Beaton (2015).

Kerosene and LPG—Unlike gasoline and diesel, the price of kerosene was not altered in either November 2014 or January 2015, remaining at IDR2,500 (US\$0.20) per litre. In the long term, kerosene subsidy policy is closely linked to Indonesia's LPG-for-kerosene Conversion Program, which aims to substitute the use of subsidized kerosene with the subsidized 3kg-cylinder LPG in poor rural households. Some subsidized kerosene remains in distribution because the Conversion program determined that several areas of Indonesia—such as the Maluku islands archipelago and West Papua—would not be targeted for LPG conversion “for technical reasons” (PT Pertamina [Persero] & the WLPGA, 2012).

Like kerosene, there have also been no price changes in 2014 for 3-kg cylinders of LPG, which are sold at a subsidized rate of IDR5,000 (US\$0.40) per kg. The aim of the subsidy is to help support energy access for low-income households.

A number of price changes have however taken place for 12kg-cylinder LPG. This variant of LPG is the same fuel as the 3kg-cylinder variety, but sold in larger cylinders. It does not receive a formal government subsidy (through budgetary transfers) because the one-off cost of purchase is generally too expensive for low-income households to afford, and it is therefore not targeted for government support—however, 12kg-cylinder LPG is essentially subsidized. For several years PT Pertamina has sold the fuel below its cost of supply. The cost of this subsidy is born by PT Pertamina, which claims it has sustained losses of IDR21.8 trillion (US\$2.0 billion) for selling under-priced 12kg-cylinder LPG between 2008 and 2013. Attempts in January 2014 to increase the price of 12kg-cylinder LPG by 67 per cent were unsuccessful, following public outcry and a Presidential instruction to review the decision. Since that time, PT Pertamina developed a price adjustment scheme, declaring a timeframe for price increases of “non-subsidized” LPG every six months that would last until the end of 2016. This resulted in a September 2014 price increase from IDR92,800 to IDR114,300 per cylinder (US\$7.42 to US\$9.14 per cylinder) and again in January 2015 to IDR134,700 (US\$10.78) per cylinder. On January 19, prices were adjusted once again, this time downwards, to IDR129,000 (US\$10.32) per cylinder.

Electricity—Electricity subsidies in Indonesia are conferred by the different rates per kilowatt hour charged to different customer classes by PT PLN (PT Perusahaan Listrik Negara), Indonesia's state-owned electricity company: the public service (class S), households (class R), businesses (class B), industry (class I) and government and street lighting (class P), each of which is subdivided again into groupings of small, medium, and large power connections.

At the time of writing, the household class with connections of 1,300 VA and above, the business class with a medium and large power connections (B2 and B3), and most government classes have already reached or exceeded the point that PT PLN has targeted as being the market price, around IDR1,350 (US\$0.12) per kWh (Tempo, 2012), while subsidies continue to exist for several tariff classes, especially for the low-power connections in residential, business and industry classes. By number of power connections, those classes compose the largest block of electricity users in Indonesia.

The cost of the electricity subsidy in the past year has been particularly volatile, having increased by 45.4 per cent in the State Budget Revision 2014. The large rise in expenditure has been primarily driven by the weakening of the rupiah. In May 2014, Mr. Jarman, the Director General of Electricity in the Ministry of Energy and Mineral Resources, stated that for every IDR100 drop in the IDR/US\$ exchange rate, there would be an IDR1.1 trillion (US\$0.1 billion) increase in electricity subsidy expenditure (Detik, 2014).

To help cope with mounting electricity subsidy costs, Indonesia has been bringing the electricity tariff up with periodical adjustments according to a predetermined timetable since 2013. In January 2014, the government acquired parliament's approval to apply a tariff adjustment on industry classes with medium and large connections, I3 and I4 (Tempo, 2014a), as well as agreeing for more tariff adjustments to be phased in every two months, starting in May 2014 (Lontoh, Clarke, & Beaton, 2014). This has been successfully pursued (see Table 8) and, since May 2014, PT PLN website has also started to publish monthly tariff announcements (PLN, 2014).

Table 8. Electricity Tariff Adjustments for Selected Consumer Classes, May 2014 to January 2015

Tariff Group	Tariff Class	IDR per...	May-14	Jul-14	Sept-14	Nov-14	Jan-15*
Residential	R1 up to 450 VA	kWh	415.00	415.00	415.00	415.00	415.00
	R1 900 VA	kWh	605.00	605.00	605.00	605.00	605.00
	R1 1,300 VA	kWh	979.00	1,090.00	1,214.00	1,352.00	1,496.05
	R1 2,200 VA	kWh	1,004.00	1,109.00	1,224.00	1,352.00	1,496.05
	R2 3,500 VA - 5,500 VA	kWh	1,145.00	1,210.00	1,279.00	1,352.00	1,496.05
	R3 > 6,660 kVA	kWh	1,352.00	1,352.00	1,352.00	1,352.00	1,496.05
Business	B1 up to 450 VA	kWh	535.00	-	-	535.00	535.00
	B1 900 VA	kWh	630.00	-	-	630.00	630.00
	B1 1,300 VA	kWh	966.00	-	-	966.00	966.00
	B1 2,200 VA - 5,500 VA	kWh	1,100.00	-	-	1,100.00	1,100.00
	B2 6,600 VA - 200 kVA	kWh	1,352.00	-	-	1,352.00	1,496.05
	B3 > 200 kVA	kVArh	1,117.00	-	-	1,117.00	1,159.30
Industry	I1 450 VA	kWh	485.00	485.00	485.00	485.00	485.00
	I1 900 VA	kWh	600.00	600.00	600.00	600.00	600.00
	I1 1,300 VA	kWh	930.00	930.00	930.00	930.00	930.00
	I1 2,200 VA	kWh	960.00	960.00	960.00	960.00	960.00
	I1 3,500 VA - 14 kVA	kWh	1,112.00	1,112.00	1,112.00	1,112.00	1,112.00
	I3 Tbk > 200 kVA	kVArh	938.00	1,018.00	1,105.00	1,200.00	1,159.30
	I4 > 30,000 kVA	kVArh	819.00	928.00	1,051.00	1,191.00	1,011.99
Government	P1 6,600 VA - 200 kVA	kVArh	1,352.00	1,352.00	1,352.00	1,352.00	1,496.05
	P2 > 200 kVA	kVArh	1,026.00	1,081.00	1,139.00	1,200.00	1,159.30
	P3	kWh	997.00	1,104.00	1,221.00	1,352.00	1,496.05

Notes: There are differences between the tariffs published in the PT PLN announcement and in MEMR Regulations. In this table, the tariffs from May 2014 to November 2014 are extracted from MEMR Regulations. For January 2015, wherever there are differences, numbers from the PT PLN announcement are used, which seem likely to be more accurate in reflecting the current situation. The use of a * indicates that a PT PLN tariff announcement is the source. Blue indicates no change, green indicates a tariff increase and pink indicates a tariff decrease. Sources: PLN (2014); Ministry of Energy and Mineral Resources (2014a; 2014b; 2014c).

In 2015, PT PLN declared an increase of electricity tariff for several classes in 2015. According to the newest regulation signed on December 24, 2014 by Sudirman Said, the new Minister of Energy and Mineral Resources, the electricity tariff will be determined by PT PLN, and tariff adjustment will be conducted on monthly basis, based on an evaluation on the IDR—US\$ exchange rate, the Indonesian Crude Price and the inflation rate. This regulation is operational as of 1 January 2015.

Fuel consumption for PT PLN's power generation in Indonesia is dominated by coal, with 35.51 million tons in 2012 (PLN, 2013), equal to 57.35 per cent of the fuel consumption in Indonesia's power generation (Pusdatin, 2014).

e) Recommendations, 2015

Recent dramatic changes in fossil energy pricing are an enormous step forward for Indonesia, ending over a decade of large and uncontrollable public spending and freeing up funds equal to over 10 per cent of total government expenditure for other development priorities. The challenge over the next year will be to make the most of low oil prices by developing better systems for pricing fuel and for assisting vulnerable businesses and households when world prices rise again.

Based on the above analysis, the following recommendations are made for each fuel type.

Premium-brand gasoline and Solar-brand diesel

- Develop a roadmap for the implementation of a fuel pricing mechanism that is independent from the short-term political cycle and enforced by strong regulatory powers.
- Continue to improve capacity for providing assistance to businesses and households, particularly around large increases in world fuel prices. This should include creating explicit linkages for safety net policies to respond to large upward volatility in energy prices.
- Assess the impacts of ongoing price changes in 2015 to help inform policy. This should include detailed assessment of the relationship between fuel prices and the price of other goods across the economy.

Kerosene and LPG

- Continue the implementation of the LPG-for-Kerosene Conversion Program.
- Develop a roadmap for the ultimate reform of both 3kg-cylinder LPG and kerosene subsidies, determined by the time it will take to set up alternative policy measures that can ensure households have access to clean and modern forms of energy.
- Continue efforts to ensure that the price of 12kg-cylinder LPG is regularly changed to reflect market prices.

Electricity

- Continue the implementation of gradual price reforms until electricity pricing fully recovers the ongoing costs of maintaining and improving Indonesia's electricity system.
- Develop a comprehensive strategy to improve performance of electricity lifeline rates (rates granted to lower-income households).
- Maintain the expansion of electricity production and provide a business-friendly climate for new investment in the electricity sector, at the same time as ensuring that reallocated subsidy expenditure is used to promote low-carbon electrification options where possible, particularly in cases where geothermal power and distributed renewable generation may offer competitive performance versus conventional power generation technologies.

Part Two: Guest analysis



Fuel Subsidy and the Challenges for the New Government

By Rahimah Abdulrahim and Bawono Kumoro

Introduction

The once-every-five years “festival of democracy” that is the presidential election has now passed and the new government—led by President-elect Joko Widodo Vice-President-elect Jusuf Kalla—have quickly gotten to work. Despite some resounding economic achievements during the leadership of President Susilo Bambang Yudhoyono over the past 10 years, it is clear that sustaining the country’s booming economic growth is of prime importance. In order to achieve this, tackling Indonesia’s fuel subsidy has been rightly identified as a priority. How much has been achieved? What challenges are still to come?

The Fuel Subsidy Problem

For many years, the fuel subsidy has significantly overburdened the state budget, with a clear trend of year-on-year increases. In 2011, fuel subsidies reached IDR165 trillion, and in 2012 spending increased sharply to IDR211 trillion. Costs decreased slightly in 2013, to IDR210 trillion, but bounced back in 2014 to a new high of IDR246 trillion. The numbers are high for unproductive spending that does not contribute toward job creation. Meanwhile, budget allocation for infrastructure—a productive spending that contributes toward job creation and economic growth—in 2014 was only IDR206 trillion.

Much research has criticised the allocation of funding to fuel subsidies. Data from the Ministry of Energy and Mineral Resources in 2011 shows that the largest share of fuel subsidies has been enjoyed by the owners of four wheeled vehicles (53 per cent), instead of the owners of motorcycles (40 per cent) and public transport (3 per cent). Similarly, in a report entitled “Why is Reducing Energy Subsidies a Prudent, Fair, and Transformative Policy for Indonesia?”, the Chief Economist of the World Bank in Indonesia, Ndiame Diop, revealed shocking data that indicated IDR178 trillion of the fuel subsidy is enjoyed by the upper middle class, and not the poor who truly need it.²

Wasteful spending from having the wrong subsidy targets has long been a problem for Indonesia’s economy. This seems like a trap that we never fully escape. Across the eras of President Soekarno, President Soeharto, President Bacharuddin Jusuf Habibie, President Abdurrahman Wahid, President Megawati Soekarnoputri, and President Susilo Bambang Yudhoyono (SBY), fuel subsidies have been a difficult issue to solve. Political courage from the new government is required in order to proceed with strategic actions in managing the bloated fuel subsidy budget.

Rapid reforms—and future risks

Not long after the presidential inauguration, Joko Widodo’s administration decided to hike the subsidized fuel price in November 2014. Then, approaching 2015, President Joko Widodo announced a new fuel subsidy policy. The government decided to remove fuel subsidies on gasoline while implementing a fixed-subsidy system on diesel of IDR1,000 per liter. Therefore, gasoline price will be based on market mechanism and adjust to fluctuations of the world oil price. The government’s leadership on this issue is brave, rational and visionary, even though it is far from populism.

The decision should be appreciated for its positive impacts on fiscal sustainability. By letting the gasoline price follow the movement of world oil prices, the state budget will no longer be burdened by fuel subsidies and the government has more fiscal space to address other needs.

2. Ndiame Diop, “Why is Reducing Energy Subsidies a Prudent, Fair, and Transformative Policy for Indonesia?” *Economic Premise*, World Bank, Number 136, March 2014, p. 4.

Political Challenges of Parliament

The pros and cons immediately appeared after the government issued the policy. The reduction of fuel subsidies—what's more, removal of fuel subsidies—is seen to be unpopular politically. The policy will become an attractive political commodity for the parties in the parliament, especially opposition parties. By opposing the unpopular policy issued by the government, opposition parties will be perceived as “pro poor.”

Political challenges from parliament may be likely to occur considering the political stance of the Gerindra Party, Golkar Party, National Mandate Party (PAN) and Prosperous Justice Party (PKS). They have shown strong opposition against government policy on fuel subsidies. Opposition parties are currently collecting signatures from members of parliament to submit interpellation to the government. Interpellation is a right of the House of Representatives (DPR) to request clarification from the government regarding certain policies that are considered important, strategic, and have wide ranging impacts.

This is understandable since—as mentioned before—fuel subsidies are an interesting and “sexy” political commodity. But, such a mind-set is a self-interested one, pushing aside the interest of the people and replacing it with a political stage for politicians to seek popularity.

It should also be noted that all of the parties that signed the interpellation request are those who sit on the opposition bench against the government of Joko Widodo and Jusuf Kalla. Indeed, the political position of those parties serves as the determining factor that shapes their views regarding fuel subsidy. If political parties were in the position of the ruling coalition parties, it is not a stretch to suggest that they would adopt a more realistic and proportional approach regarding fuel subsidy reduction. On the other hand, opposition political parties will most likely disagree with fuel subsidy reduction even when they have supported such a policy in the past, as was shown by the parties that supported the interpellation. It should be noted that during President SBY's administration, all of those parties supported fuel subsidy reduction.

The same situation also applies to Indonesian Democratic Party of Struggle (PDIP) during SBY's regime. The current ruling party had been consistent in its opposition against fuel subsidy reduction. Under President Joko Widodo's regime, they changed their stance 180 degrees by showing a more realistic and proportional approach towards fuel subsidy.

Test of Time

It may not be easy for the new government to stick to its commitment to reform fuel subsidies. The public will see how brave the Joko Widodo-Jusuf Kalla government will be in confronting the economic ups and downs that will undoubtedly occur throughout their Presidency: will they be able to leave behind them an era of increased public spending on priorities like infrastructure, democracy, health and education; or will they return to the formula of previous governments, subsidizing fuel for the sake of continuing popularity and electability?

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Interview: Public Attitudes Toward Fuel Subsidy Reform

The reform of subsidies for fuel has received a great deal of attention in the past months. But what do citizens think? Toward the end of 2014, Lembaga Survei Indonesia (LSI) conducted a number of focus group discussions in Jakarta, Yogyakarta and dan Makassar, as well as a nationally representative survey of public opinion. Dodi Ambardi Ph.D. and Hendro Prasetyo Ph.D. from LSI agreed to speak with the GSI's Lucky Lontoh, to share thoughts on findings from their research.

To help our readers understand your research, can you briefly explain the difference between conducting “focus group discussions” and a “public survey?” Why do both, and how do they relate to one another?

A focus group discussion—or FGD—deepens our understanding about a particular subject matter, while a survey finds a representative output from a particular survey population.

The focus group discussion in this project was conducted to assess people's general understanding and attitudes towards the policy of fuel subsidy reform. It was conducted earlier than the survey, so it could be used as a secondary input to improve LSI's survey instruments. The FGDs were conducted in three cities, Jakarta, Makassar, and Yogyakarta. The main survey was intended to identify trends of public opinion and the elements that shape opinion.

Fossil-fuel subsidy reform is a controversial topic in Indonesia, so public opinion really depends on who you ask. How did you make sure your findings were representative?

FGD respondents were selected with several categories in mind. They were all inhabitants in the provinces of Jakarta, Yogyakarta or Makassar. The respondents from Jakarta were chosen to represent the views of those from a big city urban population; in Yogyakarta, to represent rural households (deriving from a small town outside the city of Yogyakarta and several villages in the regency of Bantul); and in Makassar, to represent populations outside the Java-Bali area. Each FGD group consisted of a 50:50 ratio of male and female participants.

For both the FGD and the survey, respondents were 17 years of age or older, or already married; in other words, people who are eligible to exercise political rights in the election. Both also considered the means of transportation that respondents have. This was classified into motorcyclists, commuters with public transport, and car owners. The project also paid attention to income classifications, which was divided into two groupings, a lower-income and an upper-income groups.

For the survey, LSI used a probability method—stratified random sampling—to choose the sampling population. The total number of respondents is 2,899, covering all regions in Indonesia. The margin of error with this approach is expected to be around 1.8 per cent, assuming a simple random sampling.

Did you see a large degree of support for or against a fuel price rise?

The baseline position of most of the respondents, regardless of their social strata and region, was a strong rejection of price increase initiatives. At the same time, most of the respondents underestimated the value of fuel subsidies. Most thought that spending is more-or-less equal to other government spending on other social welfare policies. Without further explanation, most respondents also failed to estimate that high-income society groups absorb most of the fuel subsidy, or at least, they estimated that the high-income group absorbed less than it actually does. Respondents' level of knowledge about fuel subsidy issues was weak and filled with inaccurate estimations. This was found among all respondents and all groupings.

After an explanation about the state of government spending, the respondents started to be more supportive of the idea of a budgetary adjustment, including the option to reduce the amount of fuel subsidy, such as a 10 per cent reduction. The approval for a price increase came with suggestions on how to improve government performance in other ways. The level of support for government varied among the respondents. Generally, public trust in the government was found to be weak, with some respondents even expressing hostility toward the government, especially among the higher income class. Weak public trust among the lower-income class was generally manifested in apathy toward government policy.

The forms of compensation most broadly supported by respondents were healthcare and education support. The respondents normally related the type of compensation they want with their lifestyle or living condition. Most respondents from lower-income classes suggested compensation focused at the micro level and closely related to their daily lives, such as more tangible financial or capital support to their businesses. Respondents from higher

income classes favoured more sophisticated compensation schemes, such as providing credit incentives to small businesses. This example shows how groups could favour similar goals, but with a different understanding of how the economy works in practice. Motorcycle and car owners, who were taken to represent the middle and high-income class, showed greater empathy toward the poor, but they had no firm idea of how to reduce the burden of policy change on the poor.

What were the reasons that people gave for their opinions? Were there any key issues that would change participants' minds?

In our view, an individual's place on various social "spectrums"—their individual situations, such as profession and experience—influenced their attitudes and answers. Additional information about the real value of subsidy and comparisons between government spending also incited further consideration. New information was able to change respondents' views to a considerable degree. Sympathy toward the poor drove respondents in reconsidering fuel subsidy expenditure.

Did people express an opinion on how subsidies should be reformed—such as how quickly subsidies should be removed?

People from a low-income class such as farmers and fishermen in Yogyakarta, and motorcyclists in Makassar, had a more radical stance on reform, preferring a "big-bang" approach, rather than gradual changes. They assumed that this would greatly ease the burden they have to endure, since they could escape potential repeated adjustments if reform is conducted in a gradual manner. They also expected that a big-bang approach would lessen the frequency of street demonstrations that potentially disturb their business. Some of the motorcyclists in Makassar cited that they are tired of having social turmoil in their hometown. Makassar is known for having massive violent protests, sometimes developing into conflict among social groups within society, every time the government has tried to pass the price increase policy. So in general, economic stability and peace and security were their main considerations.

People at a higher income level, represented by car owners, and respondents in Jakarta, tended to opt for a more conservative approach in order to lessen the economic impact.

Generally, did people feel like their opinions mattered, and that it was possible to have a dialogue with the government on if, when and how subsidies should be reformed?

The level of public trust in the government was weak. Respondents tended to show apathy or reluctance when asked about options for delivering their views to political elites, generally reflecting a view that their opinions would not be listened to. The FGDs didn't explore in more detail, though, the specific ways in which people's views could reach political decision makers.

If readers are interested in seeing the detailed findings of your survey, is it publicly available?

The Faculty of Economics and Business has recently conducted some detailed analysis of the survey results. It is now available in English and Indonesian at: http://www.iisd.org/gsi/sites/default/files/ifs_indonesia_perception.pdf.

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The Last Word



Fuel-Price Adjustment Policy in Indonesia: A political economy analysis

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Up until 2015, fuel subsidies only continued to increase. In 2009, the amount of fuel subsidy in Indonesia's budget was only IDR49 trillion and by last year it had increased more than five times to reach more than IDR246 trillion. My own projection shows that with a *do nothing policy* this amount could have climbed to IDR334 trillion in 2019.

Evidence has shown that the energy subsidy is bad for efficiency, equity, the environment, fiscal flexibility and road quality. Yet, until this year the energy subsidy has remained huge and not easy to remove—with major reforms only taking place when world oil prices have crashed. Why? The answer is clearly not on economics, but more on politics.

Similar to trade protection, energy subsidies are bad, but they exist everywhere. There is a gap between what literature has preached and what countries have practiced. In my opinion most politicians and policy-makers, including in Indonesia, understand this issue very well. Despite this understanding, many countries struggle to move from an ad hoc pricing system to an automatic price adjustment mechanism, leaving them trapped when price adjustments are needed.

A political economy analysis framework might be more relevant to explain the existence of the energy subsidy. Economic analysis stresses the long run positive effect of removing subsidies. But in the short run, the cost (including political costs) may exceed the benefit. The short-run political costs vary across the political cycle and regional politics also play some role. In urban areas, for example, the cost would be higher than in rural.

Going forward, the focus of policy design should be on how to minimize the short-run political costs of implementing fuel-price adjustments. There are at least four short-run political costs namely, (i) short-run growth impacts; (ii) one-time inflation increases; (iii) poverty and social impacts; and (iv) political cycle costs. Let me now assess those possible costs based on Indonesia's experiences.

First, on the growth impacts: ongoing adjustments to fuel prices will have short-run negative impact on growth, at least if the average shift in prices is upwards. Indonesia's experience shows that the growth impact of a major price increase would last at most one quarter. If fiscal policy is used properly, then these short-term impacts can even be avoided because compensation policies—which typically accompany adjustments—have a higher multiplier effect. In addition, regular fuel-price adjustments will end policy uncertainty, allowing domestic demand to recover over a much shorter period, i.e. two to four quarters.

Second, on poverty impacts: ongoing upward fuel-price adjustments will obviously increase the cost of living, including that of poor families. Poverty will eventually rise. However, again with a proper compensation scheme, short-term negative impacts on poverty can be avoided. If we are able to take into account all indirect impacts when designing the compensation scheme, a rise in poverty would be avoided. Indonesia's experience in 2008 shows that poverty continued to decline in 2009 despite the fuel-price adjustment conducted in 2008.

Third, on rising inflation: concerns surrounding the inflation rate have been used frequently to prevent fuel-price adjustments, including an effort to move to a more flexible price system. However, evidence seems not to support that claim. No evidence shows that a country with a fixed price system would have a lower inflation rate and, indeed, most countries which adopt a flexible price system have on average a lower inflation rate. What can we draw from this? Inflation in a particular country is determined by other more important factors than the fuel-price regime.

Fourth, on political cost: I would argue that political costs can be fully avoided if (i) the government adopts a rule-based pass-through regime that separates price adjustments from government decision making, and (ii) Adjustments take place as early as possible once there is a gap between market prices and domestic prices, since marginal (economic and political) costs rise more than proportional ones with delayed time. Political costs also need to align with the political cycle. It will be easier and politically less costly if the government can maintain its plan of regular adjustments in the early period of the administration. The closer to the election, the higher (perceived) political costs there will be.

In conclusion, we should think that setting domestic fuel prices is a program like any other development program, and it should be judged on its merits and its marginal costs and benefits. We should learn from our own experiments—good and bad. In designing adjustments, careful planning based on empirical analysis is essential, as negative impacts can be avoided with good preparations. Finally, economic theory is the easy part, but putting theory into practice is the hard part. We also have to take into account political economy and public understanding.

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