



INDONESIA ENERGY SUBSIDY BRIEFING

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

June 2015

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

- The Indonesian economy has shown resilience after a number of major changes in its fuel subsidy policies.
- Narrowing the price gap between subsidized fuel and the non-subsidized fuel has had a positive impact on the pattern of fuel consumption in Indonesia.
- Concerns continue to surround the possibility that Indonesia’s new semi-automatic fuel pricing system could be compromised by too much political intervention.
- According to PT Pertamina, the new retail price of gasoline RON 88 determined by the government were IDR 200–750 below the output of price formula calculation.

Economy Resilient after Fuel Subsidy Reforms

The Indonesian economy has shown resilience after a number of major changes in its fuel subsidy policies: a significant increase in gasoline and diesel prices in November 2014 and the switch from fixed pricing towards a semi-automatic pricing system in December 2014, which resulted in a reduction in gasoline and diesel prices—the “managed floating rate” as described by Minister of Finance Mr. Bambang Brodjonegoro (WSJ, 2015).

Indonesia’s CPI and inflation responses to fuel price change since January 2015 provides an indication how the country’s economy has reacted to the new semi-automatic fuel pricing system.

An inflation record until the first months of 2015 published by government agency Statistics Indonesia

(BPS, Badan Pusat Statistik) found that in November and December 2014, monthly inflation rates increased by 1.5 and 2.46 points respectively, making up almost half of 2014’s annual inflation.

Following January decreases in gasoline and diesel prices, this was followed by a moderate period of deflation in January and February 2015, with rates declining by 0.24 and 0.35 points respectively (BPS, 2015).

Since then, the inflation rate has been positive and growing each month by around 0.15 points.

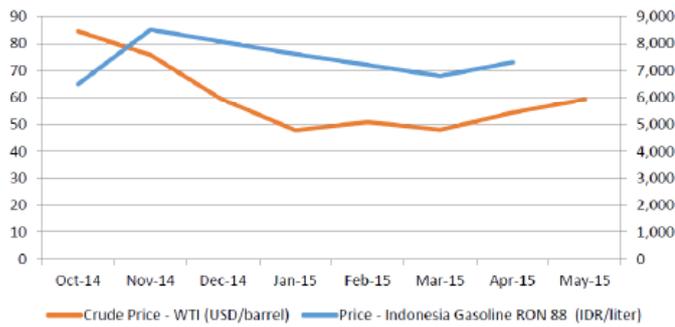
Recent growth has been attributed to increased consumption in anticipation of Ramadan and a slight recovery in global oil prices (Indonesia Investments, 2015a).

Table 1. Changes in Indonesian Fuel Prices, 2014-2015

	Pre-reform	18 Nov 2014	1 Jan 2015	19 Jan 2015	1 March 2015	28 March 2015
Prem. gasoline	6,500	8,500	7,600	6,600	6,800	7,300
Solar diesel	5,500	7,500	7,250	6,400	6,400	6,900

Source: (IISD GSI, 2015a; Kompas, 2015a; Ministry of Energy and Mineral Resources, 2015). Prices for Premium gasoline and Solar diesel have not been adjusted in April or May. The government has confirmed that no adjustments will take place in June (Jakarta Post, 2015a).

Figure 1. Changes in the Price Indonesian Gasoline RON 88 and Crude Oil (WTI)



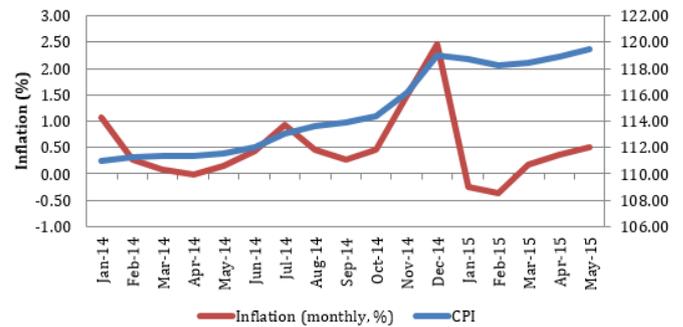
Source: (IISD GSI, 2015a; Kompas, 2015a; Ministry of Energy and Mineral Resources, 2015; Index Mundi, 2015)

Faisal Basri, a prominent economist, then the Head of Team of National Oil and Gas Management Reform, refuted the idea that the fuel pricing had been wholly handed over to a market system (Kompas, 2015b). Basri's statement was supported by an explanation from Wianda Puspongoro, Vice President of Corporate Communication of PT Pertamina, the state-owned oil and gas company.

In May 2015, Puspongoro explained that the government retained the power to intervene even with the price of non-subsidized fuel products, which according to law is supposed to be determined at the corporate level. Potential loss caused by price intervention may reach IDR 5.6 billion per day (Kompas, 2015c; Jakarta Post, 2015; Jawa Pos, 2015).

Minister of Finance, Mr. Brodjonegoro, sounded his concern over the risk of fuel subsidy revival in the future, cautioning that if the fuel subsidy comes back it will be hard to get remove it again. He also admitted that the current pricing system is still accommodating political considerations (WSJ, 2015). The decision was criticized as a "flip-flop" by opposition parties, since the government publicly announced that it has already removed the fuel subsidy, but this failed to stir much public support as a lower price increase was more popular (WSJ, 2015).

Figure 2. Changes in the Consumer Price Index and Monthly Inflation (January 2014 - May 2015)



Note: Consumer Price Index since 2014: 2012 = 100. Before: 2007 = 100.
Source: BPS, 2015

The government's decision to reform fuel subsidies was also recognized by international investors. In May 2015, Standard and Poor's improved Indonesia's BB+ rating from stable to positive, with the possibility of being raised to investment grade within 12 months. The reasons given for this change were an improved quality, effectiveness and predictability of government expenditure as a result of subsidy reforms (Jakarta Globe, 2015; Bloomberg, 2015). Fuel subsidy policy has often been cited as a detrimental factor to Indonesia's credit rating in the past few years.

The overall economy however still needs to stand the test of the global economic slump by improving performance in the other areas outside of energy subsidy policy. Jokowi's government is addressing the issue by reallocating a large sum of capital to state-owned enterprises, mainly to rejuvenate the country's infrastructure (IISD GSI, 2015b). In the latest outlooks by the Asian Development Bank (ADB), the World Bank and the International Monetary Fund, projections of economic growth in Indonesia will be slightly below the 5.7 per cent annual target cited in the Revised State Budget 2015. The ADB puts its forecast at 5.3 per cent, the IMF at 5.3 per cent and the World Bank at 5.2 percent (Indonesia Investments, 2015b).

Table 2. Changes in the Monthly Inflation Rate, January-May (2012-2015)

	2012		2013		2014*		2015	
	CPI	Inflation	CPI	Inflation	CPI	Inflation	CPI	Inflation
January	130,9	0,76	136,88	1,03	110,99 ²⁾	1,07	118.71	-0.24
February	130,96	0,05	137,91	0,75	111,28	0,26	118.28	-0.36
March	131,05	0,07	138,78	0,63	111,37	0,08	118.48	0.17
April	131,32	0,21	138,64	-0,1	111,35	-0,02	118.91	0.36
May	131,41	0,07	138,6	-0,03	111,53	0,16	119.50	0.50
November	134.76	0.07	146.04	0.12	116.14	1.5	-	-
December	135.49	0.54	146.84	0.55	119.00	2.46	-	-

* Consumer Price Index since 2014: 2012 = 100. Before 2014: 2007 = 100.

Source: BPS, 2015

Narrowing the price gap between subsidized fuel and the non-subsidized fuel has also had a positive impact on the pattern of fuel consumption in Indonesia. Mr. Muhammad Iskandar, Vice President of Fuel Marketing of PT Pertamina, explained on March 2015 that the consumption of subsidized gasoline had declined by 7,000 kiloliters per day, while there was an increase of 5,000 kiloliters per day of non-subsidized fuel with higher performance octane ratings. He added that the remaining 2,000 kiloliters per day had been supplied by other fuel retailers in Indonesia such as Shell and Total (Liputan 6, 2015a).

Backsliding Risk

Concerns continue to surround the possibility that Indonesia's new semi-automatic fuel pricing system could be compromised by too much political intervention. In late March 2015, the government adjusted the fuel price to a level that was considered by some to be slightly below the level that should be determined by the new formula.

The new Indonesian fuel pricing system for special designated fuel (fuel products with fiscal incentives for distribution cost) according to the Presidential Regulation No. 191/2014 Article 14, is based on the combined factors of production costs, distribution costs and taxes, and still needs approval by the Minister of Energy and Mineral Resources before it becomes effective.

Table 3. Disparity between Market Price and Government Price in Indonesia (2015)

Product	Market Price	Government Price	Gap
Price from 1 March 2015 (based on MOPS and exchange rate during 25 Jan-24 Feb)			
Premium for Java, Madura and Bali	7,200	6,900	-300
Premium for other areas	7,000	6,800	-200
Diesel fuel after Rp1,000/liter subsidy	6,350	6,400	+50
Price from 8 March 2015 (based on MOPS and exchange rate during 25 Feb-24 March)			
Premium for Java, Madura and Bali	8,150	7,400	-750
Premium for other areas	7,900	7,300	-600
Diesel fuel after Rp1,000/liter subsidy	6,850	6,900	+50

All figures above are shown in Rupees per liter.

Source: PT Pertamina, cited in (Jakarta Post, 2015b)

According to PT Pertamina, using the formula given to determine the fuel price, the new retail price of gasoline RON 88 on 1 March 2015 and 28 March 2015 determined by the government were IDR 200–750 below the output of price formula calculation.

In addition to that, since there is no policy set to compensate the disparity between pricing formula and government price, PT Pertamina is forced to sustain the loss for that price disparity (Jakarta Post, 2015b).

Saleh Abdurrahman, Head of Center of Communication of the Ministry of Energy and Mineral Resources, explained that the government's decision was taken in order to maintain national economy stability (Tribun News, 2015; Liputan 6, 2015b).

This new development unveiled a critical weakness in Indonesia's new pricing system. Indonesia needs to tweak its fuel pricing system, which originally was aimed to consolidate the needs to have a healthy economic continuation and the ideal to maintain a fair access to fuel for its people. But most importantly, there is an urgency to evaluate the scope government's interference in determining fuel price.

Oil and Gas Sector Management Reform

Indonesia's ongoing fuel subsidy reforms are being accompanied by efforts to improve the efficiency of its oil and gas sector management in general. Following changes in the leadership of PT Pertamina, the government has gone further by dissolving the troubled subsidiary Pertamina Energy Trading Ltd. (Petal), which has been serving as the intermediary in oil imports. The CEO of PT Pertamina, Mr. Dwi Sutjipto, claimed that the decision to shorten the trading chain has created US\$ 22 million (IDR 289 billion) benefit to PT Pertamina (Tempo, 2015).

Such efforts cannot be separated from the work conducted by the Team of National Oil and Gas Management Reform, led by prominent economist Dr. Faisal Basri. The team has delivered various reform recommendations to the new administration. Among others are recommendations to separate the "operation" function and the "regulatory" or "supervisory" function from PT Pertamina, through a future oil and gas regulatory body; switching to a higher quality gasoline and diesel supply; and the increase of national refinery and storage capacity. The tenure of Dr. Basri's team expired on 15 May 2015 and was not extended (Katadata, 2015).

The recommendations from this team are likely to influence the formulation of Indonesia's new oil and gas regulation and further reform in the oil and gas sector.

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