Fiscal Policy Office – Ministry of Finance

Republic of Indonesia

Fiscal Policy related to Fuel Subsidy and Climate Change Program In Indonesia

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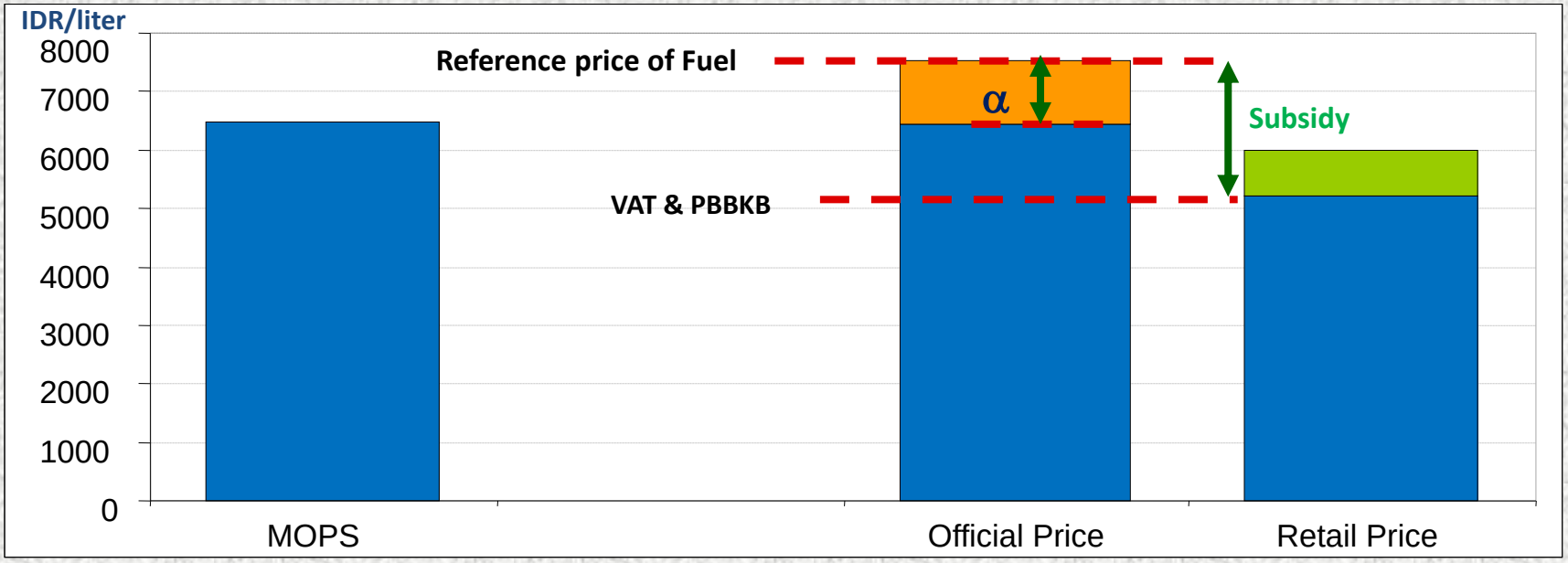
Expert Workshop on Estimating Support to Fossil Fuels, in OECD, Paris
18 - 19 November 2010

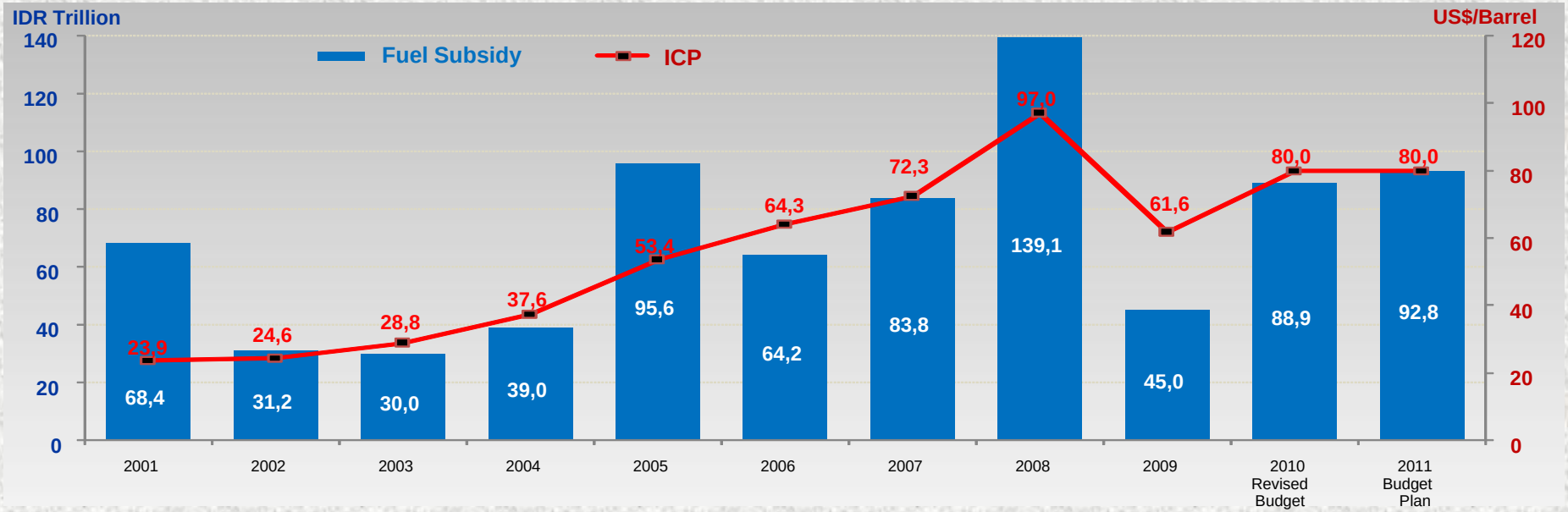
Indonesia : Fuel Subsidy Formula

Fuel Subsidy :
= [Reference Price of Fuel - (Retail Fuel Prices - Tax)] x Fuel Volume

- **Retail fuel price** is the retail selling price per liter of fuel in domestic area.
- **Tax** is a Value Added Tax (10%) and Motor Vehicle Fuel Tax (5%).
- **Reference price of fuel** is calculated based on the MOPS price plus distribution costs and margins.
- Reference price of fuel = **MOPS + α**
  - ✓ **α** is the distribution cost + margin
  - ✓ **MOPS** (Mid Oil Platt's Singapore) is the price on the stock sale and purchase transactions on the Singapore oil



State Budget And Fuel Subsidy Policy



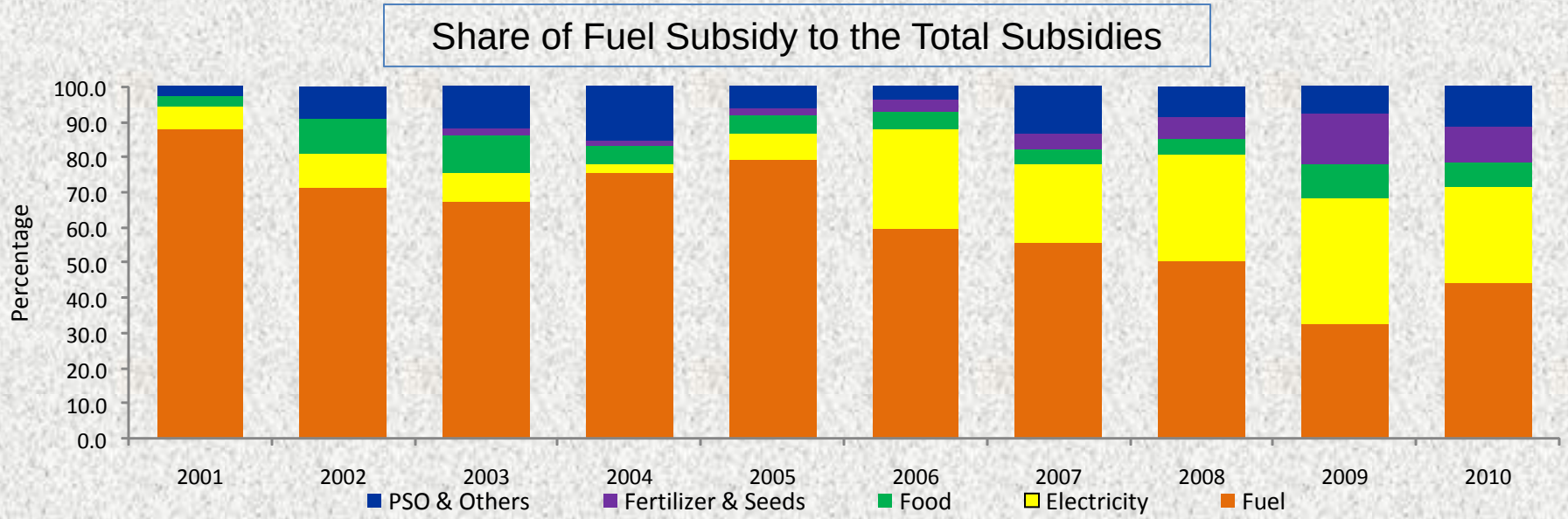
Policy Implementation:

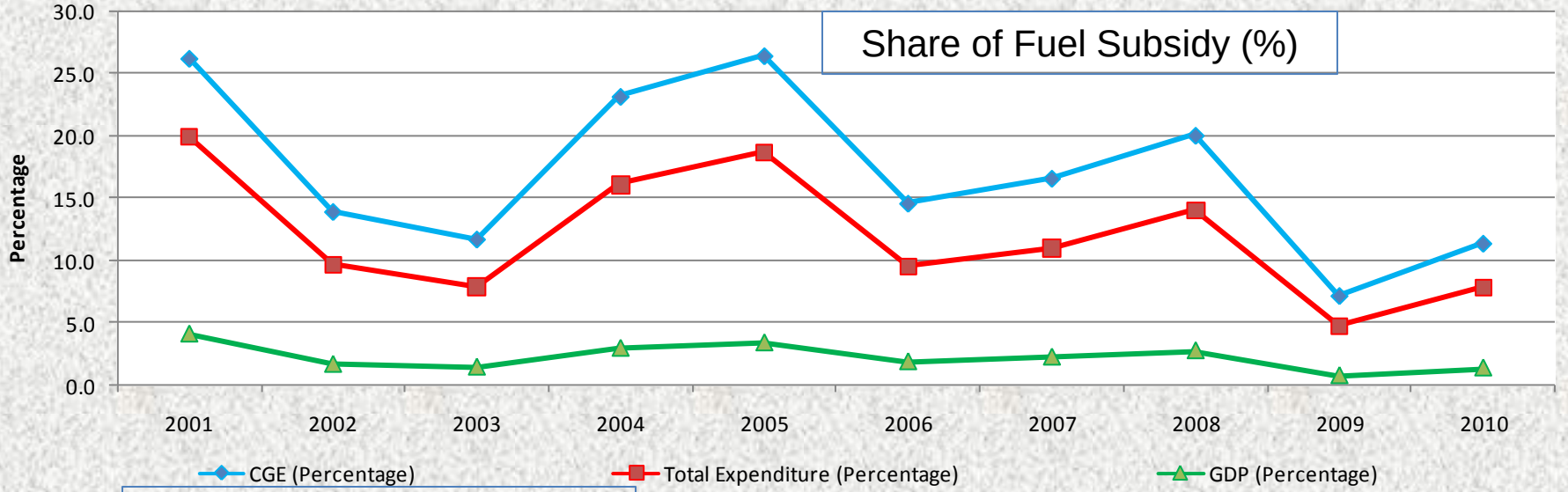
- Reducing subsidized fuel in 2005 from 5 to 3 commodities by removing Diesel Oil for industry and Fuel Oil from subsidy.
- Conversion program (kerosene to LPG)
- Energy diversification (Gas for Bus and public transportation)
- Retail fuel price adjustment
- Improving the subsidized fuel distribution mechanism to enable the subsidy to be more targeted

Challenges :

- Ensuring availability of gas supply for conversion of kerosene to LPG achieved
- Increased development of gas fuel stations and filling stations and transport of bulk of LPG
- The vulnerable of oil price
- Community dependence on fossil fuel subsidies is still high
- Targeted fuel subsidies

Fuel Subsidy Compare to Other Subsidies, Central Government Expenditure, Total Expenditure, and GDP





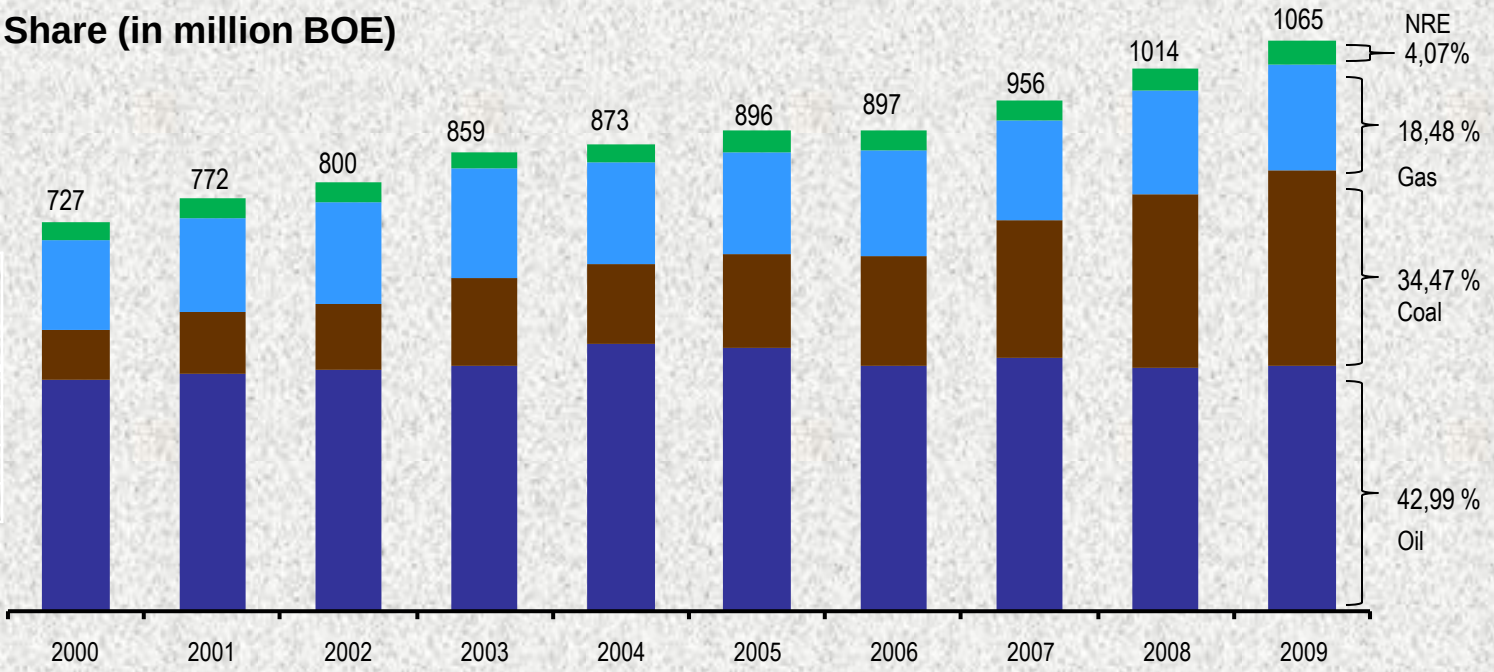
CGE = Central Government Expenditure

GROWTH OF SHARE AND FOSSIL FUEL SUBSIDY, 2000 – 2009

A. Increase of Total Share (in million BOE)

Average increase in last 10 years:

1.Oil	:	0,52 %/year
2.Coal	:	13,70 %/year
3.Gas	:	1,81 %/year
4.Total	:	4,33 %/year



B. Increase of Fossil Fuel Subsidy (in billion IDR)

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
1. Electricity	3.93	4.30	4.10	3.36	3.31	10.65	33.90	37.48	78.58	53.72
2. Electricity using Fossil Fuel	3.30	3.55	3.49	2.92	2.86	9.20	29.75	32.63	68.16	46.14
3. Fossil Fuel Subsidy	55.64	63.26	31.75	30.04	59.18	103.35	64.21	83.79	139.03	45.04
4. LPG Subsidy	0	0	0	0	0	0	0	0.15	3.84	7.78
Total Fossil Subsidy	**58.94**	**66.81**	**35.24**	**32.96**	**62.04**	**112.55**	**93.96**	**116.57**	**211.03**	**98.96** *)

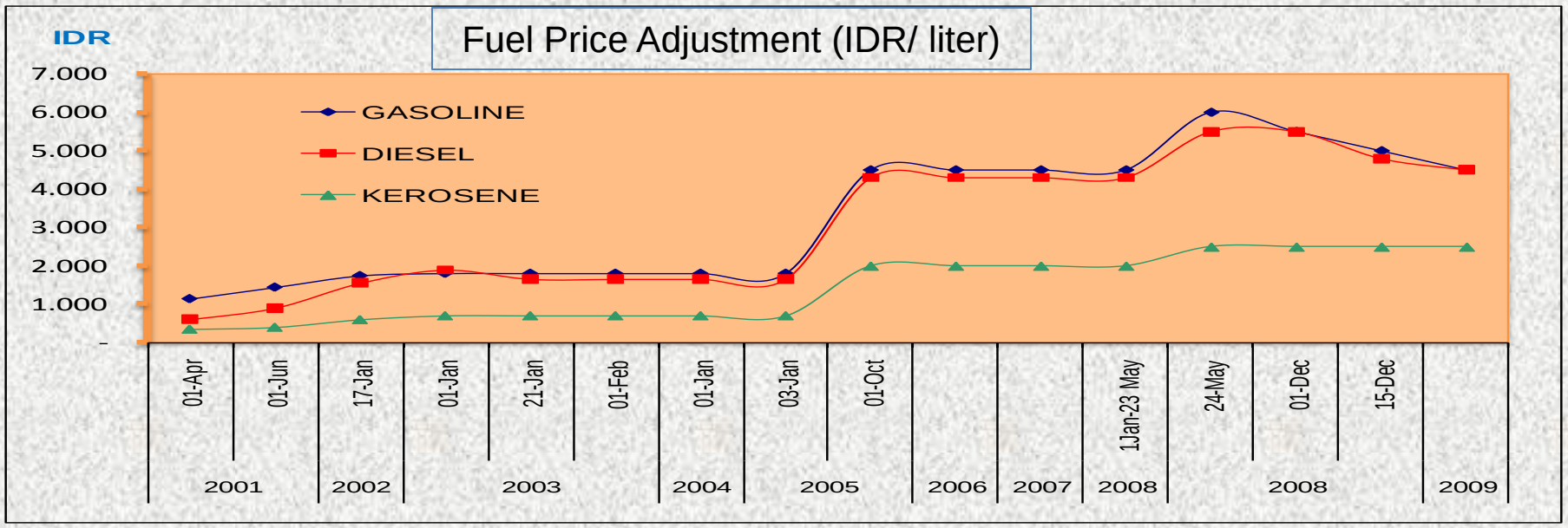
*) = 2+3+4

Source : Ministry of Energy and Mineral Resources

Commodities and Fuel Domestic Prices, 2003-2010

Year	2003	2004	2005		2006	2007	2008	2009	2010
	1Jan-31Des	1Jan-31Des	1Jan-1Oct	1Oct-31Des	1Jan-31Des	1Jan-31Des	1Jan-31Des	1Jan-31Des	1Jan-31Des
GASOLINE	S	S	S	S	S	S	S	S	S
DIESEL	S	S	S	S	S	S	S	S	S
KEROSENE	S	S	S	S	S	S	S	S	S
DIESEL OIL FOR INDUSTRY	S	S	S	NS	NS	NS	NS	NS	NS
FUEL OIL	S	S	S	NS	NS	NS	NS	NS	NS

Note : S = Subsidy, NS = Non Subsidy



Roadmap of Kerosene to LPG Conversion Program

Up to 2007

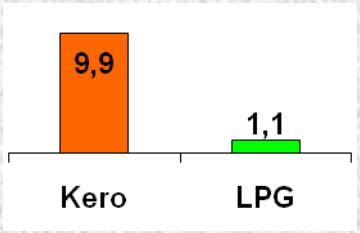
- Kerosene used by majority households in Indonesia (9.9 million KL) and subsidized by Government (more than Rp 37 Trillion /year)
- LPG only used by 10% of households and more expensive than subsidized kerosene.

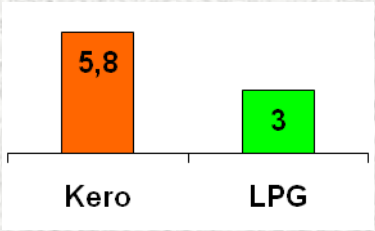
2007 - 2009

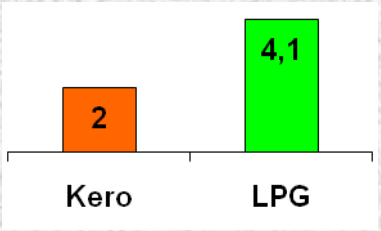
- Government program : distribute 42 millions of conversion package to targeted households.
- Removing 2,069 million KL of kerosene and distribution of 19 million conversion package up to 2008.
- Removing 4,1 million KL of kerosene and distribution of 23 million conversion package up to 2009.T

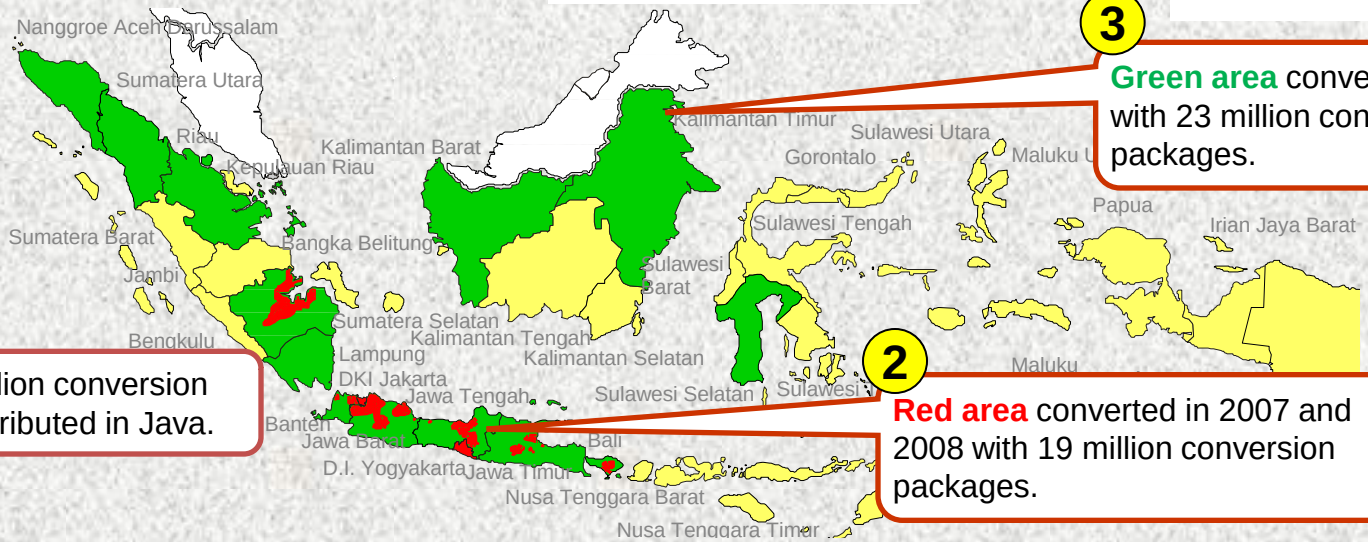
2010 forward…

- LPG will become major energy with estimated volume of 4.1 million tonnes/year.
- 6 million KL of kerosene will remove and only maintain 2 million KL.







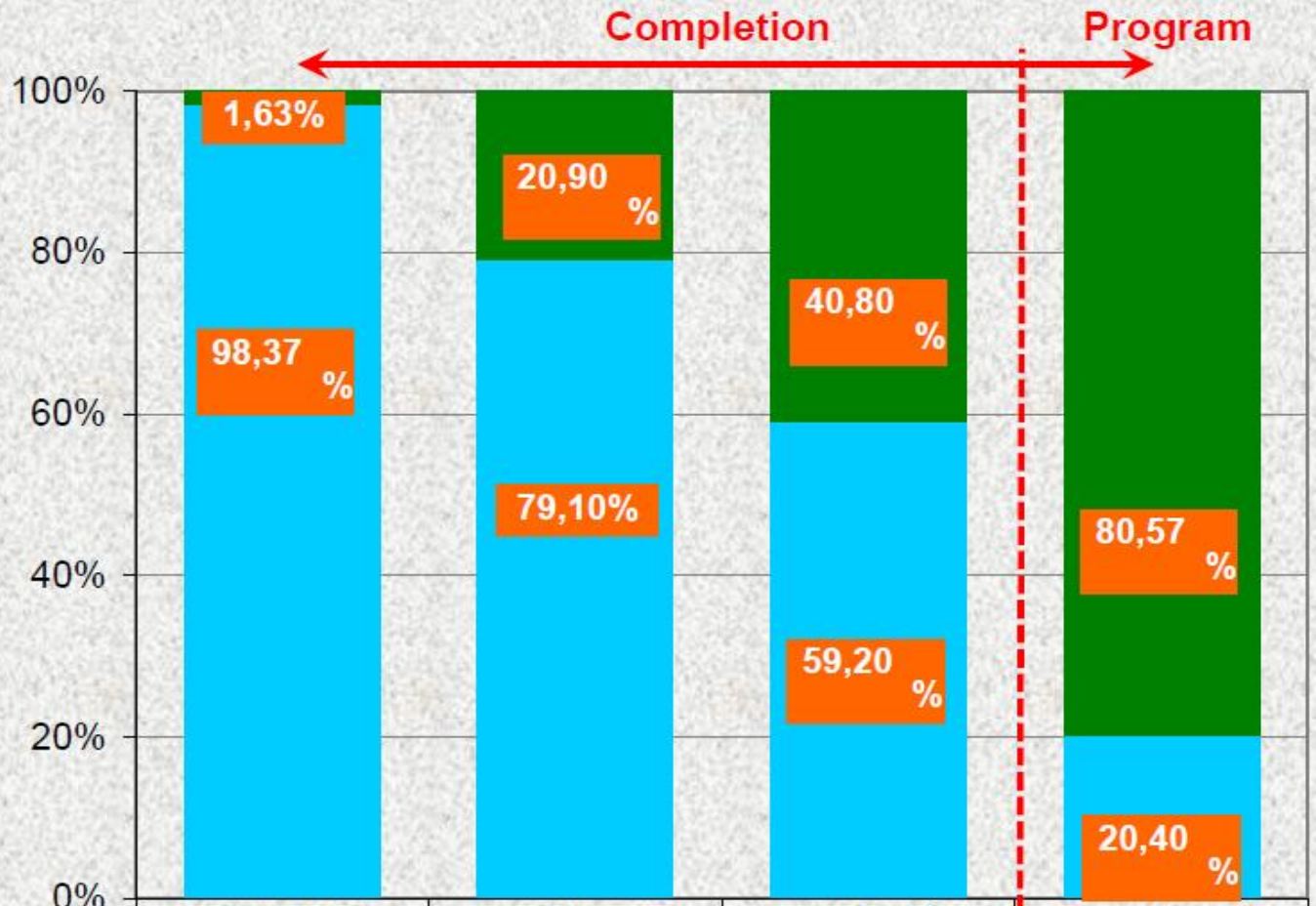


1 In 2007, 4 million conversion packages distributed in Java.

2 **Red area** converted in 2007 and 2008 with 19 million conversion packages.

3 **Green area** converted in 2009 with 23 million conversion packages.

Achievement of Kerosene to LPG Conversion Program



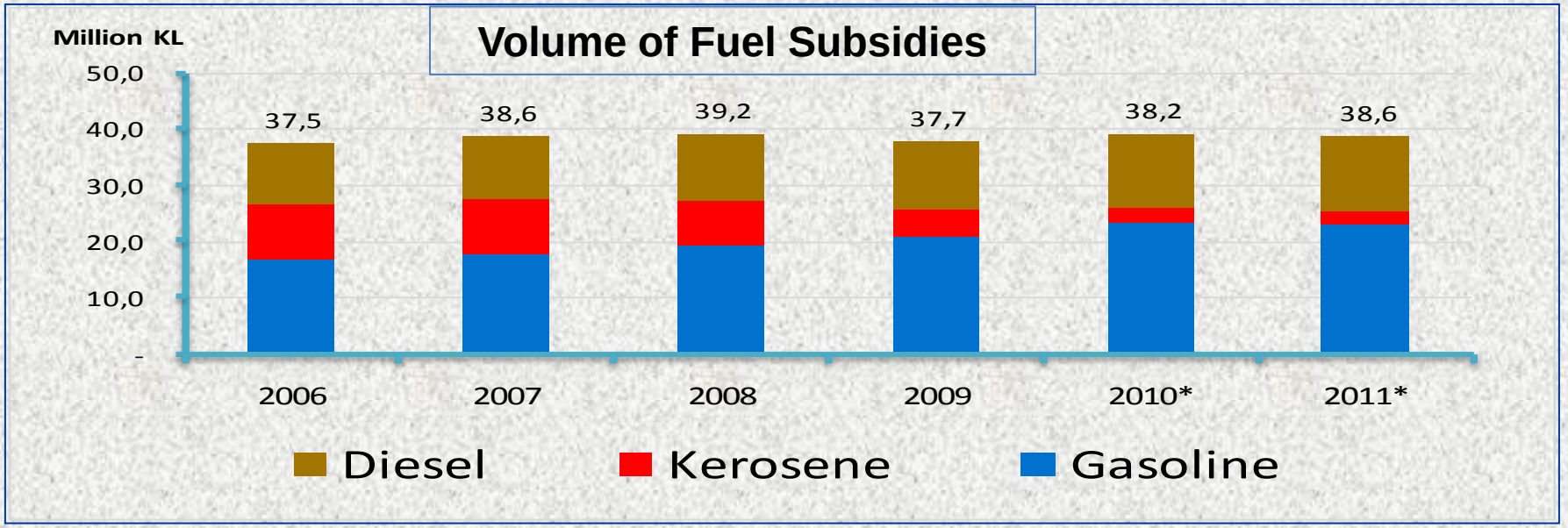
	2007	2008	2009 *)	2010
LPG (kL eq. to kerosene)	163,182	2,069,536	4,000,000	7,900,000
Kerosene (kL)	9,851,812	7,832,280	5,804,911	2,000,000

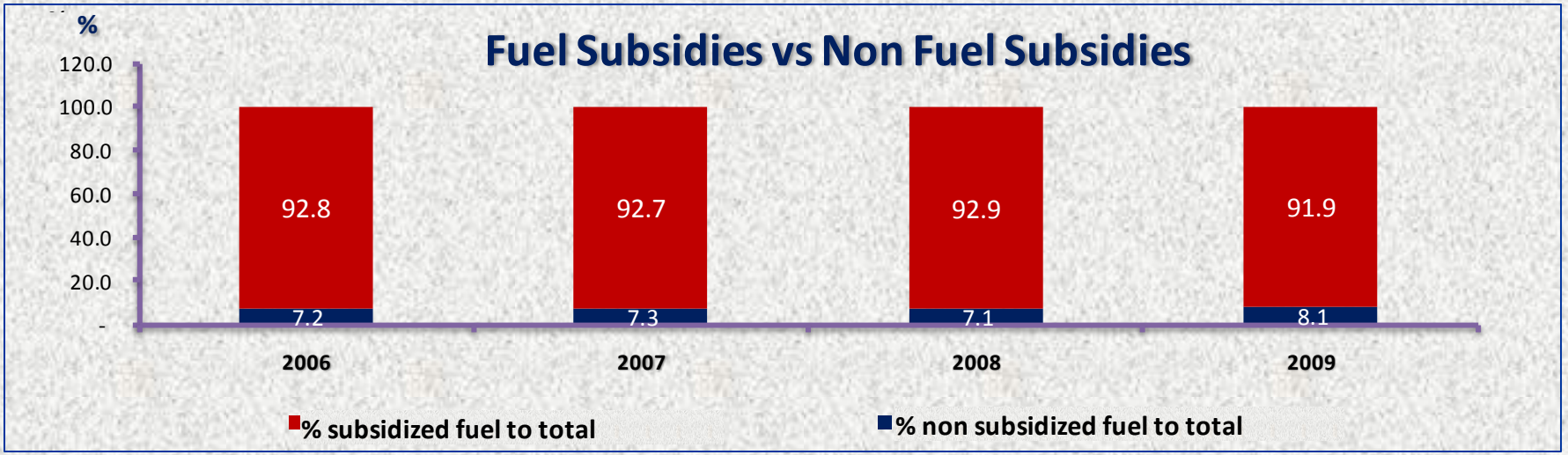
Note:

In 2010, subsidized kerosene remained in the market used only for household in remote area, small business and house lighting.

*) **Unaudit**

Volume of Fuel Subsidies, 2006 - 2011

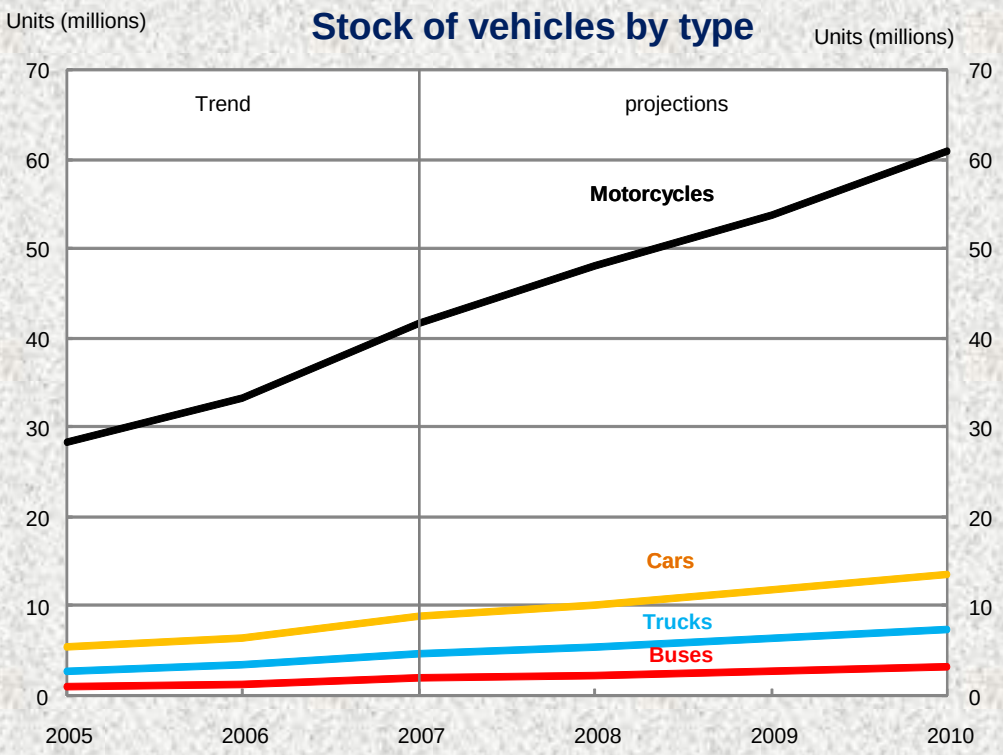




Challenge : Stock of vehicles is growing quickly, driven by motorcycles

- Stock of vehicles is growing quickly, in line with strong economic growth and rising incomes, driven by motorcycles whose number could reach an estimated 60 million in 2010 – roughly 1 per household – up from 42 million in 2007
  - Motorcycle sales in 2010 have averaged almost 600,000 units per month, which would add 7 million new units if trend maintained

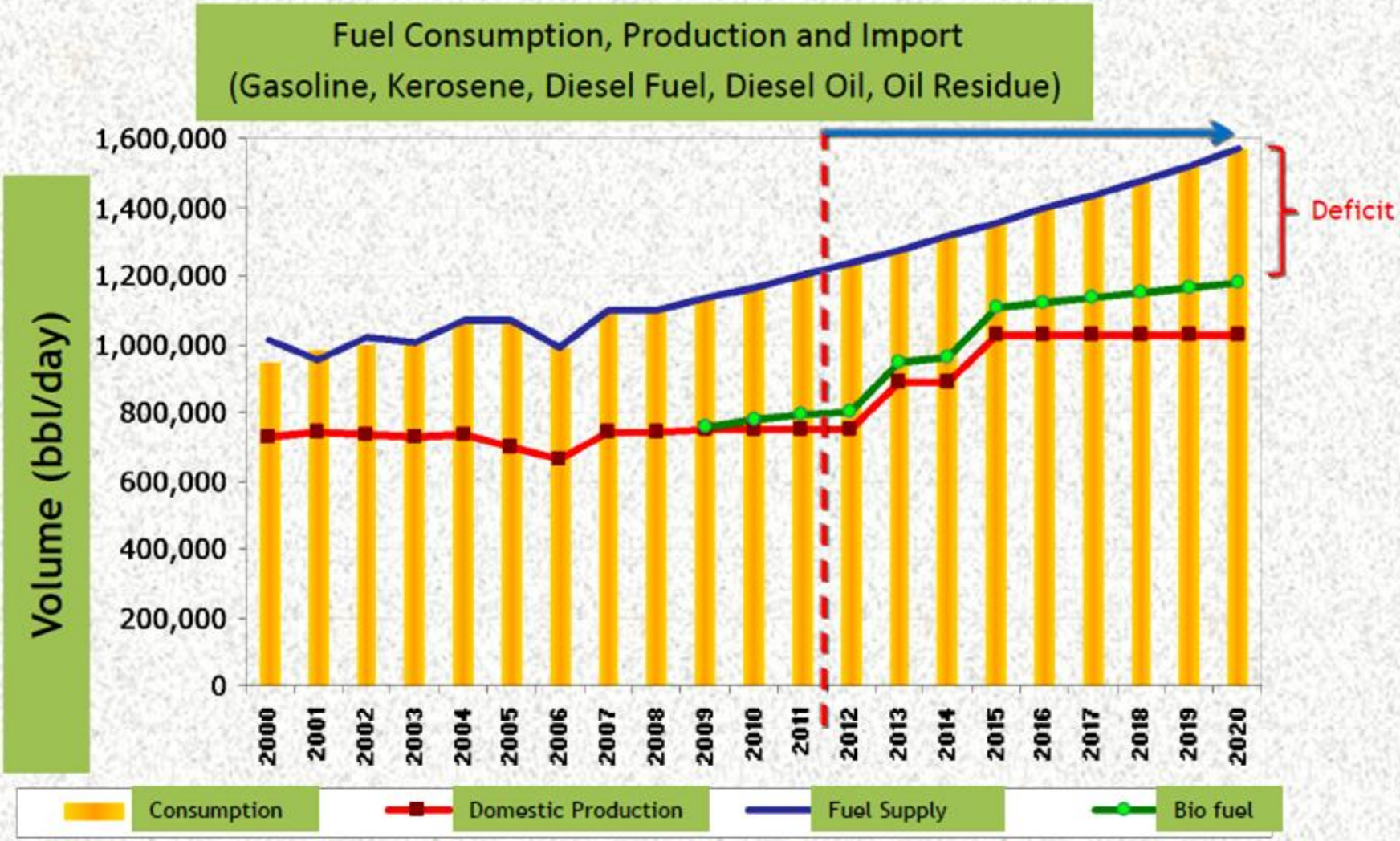
- **Stock of cars, trucks and buses grew even faster between 2005-2007, almost 30% per year, albeit off a lower base**
  - **Number of cars could reach almost 14 million in 2010, followed by trucks (8 Mn) and buses (3.5 Mn)**



Source: Statistics Indonesia for 2005-2007, BPS. 2008 onwards are WB staff projections based on trends & monthly motorcycle sales.

Source : World Bank study

FUEL SUPPLY – DEMAND, in the long term



Note:

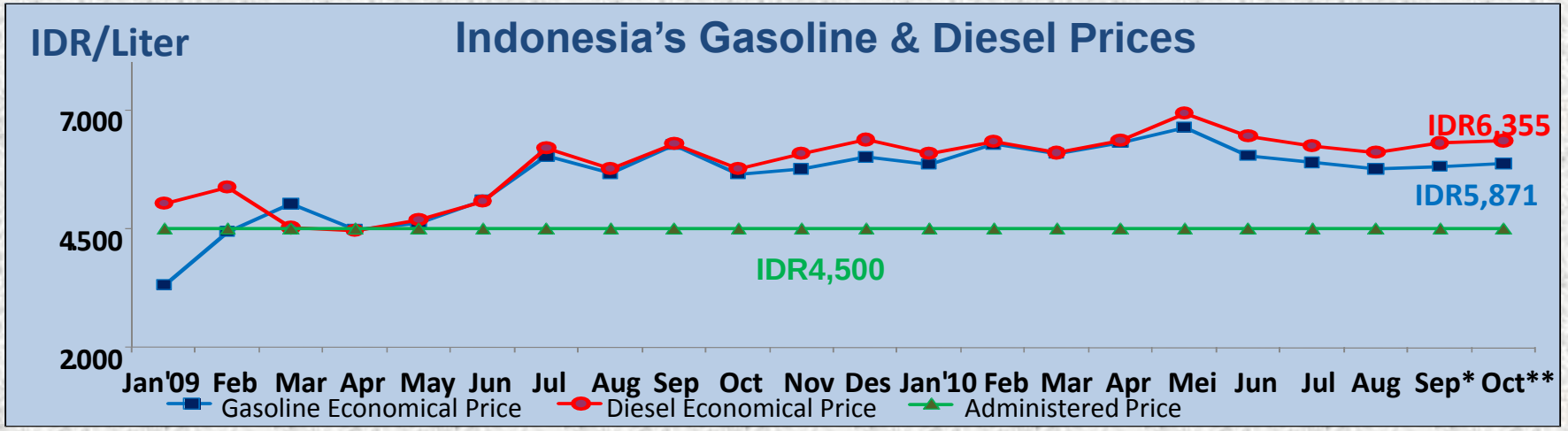
- Fuel Supply = Domestic Production + Import

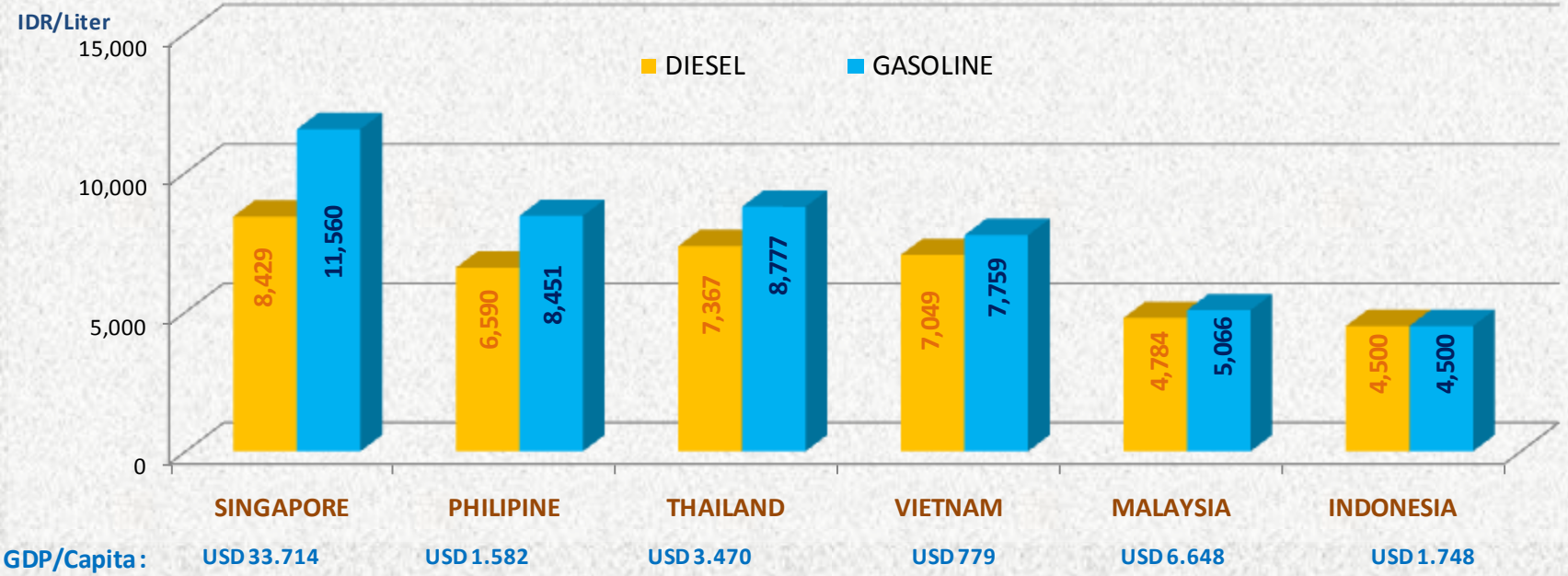
Source : Ministry of Energy and Mineral Resources

Fuel Subsidy Policy, 2010-2011

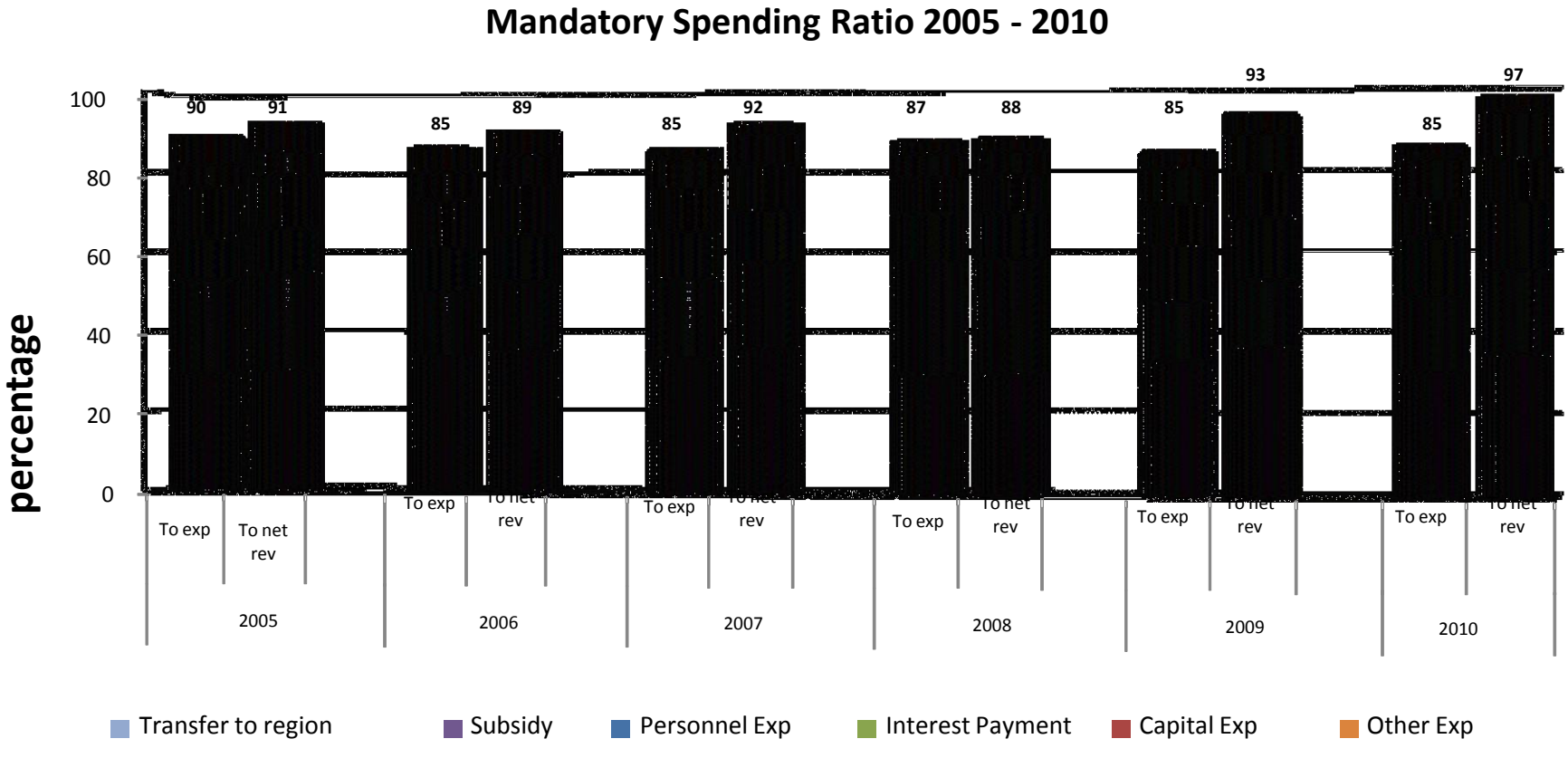
- Limiting subsidized fuel users to households, micro businesses, fishery businesses, public transportation and public services
- Reducing the consumption of fossil fuels by introducing new types of bio-fuel
- Enhancing the development of alternative energy,
- Continuing conversion program of kerosene to LPG 3 kg
- To enhance monitoring of subsidized fuel distribution and law enforcement for misuse

Indonesian Fuel Price : Compare to Other Countries' Fuel Price





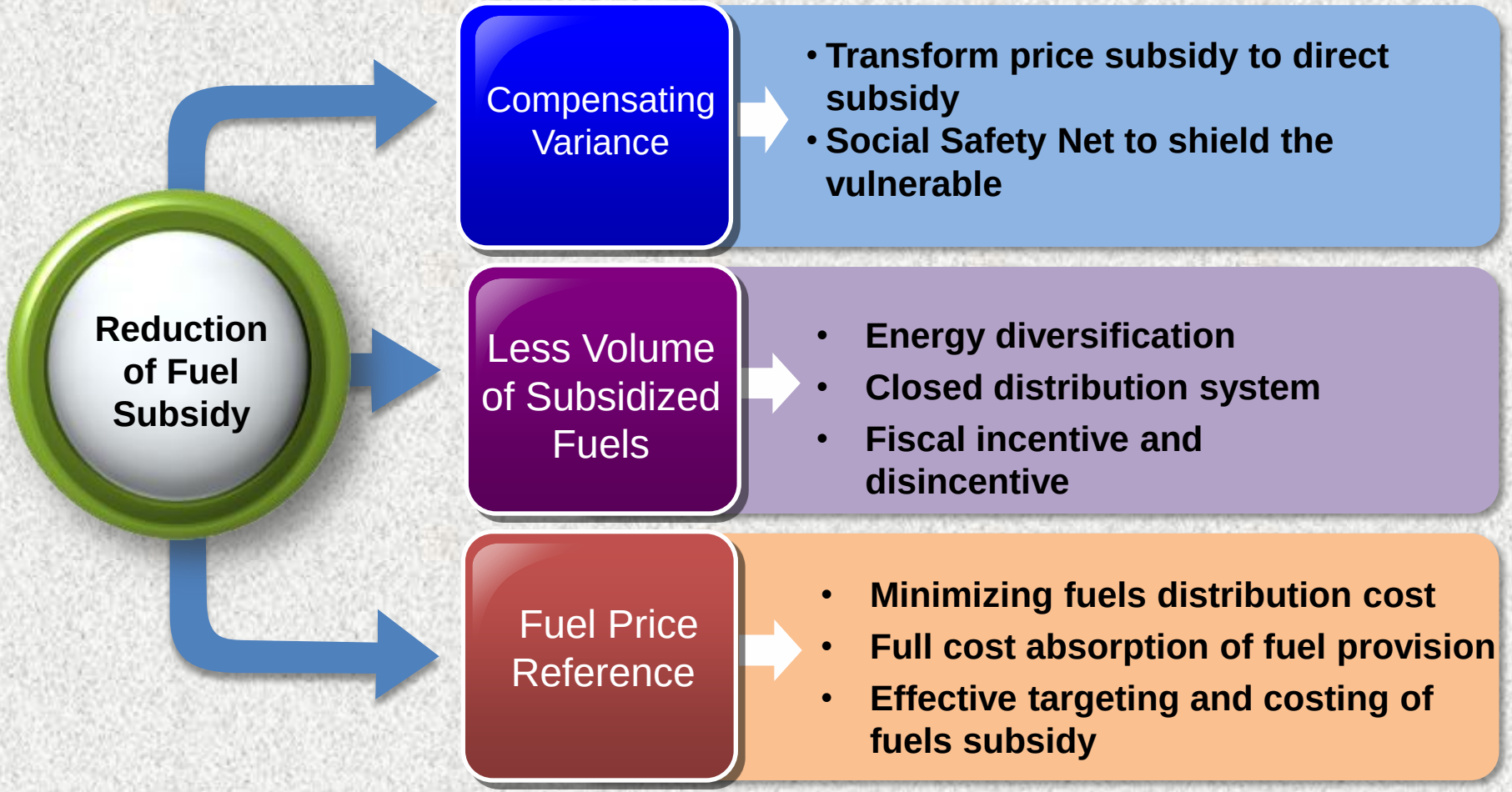
Challenge : phasing out fuel subsidy will be a tool to improve Fiscal Space ?



Fiscal space was limited, 2005-2010 :

- In term of revenue : fiscal space was around 85% - 97%
- In term of expenditure : fiscal space was around 85% - 91%

Mid-Term Development Plan Fuel Subsidy Phase-out Strategy



Road map of Fuel Subsidy Targeted

Fuel User	Stage V			Stage VI		Stage VII		Stage VIII			
	Sep ' 05	Okt ' 05	Apr ' 06	2007	2008	2009	2010	2011	2012	2013	2014
Kerosene											
Household	S	S	S	S	S	S/Closed 1		S/Closed 2			
Small Business	S	S	S	S	S	S/Closed 1		S/Closed 2			
Industry	NS	NS	NS	NS	NS	NS	NS	NS	NS	NS	NS
Gasoline											
Transportation	S	S	S	S	S	S/Closed 1		S/Closed 2			
Fishery	NS	NS	S	S	S	S/Closed 1		S/Closed 2			
Industry	NS	NS	NS	NS	NS	NS	NS	NS	NS	NS	NS
Diesel											
Transportation	S	S	S	S	S	S/Closed 1		S/Closed 2			
Fishery	S	S	S	S	S	S/Closed 1		S/Closed 2			
Industry	NS	NS	NS	NS	NS	NS	NS	NS	NS	NS	NS
Diesel Oil for Sea Freight Industry											
Sea Freight Industry	NS	NS	NS	NS	NS	NS	NS	NS	NS	NS	NS
Fuel Oil for Sea Freight Industry											
Sea Freight Industry	NS	NS	NS	NS	NS	NS	NS	NS	NS	NS	NS

S = Subsidy

NS = Non Subsidy

S/closed 1 : Test arrangement for closed distribution system (2009-2010)

S/closed 2 : The trial closed distribution system in gradually (2011-2014)

Source : Ministry of Energy and Mineral Resources

MANDATORY for BIODIESEL UTILIZATION (minimum %)

SECTOR	Oct - Dec 2008	January 2009	January 2010	January 2015**	January 2020**	January 2025**	REMARK
PSO Transportation	1 % (existing)	1 %	2,5 %	5 %	10 %	20 %	* Based on Needs
Non PSO Transportation	-	1 %	3 %	7 %	10 %	20 %	
Industry and Commercial	2,5 %	2,5 %	5 %	10 %	15 %	20 %	* Based on Needs
Power Plant	0,1 %	0,25 %	1 %	10 %	15 %	20 %	* Based on Needs

Mandatory for Bio ethanol Utilization (minimum %)

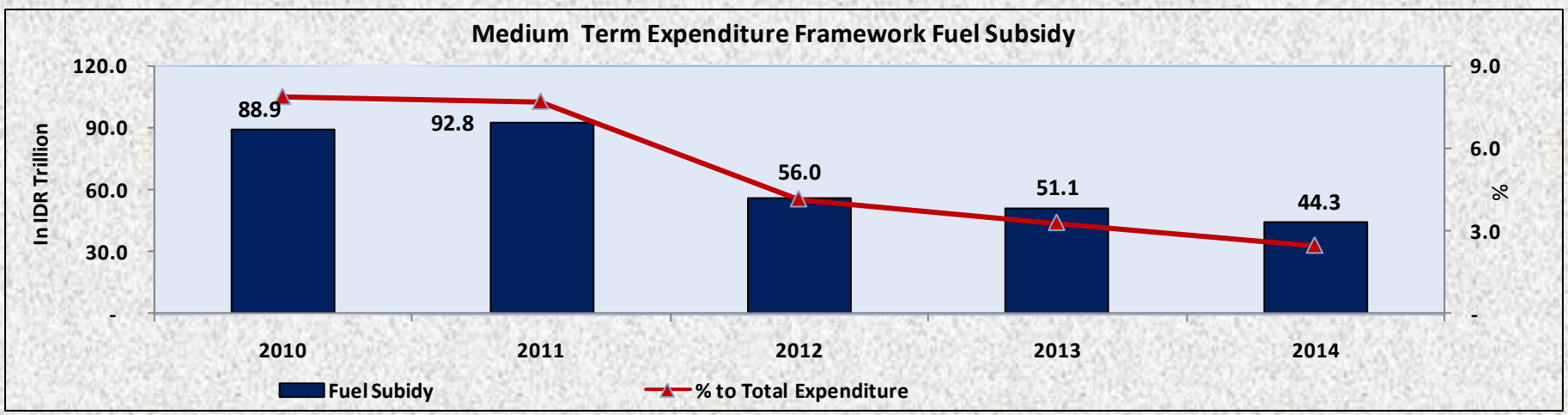
SECTOR	Oct - Dec 2008	January 2009	January 2010	January 2015**	January 2020**	January 2025**	REMARK
PSO Transportation	3 % (existing)	1 %	3 %	5 %	10 %	15 %	* Based on Needs
Non PSO Transportation	5 % (existing)	5 %	7 %	10 %	12 %	15 %	* Based on Needs
Industry and Commercial	-	5 %	7 %	10 %	12 %	15 %	* Based on Needs

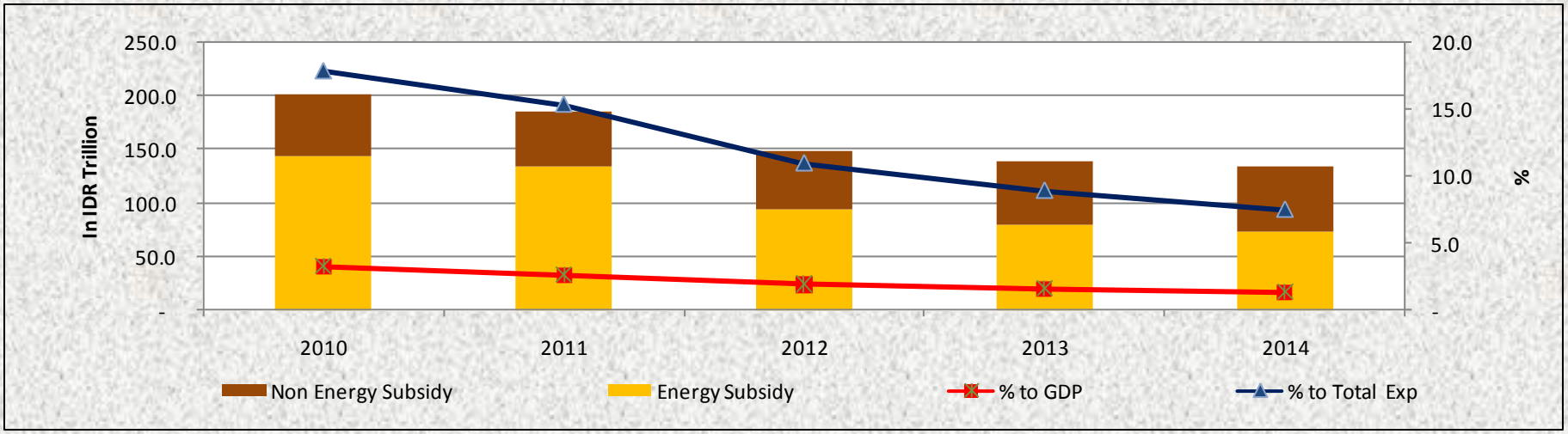
Mandatory for Pure Plantation Oil Utilization (minimum %)

SECTOR		Oct - Dec 2008	January 2009	January 2010	January 2015**	January 2020 **	January 2025 **	REMARK
Industry and Transportation (Low & medium speed engine)	Industry	-	-	1 %	3 %	5 %	10 %	
	Marine	-	-	1 %	3 %	5 %	10 %	
Power Plant		-	0,25 %	1 %	5 %	7 %	10 %	* Based on Needs

Source : Ministry of Energy and Mineral Resources

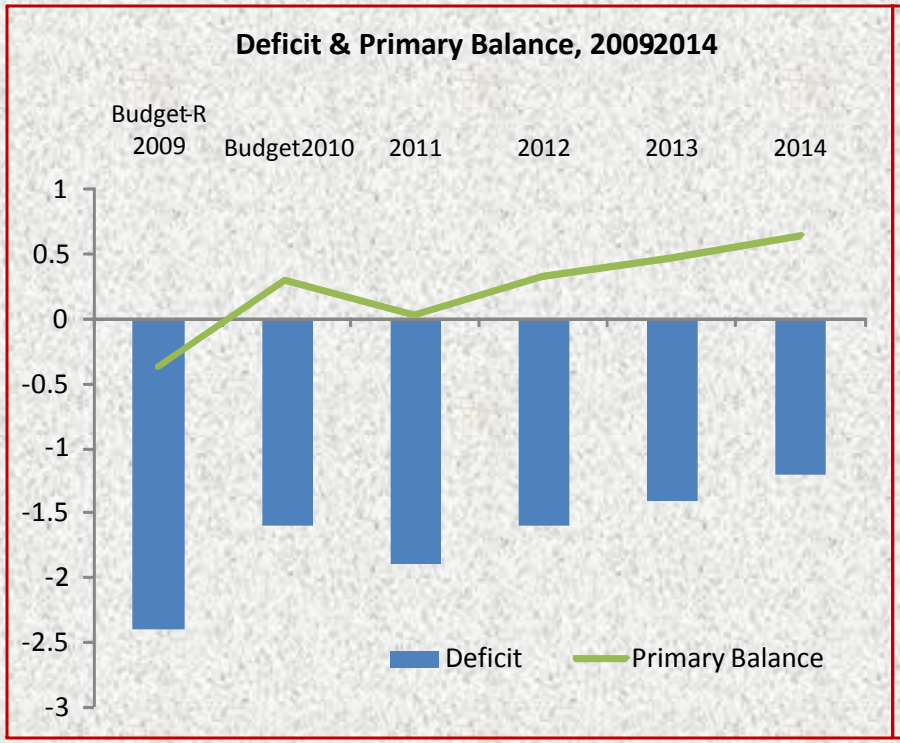
Subsidies Policies 2009-2014

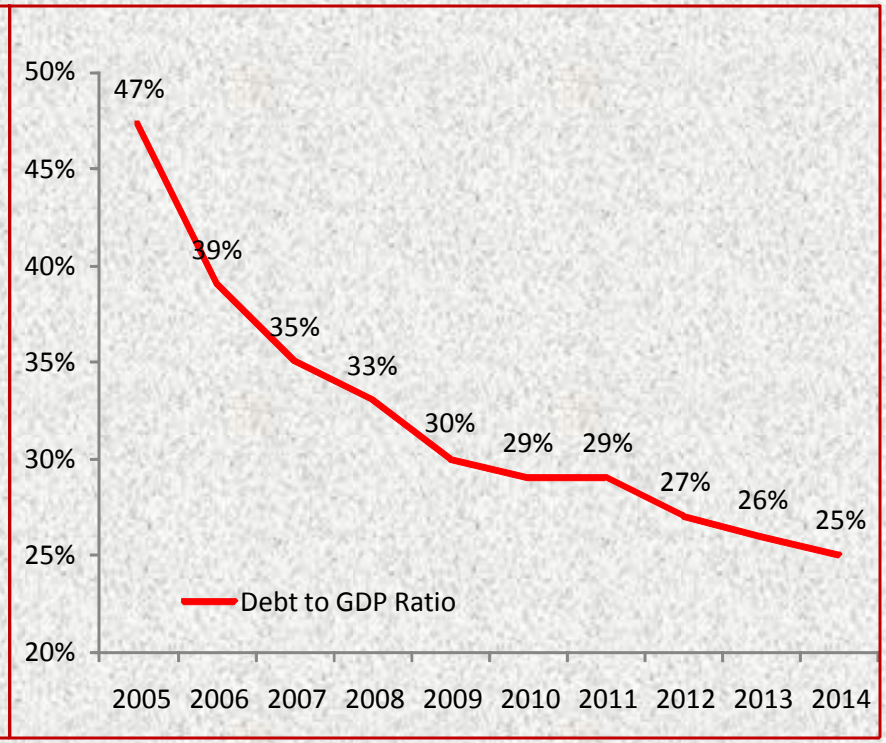




- Controlling subsidised fuel consumption by closed distribution and regulation improvement
- Developing alternatives energies (coal, gas, geothermal)
- Electricity tariff adjustment

Energy Subsidy Policies will Support Fiscal Sustainability in the Medium Term





- ✓Budget deficit is consolidated into 1% in 2014 and primary balance keeps increase
- ✓Financing Policies:
  - Lowering debt GDP ratio to maintain fiscal sustainability
  - Debt instruments diversification to minimize cost and risk
  - Lowering government debt ratio to GDP consistently
  - Improving transparency and accountability on debt management

Challenges

- Phase out fuel Subsidy will have a broad impact, such as :
  - ✓ Inflation
  - ✓ Poverty and Unemployment
  - ✓ Competitiveness of Industry
  - ✓ Economic growth
  - ✓ Fiscal sustainability
  - ✓ Energy sustainability
- How to design a comprehensive of phase out fuel subsidy, include its broad impact
- Followed up by compensation policies to society and industry to minimize its negative impact
- In developing countries (i.e. Indonesia, Malaysia, India), implementation of phase out fuel subsidy policy will be affected by political decision.

Fiscal Incentive for Climate Change

1. Minister of Finance (MoF) Regulation on Taxation and Customs Facility for Renewable Energy Sources Utilization Activities;
2. MoF Regulation on VAT burden by the Government on the Import of Goods for Geothermal Activities
4. MoF Regulation on VAT burden by the Government for Bio Fuel
5. Price subsidy for Bio Fuel
6. MoF Regulation on VAT burden by the Government for mitigation and adaptation climate change
7. Revolving fund for geothermal exploration (IDR1 trillion in 2011)

(Billion IDR)

Tax Subsidies	2008		2009		2010		2011
	Revised Budget	Real.	Revised Budget	Real.	Budget	Revised Budget	Proposed Budget
a. Income Tax on geothermal energy commodities	500,0	500,0	800,0	800,0	624,3	624,3	1.000,0
b. VAT for adaptation and mitigation climate change	-	-	-	-	-	900,0	500,0
Total	**500,0**	**500,0**	**800,0**	**800,0**	**624,3**	**1.524,3**	**1.500,0**

Transfer to Region for Climate Change Programs

Climate Change Financing for Regions

- To support climate change-adaptation and mitigation in the region, the Government attempt to fund activities related to climate change trough the Special Allocation Fund (DAK). There are two sectors related to climate change activities that are DAK Forestry and DAK Environment

(Billion IDR)

Sector/Year	2006	2007	2008	2009	2010
Environment	217.5	351.6	351.6	351.6	351.6
Forestry			100.0	100.0	100.0

DAK Forestry

Improve watershed function, in order to maintain and increase the carrying capacity of forest resources, land and water, and to support climate change mitigation. The policy is sated by preventing more damage of forest resources, soil water that is in the watershed trough implementing land rehabilitation, forest management in the scope of the district / city / province affairs, including the development of village nurseries and peat land conservation.

DAK Environment

Support the national priority targets of pollution loads reduction and alleviation of 50 percent pollution level by the implementation of water pollution control, air and solid waste in the region and to strengthen the implementation of regional environmental field of Minimum Service Standard (SPM).

Thank You