

Highlights of the week



A tailored approach for defense budget needed

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High absenteeism Jokowi's worst nightmare

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Poor policy design and tax regulation cancellation

The government abruptly cancelled the implementation of Finance Ministerial Regulation No. 210/2018 on e-commerce taxation after it was slated to kick off on April 1, rising questions over the soundness of the design of this policy. We suspect the cancellation was because of poor regulation design, in which it neglects the fact that social media platforms remain the most used platforms for e-commerce transaction instead of online marketplace.



Financial woes shackle Krakatau Steel

State-owned steel producer Krakatau Steel has been leading local steel producers in their two-front fights against the low-quality steel produced domestically and cheap steel imports, dumped mainly from China. As the fights are escalating, Krakatau Steel now faces its own internal problem, mounting debt.

POLITICS

Debating defense budget: A tailored approach needed

One of the interesting issues highlighted during the fourth presidential debate was Indonesia's defense budget, or lack thereof. The two presidential candidates presented contrasting ideas: One argued that it should be increased, while the other argued that the current budget was sufficient. Defense, however, is a peculiar matter and each country must tailor its respective defense measures according to its own security needs. Nevertheless, the ideas proposed by the candidates still lack a thorough grasp of Indonesia's unique needs and objectives.

Takeaways:

- Jokowi's approach to defense and security is somewhat human-centered, in that it focuses on securing citizens by creating "freedom from want" and "freedom from fear". In this way, Jokowi highlights the importance of diplomacy, infrastructure and human development instead of increasing the defense budget.
- In contrast, Prabowo's approach to defense and security is very traditional and state-centered, in which foreign invasion remains the biggest security threat against territorial sovereignty. The country's military capabilities, thus, are considered to be very crucial; hence the proposal to increase the defense budget.
- In debating the defense budget, it should be tailored in accordance to a country's strategic objectives and needs. Other countries' defense budgets, thus, may not be the most relevant parameter to deliberate one's defense measures.
- Should the defense budget increase, budget allocation should address not only problems surrounding weaponry, but also military strategies, human resources and soldiers' welfare. Defense measures should also contemplate risks posed by contemporary warfare, not only conventional warfare.

Background: Indonesia's defense budget became one of the issues fiercely debated during the fourth presidential debate on March 30. The views of the presidential candidates, Joko "Jokowi" Widodo and Prabowo Subianto, could not be more opposite. Prabowo first brought up the issue of the defense budget, which he said was still far from ideal. A former Army general himself, Prabowo repeatedly emphasized Indonesia's unpreparedness for war and foreign invasion, which according to him could occur at any time.

Meanwhile, Jokowi shared his great confidence in the current defense budget, citing his disbelief in immediate foreign attacks. Increasing the defense budget is thus not his priority. Rather, according to Jokowi, the country should focus more on developing infrastructure and human resources.

A country's defense policies, however, should act in parallel with its security needs and larger interests. Regardless, the candidates' proposed defense measures do not necessarily match Indonesia's security needs and risks. The inconsistency between the proposed defense measures and the actual circumstances therefore indicates that an increased defense budget may not offer the most ideal solution.

Insight: While never explicitly stated, President Jokowi's and Prabowo's opposing views on defense might result from the different approaches to security that they adopted; while Jokowi envisioned a human-centered security, Prabowo espoused a more traditional state-centered security.

In regard to Jokowi, the proposal on defense and security that he presented during the fourth presidential debate can be summarized as less military power, more diplomacy. Claiming that the current defense budget had been adequate, Jokowi suggested that the state should focus more on infrastructure and human development instead. Indeed, Jokowi is known for his ambitious infrastructure projects and would shift his focus to human development if he gets reelected. It is no surprise then if his perception on defense and security overlaps with the notion of human-centered security, where the referent object of security is the people and the main objective is to create "freedom from want" and "freedom from fear".

To establish Indonesia's international presence, Jokowi proposed employing diplomacy. Having the largest Muslim population in the world, Indonesia, for instance, may use its demographic composition as diplomatic leverage. According to Jokowi, such a strategy bore fruit in the past, such as when Indonesia was chosen by the United Nations secretary-general António Guterres to be a conflict mediator in Rakhine state, Myanmar. Furthermore, in accordance to his free, active foreign policy, Jokowi also sought deepening economic cooperation with other states as a means to ensure stability and security.

In contrast, Prabowo frequently cited threats of foreign invasion. Asserting Indonesia's vulnerability, he reiterated the importance of increasing the defense budget. Prabowo also scoffed at Jokowi's preference for diplomacy, claiming that diplomacy and being "the nice guy" would not be so useful in the face of foreign invasion. In short, Prabowo does not believe in diplomacy if it is not gunboat diplomacy. In this sense, it is clear that Prabowo believes in a state-centric approach of security, where foreign military aggression poses the biggest threat against one's territorial sovereignty.

There are some errors, however, in Prabowo's perspective. First, discussions on defense measures should not center around budgets, but rather on how the measures can be tailored according to the country's geostrategic objectives. Prabowo's comparison of Indonesia's defense budget and Singapore's is, thus, irrelevant as both countries have different strategic needs, roles and security risks. Furthermore, instead of creating a more stable and secure environment, using neighboring countries as one's parameter in determining a defense budget may prompt a security dilemma, which refers to a situation in which a country's decision to diminish its security risks by improving its defense capabilities is perceived by other countries as a threat. Consequently, countries often respond with similar measures, leading to a spiraling situation in which countries become embroiled in an arms race. Aiming to rival Singapore in terms of its defense budget, thus, may lead to regional instability.

Second, a country's defense and security measures should be in line with its domestic and international interests at large. Prabowo's suggestion to take a stronger military stance, however, contradicts his proposed "thousand friends zero enemies" principle in regard to foreign policy. After all, who wants to befriend an aggressive and militarized country?

No wonder if Prabowo's adoption of a state-centric approach to security affects his perception of threats. Denouncing President Jokowi's disbelief in the possibility of war in the upcoming years, Prabowo repeatedly emphasized the imminence of foreign invasion throughout the debate. Regardless, Jokowi's optimism is not as unfounded as Prabowo insinuated. The end of the Cold

War has indeed ushered in a contemporary mode of warfare, in which major direct invasions become unlikely. Instead of total war as Prabowo illustrated, modern warfare often takes the form of isolated local conflicts and centers around information and networks instead of brute military strength. Basing his proposal on the conventional conception of military threats may be irrelevant in today's era.

Despite the errors in Prabowo's argument, he did bring up an interesting point. However, should Indonesia decide to increase its defense budget, its use must be in accordance with the new security reality that Indonesia faces. Among others, Indonesia's most notable security risks include the issue of separatism in Papua, the return of Indonesians who had joined the Islamic State (IS) movement in Syria and the increase of cyberwarfare in the forms of hoaxes and private data theft.

To address these security risks, several aspects of Indonesia's defense should be considered. First, the country's defense industry is still deemed lacking. Fatal accidents caused by outdated military equipment still occur.¹ President Jokowi himself has underlined the importance of improving the domestic defense industry; during the debate Jokowi proposed investments in the domestic defense industry.² Through maximum investments, it is expected that Indonesia can produce more weapons for defense and lower arms exports. This, however, leads to the second issue, which is the mismatch between Indonesia's primary weaponry defense system (Alutsista) and the type of weapons actually needed in the current era of warfare. As previously stated, contemporary warfare is markedly different from warfare in the past. In combating cyberwarfare, for instance, tanks are not as useful as they are in front-line combat. Lastly, an enhanced defense industry and updated weaponry are nothing without competent, well-organized and prosperous soldiers. While soldiers' welfare has been addressed by President Jokowi,³ issues about a bloated military recently emerged.⁴ A long-term plan of restructuring, thus, is urgently needed to address the military's internal management problems.

In short, will increasing the defense budget answer Indonesia's current security issues? The answer is no if the budget is allocated selectively. In the case of Prabowo, it may be extensively used to counter "imminent foreign threats", while in the case of Jokowi the defense budget has been mostly used for soldiers' welfare. Meanwhile, in order to completely strengthen one's military capability, four pillars must be addressed, namely weaponry, human resources, strategies and soldiers' welfare. The aim is thus not to increase the defense budget, but to use the budget effectively across the entire defense spectrum according to Indonesia's geostrategic objectives.

¹Thejakartapost.com, "Jokowi pledges ambitious arms spending" 24 February 2016 <http://tinyurl.com/y4kjhate>

²Kompas.com, "Jokowi Sebut Minimnya Anggaran Pertahanan Disiasatidengan Investasi Alutsista" 30 March 2019 <http://tinyurl.com/y5sfbkt5>

³Tribunnews.com, "Ini Daftar Kenaikan Gaji TNI 2019 Mulaidari Prajurit Sampai Jenderal, Banding kandengan PNS-Polri" 26 March 2019 <http://tinyurl.com/y3lvogd5>

⁴Laksmiana, Evan A., "Military personnel problems need more than quick fixes" 1 February 2019 <http://tinyurl.com/y7wxno47>

High absenteeism Jokowi's worst nightmare

Incumbent President Joko “Jokowi” Widodo looks set to win his reelection bid, at least that’s what most opinion polls say with less than two weeks to go. Of 10 surveys by reputable institutions, all but one say he is leading by double digits over challenger Prabowo Subianto. Jokowi looks unbeatable. What could possibly go wrong? Apparently, Jokowi’s campaign team has been concerned about the possibility of a high level of absenteeism as the one thing that could ruin his chances. Working on the assumption that most of the possible absentee voters would vote for Jokowi, his campaign team has been going around persuading or even intimidating people to go out and vote on April 17.

Takeaways:

- While Jokowi looks set to secure his reelection bid, absenteeism remains a major threat for the President. There is shared concern that absenteeism would be higher than the 25 percent recorded in 2014 election.
- Not only does the level of absenteeism measure the faith of people in the political system, a high level of absenteeism may potentially undermine the elected government.
- The fight against absenteeism has been strong, involving politicians, Cabinet officials and key religious figures.
- The reasons behind absenteeism are many, including indifference or political apathy, limited choices offered by the electoral systems and disillusionment. This year’s presidential election is particularly vulnerable to absenteeism as it takes place a day before the Good Friday. People, thus, may prefer to skip voting in order to take an extended holiday.

Background: “Punch and then go on holiday,” was the latest key message Jokowi has been voicing in the last weeks of the campaign period. (Indonesians vote by punching a hole in their ballot papers.) Jokowi did not have to sell his policies. Being the incumbent, his track records speak for him. Good or bad, or not good enough, is something voters decide for themselves. At this stage, most have made up their minds and opinion polls indicate he would win the presidential race.

All that Jokowi needs to do is to convince people to get themselves up on the morning of April 17 to cast their votes and enjoy the rest of the day, which has been declared a national holiday.

Voter turnout 1999-2014 (%)		
1999	93	Electoral college system
2004	76 - 78	Direct presidential election, two rounds
2009	72	Direct presidential election, one round
2014	75	Direct presidential election, one round

That seems harder to do. Voting is not compulsory and going by social media memes, many disillusioned voters have declared themselves to be “Golput”: the term coined during the Soeharto years to describe the group of voters who spoiled their ballot papers to protest against the rigged political system that ensured victory for Soeharto and his Golkar party. This time, it looks like there are enough disillusioned and apathetic voters, but rather than casting a spoilt ballot paper, most would likely vote with their feet. The Good Friday national holiday on April 19 gives an added incentive for many to leave town that week and enjoy a much longer vacation.

Jokowi's appeal to people to take their holidays after casting their votes and other similar messages, some delivered with harsher words by his campaign team, suggest they are worried sick that high absenteeism, rather than Prabowo, could deny Jokowi his second term in office.

Insight: The level of absenteeism has always been a concern to the government and the General Elections Commission (KPU) for it measures the faith people put in the political system and a low turnout would also undermine the legitimacy of the elected government.

This is the fifth democratic election in post-Soeharto Indonesia, but in a democracy where voting is not compulsory, not voting is a democratic right and a choice, as much as the KPU abhors it. For the independent KPU, the scale of absenteeism is considered one of the key performance indices (KPI) to measure its success. For 2019 the KPU has set itself the target of a voter turnout of 77.5 percent.

Since not voting is an option, there is more than one reason that explains the level of absenteeism, from people simply being indifferent and politically apathetic (believing their votes don't matter), to people feeling the electoral system doesn't give them real choices (since there are the same two candidates as in 2014) and people not voting because they are too disillusioned with their chosen candidates.

The latter group includes many of the traditional supporters of Jokowi who are not impressed by his performance on issues dear to them. In Jokowi's case, protecting the rights of minorities and upholding human rights count high among issues for which the incumbent failed to deliver.

His shifting to the right side of the political spectrum, as reflected by the choice of Ma'ruf Amin, a conservative ulama, as his running mate and giving more concessions to the military has further caused many of his traditional supporters to abandon him. This ideological shift has not come without a cost to Jokowi. Many of his supporters on the left of the political spectrum feel Jokowi has abandoned them. They are upset, but not upset enough to give their votes to Prabowo. They are the ones who have openly declared on their social media to be participating in Golput.

WHAT THEY SAY ABOUT GOLPUT	
Incumbent President Joko Widodo	Punch and then go on holiday
Megawati Soekarnoputri, chair of the Indonesian Democratic Party of Struggle	Golput forfeits their Indonesian citizenship
Wiranto, Coordinating Minister for Politics, Law and Security	People who incite others to become Golput are troublemakers. There are law against this.
Indonesian Ulema Council (MUI)	Voting is obligatory. Golput is haram.
Catholic Father Magnis Suseno in a Kompas article. Later he regretted at his choice of words.	Golput reflects three possible characters: stupid, parasite mentality, or mentally unstable (psycho-freak).
The Council of Churches in Indonesia (PDI)	Be a 100 percent Indonesian citizen and 100 percent member of the church
Bishops' Conference in Indonesia (KWI)	Golput is tantamount to letting this nation be governed by anyone, including those who would undermine Pancasila and destroy this country.
Dahnil Simanjuntak, spokesman for Prabowo-Sandiaga campaign team	They become golput because they are disappointed with the current government. They say the incumbent is a failure.
Fadli Zon, founding member and deputy chair of Gerindra	The government is panicking over golput. We don't need golput votes. We'll win without them.

The two national holidays, April 17 and Good Friday on April 19, are further incentive for people not to vote and instead leave town for an extended vacation. Indonesians have the expression “Harpitnas”, short for *hari kejepit nasional* (national in-between holiday), which refers to people taking a day off from work on a day that is caught between two national holidays or with the weekend. Whoever in the KPU last year decided on April 17 as election day had not foreseen the possibility of Harpitnas.

The fear of losing ground on Jokowi’s traditional support base has triggered a concerted campaign to get the vote out. The incumbent has been joined by his Cabinet officials and religious leaders in appealing to people to use their voting rights. Some went as far as intimidating or threatening those who have declared Golput or are thinking of abstaining.

The Protestant and Roman Catholic communities, which are counted among Jokowi’s traditional support base, are most vulnerable to the Harpitnas appeal. Many are disillusioned enough at his failure to protect their interests that they have decided to skip the election and celebrate Easter out of town, or out of country.

The growing ranks of Golput participants among the Christian minorities has prompted Father Magnis Suseno, a respected Catholic priest, to write harshly about Golput people, describing them as stupid, having a parasite mentality or just mentally unstable, and he used the expression “psycho-freak”. His *Kompas* article went viral but in an interview with *Tempo* magazine a few days later, he said he regretted his choice of words, saying he had written it in the spur of the moment and was dazzled by the fancy words.

While Golput is not a crime, inciting others not to vote is and Coordinating Political, Legal and Security Affairs Minister Wiranto has threatened to prosecute those who have declared Golput in social media, saying that this could amount to inciting others to join them. He was quickly rebuked, not surprisingly, by people in the Prabowo camp. Although the electoral law makes it a crime for people to incite others or use force to prevent them from voting, no one has gone to jail for this.

Opinion polls have not quite captured the numbers of disillusioned voters as no one who was surveyed would openly declare they are going to abstain. Different pollsters have also made to many different estimates about the size of absenteeism for anyone to be able to make any conclusion about this phenomenon. The scale of absenteeism can only be known on election day.

There is an agreement or a shared concern, particularly in Jokowi’s camp, that absenteeism would be higher than the 25 percent recorded in 2014. Normally, the scale of absenteeism would reflect badly on the elected president and leave him open to accusations of having low legitimacy. For Jokowi, legitimacy is the least of his worries, compared to losing the election.

Commentary: Police’s neutrality under question again

National Police chief Gen. Tino Karnavian has taken measures to make the upcoming general election a success, starting from discouraging poll abstention to advising on the danger of hoaxes. The neutrality of the police, however, has come under public scrutiny following several incidents. A widely circulated screenshot of a WhatsApp conversation between the head of a precinct police and his subordinates, for instance, shows how the police have been urged to support one particular presidential candidate. Furthermore, the former head of a subprecinct police admitted that he had been rotated because he took a photo of him and a certain presidential candidate.

Insight: Ensuring the neutrality of state institutions, including the police, in political contestation, plays a major role in preserving the legitimacy of elections, creating a peaceful environment throughout the election process, and building public trust in the institution. While on the surface the National Police have shown their good intention to stay neutral, the recently circulated WhatsApp conversation between police officers indicates otherwise. Police's roles, duties and obligations throughout the campaign and election period have now been doubted.

If candidates manage to acquire the support of state institutions, especially one as preeminent as the police, it will surely greatly benefit their electoral campaign. Support at the grassroots level can be easily secured by the police, where officers' clout and network are extensive. The issue of police neutrality would lead to both benefits and damages to the candidates.

Regardless, the benefits may not worth the hassle. As more people question the neutrality of the police, people may start losing their faith in the candidates allegedly supported by the police. The alleged mobilization of state institutions will cause people to question the validity and legitimacy of the election's results. One wrong move and the other candidate may reap electoral benefits from the suspected candidate's clandestine relationship with the police.

Commentary: Bowo's case indicates growing attempts of counterattack

Golkar Party politician Bowo Sidik Pangarso has been named a suspect by the Corruption Eradication Commission (KPK) for allegedly accepting bribes. Bowo reportedly plans to distribute the money to voters hours before voting begins on April 17. Such tactic is locally known as *serangan fajar* (dawn attack). The KPK's discovery of thumbprints on envelopes found as evidence for the case, however, has created speculation that vote-buying is also related to the presidential election.

Insight: While Bowo's bribery case indicates that transactional politics continues to occur in the electoral system, it conveys a more important message: supporters have become more fervent and sporadic in endorsing candidates. Supporters of presidential candidate Prabowo Subianto and running mate Sandiaga Uno have attempted to associate the thumbprints found on Bowo's envelopes as a sign that the bribery case is related to incumbent Joko "Jokowi" Widodo's reelection bid, all because the President's campaign is known for its thumbs-up gesture. The fact that Bowo is a member of a political party supporting Jokowi is also used by Prabowo-Sandiaga supporters to corroborate their far-fetched hypothesis.

With only less than a month left before the 2019 general election takes place, candidates may grow more desperate to acquire votes. Any last-minute, sporadic measures may be imposed, even if their foundation is shaky at best, or purely irrational at worst. Consequently, not only are more and more wild speculations circulating among the public but common sense is also being attacked. In the long run, such sporadic attacks may turn the public sphere into a fertile ground of falsehood and misinformation.

BUSINESS & ECONOMIC POLICY

Poor policy design behind sudden cancellation of e-commerce regulation

The government abruptly cancelled the implementation of Finance Ministerial Regulation No. 210/2018 on e-commerce taxation after it was slated to kick off on April 1, rising questions over the soundness of the design of this policy.

Takeaways:

- The government canceled the implementation of PMK 210/2018 on April 1 because of poor regulation design, in which it neglects the fact that social media platforms remain the most used platforms for e-commerce transaction instead of online marketplace.
- The e-commerce taxation policy is likely to continue with strong influence from e-commerce business players.

Background: On December 31, 2018, the Finance Ministry announced Finance Ministerial Regulation No. 210/2018 on e-commerce taxation.⁵ The regulation would have stipulated how merchants and marketplace operators should report their taxes.

All merchants that operate in a marketplace platform must register either their tax ID (NPWP) or their citizen ID number (NIK), if they do not have their NPWP yet, to marketplace operators. Moreover, merchants with annual revenues over Rp 4.8 billion must be registered on the corporate taxpayer list (PKP) to collect value added (PPN) and luxury goods (PPnBM) taxes. These taxes would have been documented and reported to the tax authority by marketplace operators.

Besides regulating tax reports and the enforcement of tax collection by merchants in online marketplaces, the regulation would have also stipulated the taxation and duties on e-commerce transactions conducted by marketplace platform provider companies such as Blibli, Bukalapak, Elevenia, Lazada, Shopee and Tokopedia.

However, the regulation fell short in addressing e-commerce transactions conducted in social media platforms such as in Instagram and Facebook, where the bulk of Indonesia's e-commerce transactions are made.⁶ For marketplace platform provider companies, this is a source of concern.

Insight: The sudden cancellation of this highly anticipated policy surprised the public, as the government has insisted on the soundness of this regulation by stating that it would be widely accepted and welcomed by both online and offline retailers. For offline retailers, e-commerce tax is necessary because it levels the playing field between online and offline retailers.⁷ For online retailers, however, the regulation is inadequate and does not match with reality on the ground.

⁵ Indonesian Tax Office, "Kado Manis Sri Mulyani PMK-210 tahun 2018," Jan. 15, 2019.

<http://tinyurl.com/yxep4n96>

⁶ Hukumonline.com, "Inipokok-pokokkeberatanpelakuusahaatasterbitnya PMK e-commerce." 14 January 2019

<https://tinyurl.com/ya5qzori>

⁷ Beritasatu.com, "Pajak e-commerce buatpersaingndenganritellebihadil." 16 January 2019

<https://tinyurl.com/y9zp89ws>

It seems that the Finance Ministry used the offline retailers' logic when it designed the e-commerce tax. In January 2019, for example, Finance Minister Sri Mulyani Indrawati stressed the regulation would close the price gap between goods sold online and offline, hence creating a fair level playing field between e-commerce and conventional businesses. The ministry's spokesperson, Hestu Yoga Saksama, also complemented Sri Mulyani's statement by saying it would become a legal basis for e-commerce's merchant and customers' protections.⁸

The high economic potential of the Indonesian e-commerce sector is another main factor behind the taxation policy design. A study by the Indonesia Investment Promotion Center (IIPC) of New York revealed that e-commerce is the main driver of Indonesia's digital economy, which has an estimated value of US\$27 billion.⁹ Data from Bank Indonesia also shows that Indonesia's e-commerce sector has grown rapidly since 2017, specifically from Rp 1.9 trillion in January 2017 to Rp 10.9 trillion in December 2018.

Nevertheless, the fact that social media hosted up to 80 percent of e-commerce transactions in Indonesia – according to Paypal Asia's Survey in 2017¹⁰ was not considered by the government when it designed PMK 210/2018.

In 2018, the Indonesian e-Commerce Association (idEA) conducted a survey to convince the government that social media is the most used platform for e-commerce activity, rather than online marketplace platforms. The survey has not been published, yet, but there is a rumor circulating that the findings are not much different from idEA's survey in 2017, in which 59 percent of e-commerce transactions are conducted through social media platforms such as Instagram and Facebook, while e-commerce transactions through online marketplace platforms only account for 16 percent.

Using this finding, idEA lobbied the Finance Ministry to delay the implementation of PMK 210/2018. idEA also argued that hasty implementation of PMK 210/2018 would only result in an exodus of the marketplace's vendors and merchants to social media platforms to avoid the new e-commerce tax.

E-commerce and E-money transaction value growth 2017-2019 (Rp trillion)

Year	Month	E-commerce transaction value	E-money transaction value
2017	January	1.9	0.7
	February	1.8	0.8
	March	2.1	0.7
	April	2.0	0.6
	May	2.3	0.9
	June	2.2	1.02
	July	2.6	1.14
	August	2.9	0.8
	September	3.0	0.8
	October	3.2	1.26
	November	3.5	1.64
	December	3.7	1.95
2018	January	3.53	3.49
	February	3.52	3.36
	March	4.4	3.45
	April	4.7	3.35
	May	6.4	3.53
	June	4.3	3.46
	July	5.9	3.58
	August	6.7	3.89
	September	7.8	3.51
	October	9.8	4.44
	November	11.2	5.19
	December	10.9	5.88
2019	January	8.6	5.81

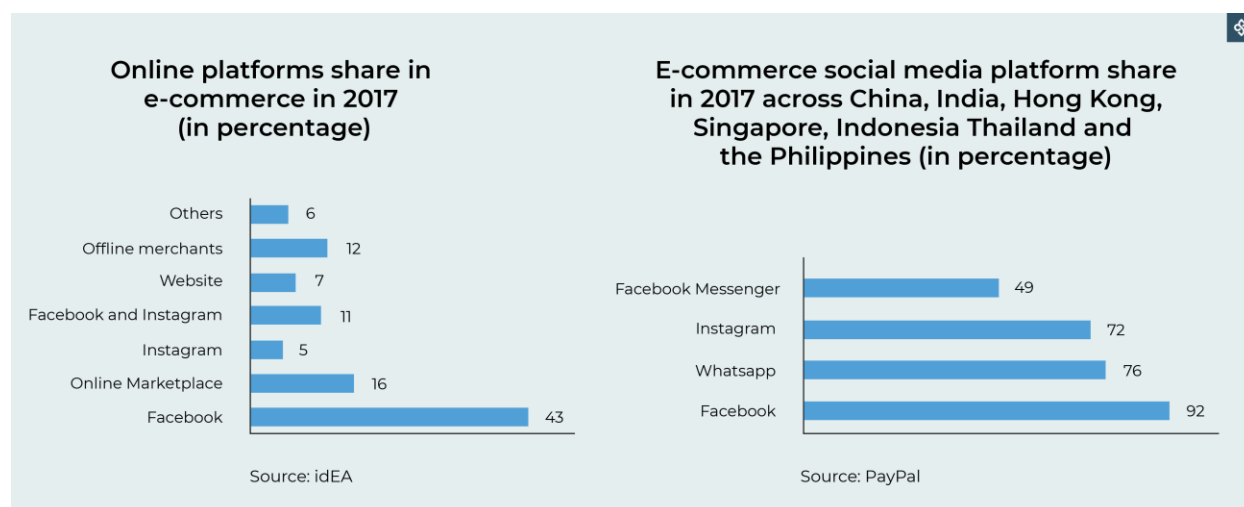
Source: Bank Indonesia

⁸ Finance Ministry, "Inialasanditerbitkan PMK 210 tentang E-commerce," Feb. 15, 2019. <http://tinyurl.com/yxzgyfzd>

⁹ *Tempo.co*, "Indonesia's digital economy in 2018 largest in Southeast Asia," Feb. 22, 2019. <http://tinyurl.com/y52l4tb9>

¹⁰ *Katadata.co.id*, "Pembatalanaturanpajak e-commerce," Apr. 1, 2019. <https://tinyurl.com/y48vhuyum>

After an idEA lobby on March 28, a few days before the regulation was supposed to start,¹¹ the Finance Ministry eventually gave in to idEA's demand. In announcing the delay, Sri Mulyani explained that the public and the e-commerce community need further information on PMK 210/2018 to avoid any false interpretation and misunderstanding in the future.



Financial woes shackle Krakatau Steel

State-owned steel producer Krakatau Steel has been leading local steel producers in their two-front fights against the low-quality steel produced domestically and cheap steel imports, dumped mainly from China. As the fights are escalating, Krakatau Steel now faces its own internal problem, mounting debt.

Takeaways:

- Mounting debts have diminished Krakatau Steel's profitability amid unfavorable market conditions. Worse, the company has resorted to taking out new loans to cover past debts.
- The newly appointed president director Silmy Karim, has a good track record and could potentially turn the company around. However, he would still need strong support from the government to settle the debts hanging over the company.

Background: State-owned steel producer Krakatau Steel has been leading local steel producers in their two-front fights against the low-quality steel produced domestically and cheap steel imports, dumped mainly from China. As the fights are escalating, Krakatau Steel now faces its own internal problem, mounting debt.

Krakatau Steel is facing fierce competition from cheap, low-quality steel produced by induction furnace steel mills relocated from China. These relocated steel mills have grown in number and they sell their products much cheaper, undermining Krakatau Steel and other local steel producers that face difficulties in selling their products, even though they are said to be of higher quality and environmentally friendlier.

¹¹Investor Daily, "Transaksi di medsosharusdapatperlakuanpajaksama," Mar. 29, 2019. P.24

Not only that, Krakatau Steel is also facing tough competition from cheap imported steel, mainly from China. Following complaints from local producers, the Indonesian Antidumping Committee (KADI) investigated the imported steel from China and found dumping practices. The government then slapped antidumping duties on imported steel from China. However, our sources said that the antidumping duties were not effective as importers found ways to get around them. As a result, imported steel is still prevalent in the market.

Simply unable to compete in its own domestic market, Krakatau Steel is facing deeper internal, financial problems, with continuing losses year after year since 2014 and mounting debts – the latest figure is at Rp 35 trillion (US\$2.5 billion) (see tables below). The market is weary over Krakatau Steel eventually having to default on some of its debts.

Rp billion	2014	2015	2016	2017	2018 (to Sept)
Operating profit	-876.3	-2,690	58,984	687,480	-159.8
Net profit	-1,951	-4,785	-2,428,	-1,166	-548
Retained earnings	-439.4	-5,245	-6,876	-8,174	-9,565
Total equity	11,094	26,208	24,717	25,101	25,054
Total liabilities	21,229	28,054	28,175	30,639	35,192
Total assets	32,324	54,262	52,893	55,741	60,261

Krakatau Steel short-term and long-term debt (in million USD)			
Krakatau Steel short-term loans as of Sept. 2018		Krakatau Steel long-term loans as of Sept. 2018	
Bank Mandiri	350.9	Syndication of Mandiri, BNI, BRI	515.1
Bank Negara Indonesia (BNI)	233.1	Syndication of OCBC, ICBC, CIMB, Eximbank	154.2
Bank CIMB Niaga	193.5	Syndication of Commerzbank, AKA	136.4
Bank OCBC NISP	77.5	Bank Mandiri	49.2
Indonesia Eximbank	53.1	BRI	36.5
Bank Rakyat Indonesia (BRI)	50.9	PT SMI	9.5
Bank DBS Indonesia	30.6	BNI	7.7
Bank Standard Chartered	27.3	Bank Muamalat	1.7
Bank Central Asia	18.9	BJB	0.5
Bank Danamon Indonesia	13.3	BNI Syariah	0.2
BNI Syariah	9.2	Others	10
PT SMI	1.5		
BJB	0.2		
Total	1,060	Total	921

Source: Krakatau Steel financial report

Insight: Krakatau Steel is “*Bagai tikus mati di lumbung padi*” (like a rat dying in a rice barn). In the past four years, the government has been busy building infrastructure in various sectors, and most of them – if not all of them – would require steel to build. As a state-owned company that has long enjoyed various privileges, Krakatau Steel has performed poorly. It has suffered

losses year after year in the past five years. Retained earnings have been negative. And its debt has been mounting.

Rather than being busy attacking cheap steel products in the market, Krakatau Steel better look into its own business processes to determine why it cannot compete with both locally produced and imported steel products. There must be issues within Krakatau Steel that has caused it to be unable to compete in its own market.

Indonesia's steel market has been on the rise since as the government focuses on infrastructure development. Demand for steel grew to 13.4 million tons per annum last year, of which local producers -- including environmentally-unfriendly induction steel mills -- could supply only about half. The Indonesian Iron and Steel Industry Association (IISIA) has projected that demand is to increase further to 23 million tons in 2025 and 45 million tons in 2035.¹²

Therefore, the steel business has been good in Indonesia. Yes, there is steel oversupply in the world, resulting in the flooding of cheap imported steel into Indonesia. Yes, there has been market disruption from cheap steel produced locally by induction steel. But the demand is still big. And much of the demand comes from state-owned companies, that by far, could be the captive market for Krakatau Steel. In fact, that was exactly what Krakatau Steel president director Silmy Karim did soon after he assumed his position last year.

Silmy took his chance to secure as many as customers he could find in the market. A month after his appointment, Silmy sealed deals with multiple state-owned construction operators, namely Waskita Karya, Adhi Karya, Wijaya Karya, Hutama Karya, Nindya Karya and PT Pembangunan Perumahan (PP), to supply up to 1 million tons of steel to construction projects done by these companies. Concurrently, he lobbied state-owned companies to use steel his company produced and gained assurance from Waskita Karya, Adhi Karya and Wijaya Karya. As a result, last year Krakatau Steel booked a much lower net loss of Rp 548 billion, compared to a loss of over Rp 1 trillion in 2017, Rp 2.4 trillion in 2016 and Rp 4.8 trillion in 2015.

Silmy also moved ahead with the company's joint venture with POSCO of Korea to build a 10 million-ton-capacity steel industry cluster in Cilegon, which will require investment of between US\$3.5 billion and \$4.5 billion. The project is estimated to be completed before 2025. This year, both companies will focus on the completion of Hot Strip Mill 2, which will cost \$515 million. Hot Strip Mill 2, which will have a production capacity of 1.5 million tons per year, is expected to start operations this year.¹³

Silmy has a good chance to be successful in leading Krakatau Steel. However, looking at the severity of the company's debt, he would need political support from the government to solve the company's debt hung.

What we've heard: According to a government official, the State-Owned Enterprises Ministry is preparing a strategy to save Krakatau Steel from financial catastrophe. One of the measures is requiring the steel producer to restructure its debt, which amounted to Rp 35 trillion as of September 2018.

¹² The Jakarta Post, "Steel imports inevitable for Indonesia", Feb. 8, 2018.

¹³ The Jakarta Post, "Krakatau Steel to focus on Cilegon steel cluster development," March 26, 2019

Silmy Karim, specialist for deceased SOEs

Silmy Karim is known to the media as the “specialist of deceased SOEs” for his track record in fixing state-owned companies’ financial woes.¹⁴ Starting off his executive career in 2014, Silmy led state-owned weapon manufacturer Pindad out of market deficiency and increased the company’s yearly sales by 36 percent in 2016. Pindad became one a world renowned weapon manufacturer in two years through market expansion and production capacity improvement less than 20 months after Silmy was appointed. Silmy achieved this after he managed to help the Defense Ministry resolve a weapon sales dispute during his service as a ministerial economic consultant prior to 2014.

Following his success in Pindad, Silmy was assigned to improve state-owned machine manufacturer PT Barata Indonesia’s declining performance. Under his leadership, Barata was able to secure multiple contracts with the highest worth of Rp 866 billion for the Gempolkrep sugar factory – belonging to state-owned plantation company PT Perkebunan Nusantara X – before he left the company for Krakatau Steel.¹⁵

The rising debt has disappointed State-Owned Enterprises Minister Rini Soemarno, who initially planned to place Krakatau Steel under mining holding company Inalum this year. Rini has reportedly reprimanded her deputy, who is responsible for the steel industry for being slow in solving the Krakatau Steel debt problem.

To solve its financial woes, Krakatau Steel met with a number of state-owned lenders to restructure their loans. State lenders’ loans to Krakatau Steel reached 60 percent of its total debts. Bank Mandiri reportedly lent the most money to Krakatau Steel, reaching US\$760 million in 2018. The debt accumulation happened because the company was unable to settle its previous debts and resorted to new loans to cover up its debts.

After some meetings, Krakatau Steel and its lenders agreed to restructure the company’s debt, just one day before the Corruption Eradication Commission (KPK) caught red-handed Krakatau Steel technical operation director Wisnu Kuncoro for allegedly accepting bribes. The debt restructuring includes cutting interest rates and prolonging the debt expiration period.

State lenders are cooperative with Krakatau Steel but private lenders are not. As such, not all private lender agree to the debt restructuring plan. Some of the known private lenders are CIMB Niaga, BCA and ICBC NISP.

As Krakatau Steel is still negotiating the debt restructuring, the company is finding new alternative sources of funding by selling its assets to other state-owned enterprises. This path is being pursued to stop the emergence of privatization ahead of the elections. One of the auctioned assets is a power plant in an industrial complex in Cilegon, Banten, which was sold to state-owned electricity company PLN. Krakatau Steel’s bulk port in Cilegon was also listed as one of the auctioned assets.

According to the source, Rini has been helping Krakatau Steel by gathering several CEOs of state-owned enterprises, such as PLN, state-owned port operator Pelindo and state-owned banks, to assist Krakatau Steel.

¹⁴ *Kumparan*, “TheCEO: Silmy Karim, spesialis BUMN sakit,” Jan.4, 2019. YouTube video: <https://tinyurl.com/y6p9wryd>

¹⁵ *Kompas*, “Dirut Barata Indonesia digeser untuk menyelamatkan Krakatau Steel,” Sept.14, 2018. <https://tinyurl.com/y3s2dgg3>

Policy update: New fare stipulations for app-based motorcycle taxis disadvantageous

The Transportation Ministry finally announced the long-awaited fares for app-based *ojek* (motorcycle taxis) last week - via a ministerial decree as a derivative of Ministerial Regulation No. 12/2019 - after the government “recognized” the mode as public transportation the previous week.

Takeaways: Fare setting should have been left to natural supply-and-demand market mechanisms. Government intervention through fare stipulation will reduce firms’ incentives to improve their performance, will prevent newcomers breaking into the industry and reduce customer benefits.

Background: The announcement came as a relief following a series of protests drivers had been staging over the past year demanding better pay and working conditions. These protests have heightened tension between drivers and application providers, namely Grab and Go-Jek, who have their own interests in maintaining control of their market share through various methods of discount coupons and low fares per kilometer. The new set of fares was calculated based on input from applicators, drivers’ associations and government studies of drivers’ indirect and direct operational costs.

Components of direct costs	Component of indirect costs
Partner’s profit, vehicle depreciation, driver’s personal costs, interest fees, fuel costs, maintenance and repair costs, internet and telephone bills, vehicle taxes, insurance fees	Application service fees

The decree stipulates that total fares must cover direct and indirect costs, where maximum indirect costs are 20 percent of the total components of direct costs that would be added to the total fares for customers to pay. Starting from May 2019, customers must pay around Rp 2,312 – Rp 3,000 per kilometer and an additional service fee of Rp 7,000 to Rp 10,000 when using online *ojek*.¹⁶

Type of fare	Zone I	Zone II	Zone III
Minimum fare	Rp 1,850	Rp 2,000	Rp 2,100
Maximum fare	Rp 2,300	Rp 2,500	Rp 2,600
Basic fare	Rp 7,000 – Rp 10,000	Rp 8,000 – Rp 10,000	Rp 7,000 – Rp 10,000

Zone I: Java, Sumatra, Bali – East Nusa Tenggara; Zone II: Greater Jakarta Area; Zone III: Sulawesi, Kalimantan, Molucca, Papua and West Nusa Tenggara

Source: Transportation Ministry

¹⁶ *Bisnis Indonesia*, “Tarif ojol telah ditetapkan Kemenhub, ini dasar penghitungannya,” Mar. 26, 2019.

<https://tinyurl.com/y6pmcvwh>

However, Land Transportation Director General Budi Setiyadi stressed that applicators can still provide promotional prices and discounted rides as a business strategy as long as they do not breach government-set tariffs for drivers.¹⁷

Insight: Transportation Ministerial Regulation No. 348/2019 complements Transportation Ministerial Regulation No. 12/2019. However, the fare stipulation provides legal certainty to app-based *ojek* (motorcycle taxis), although they are yet to be considered public transportation by the Transportation Law. However, if the government wants to set the fares for online *ojek* and to make them a legal transportation option, it must also enforce the regulations on traditional *ojek*/non-online *ojek*.

Unfortunately, the fare stipulation is likely to create unhealthy business competition. First, the minimum fare stipulation will put passengers at a disadvantage as they will not be able to avail of lower fares during low-demand periods. Moreover, they must pay higher fares for short-distance trips.

An interesting comparison is the difference between the starting price of online *ojek* and other transportation options. For example, in Jakarta, the fare for the first kilometer on an online *ojek* (Rp 8,000) is higher than for conventional taxis (Rp 6,500). Although a taxi's per kilometer fare is still far higher (Bluebird: Rp 4100/km; Express: Rp 3800/km) than online *ojek*¹⁸, it is still surprising to see that online *ojek* starting prices are higher than more comfortable transportation options like taxis.

Secondly, the fare stipulation provides leeway for cartel by regulation. Companies will tend to set similar fares and lose their sense of competition with minimum fares. The absence of competition, then, will put customers at another disadvantage by reducing companies' motivation to operate more efficiently. At the same time, the new fare regulation also creates a barrier for newcomers. The set fares require newcomers to have higher startup capital in order to provide the same quality of services as their established competitors.¹⁹

¹⁷ *CNBC Indonesia*, "Tarif ojol baru: Berapa keuntungan yang diperoleh aplikator?," Mar. 25, 2019. <https://tinyurl.com/y3stexy6>

¹⁸ *Republika.co.id*, "Polemik tarif taksi online dan kenyamanan yang digadaikan," Apr. 5, 2019. <http://tinyurl.com/yxhuwr8v>

¹⁹ *CNN Indonesia*, "KPPU: Tarif ojek online tak perlu batas bawah dan batas atas," Mar. 26, 2019. <http://tinyurl.com/y3tu9rxf>

Issue update: Susi faces uphill battle against illegal fishing

Maritime Affairs and Fisheries Minister Susi Pudjiastuti has called for an end to the auctioning of foreign fishing vessels caught in Indonesian waters by sending a tweet: “Destroy them all!”²⁰

Background: Susi expressed her anger and disappointment through her Twitter account on Monday when she found that many of the foreign fishing vessels caught for illegal fishing by her ministry were allowed to operate again after being auctioned. “We must stop this nonsense,” she tweeted.

Susi has been hardening her position on the destruction of illegal fishing vessels. Her suspicion of possible collusion between government officials and owners of the detained fishing vessels through state auctions has strengthened her resolve. Susi’s suspicion is not without evidence. In February, the Maritime Affairs and Fisheries Ministry recaptured a Malaysian vessel that had been caught in August 2017 and released through an auction by the North Sumatra Prosecutor’s Office a few months later.

The Attorney General’s Office and the North Sumatra Prosecutor’s Office denied allegations of fraudulent practices in the auction, saying that the process followed the law and prevailing regulations. North Sumatra State Attorney Office representative Sumanggar Siagian said the auctioned off Malaysian fishing vessel was reported to the Attorney General’s Office. At the same time, another problem has resurfaced, namely a disagreement between the Maritime Affairs and Fisheries Ministry and the Office of the Coordinating Maritime Affairs Minister over the prohibition of lobster seed sales for lobster farming. On Tuesday, Coordinating Maritime Affairs Minister Luhut Pandjaitan suggested to relax the prohibition, arguing that the relaxation was necessary to support the government’s plan to develop the domestic lobster farming industry, including the lobster farm pilot project in Sukabumi.

The Maritime Affairs and Fisheries Ministry opposed Luhut’s suggestion, arguing a relaxation would open a loophole for smuggling, which in turn would damage the ministry’s program in promoting a sustainable supply of lobster. The ministry also argued that lobster farms’ production capacity, which just reached 200,000 per year, was below the recommended level for sustainability.²¹

What we’ve heard: Susi Pudjiastuti submitted a leave request to President Joko “Jokowi” Widodo in February to avoid a possible political quarrel with other ministers, including Luhut, before the presidential election on April 17.

A source said Susi is fed up with the Indonesian Navy and the Office of Coordinating Maritime Affairs Minister’s lack of support for her ministry program in eradicating illegal fishing. She is also disappointed with the lower number of illegal fishing vessels caught this year, despite the fact that illegal fishing is still widespread in Indonesia. The Navy patrol has become less effective, because many illegal fishing vessels caught by the Navy were released immediately due to intervention from high-ranking officers in Jakarta. The officers also instructed Navy captains to reduce their efforts in tracking down illegal fishing vessels. This situation has made Susi feel constricted.

²⁰ *Koran Tempo*, “Tenggelamkan,” Apr. 2, 2019. P.1, 2

²¹ *Koran Tempo*, “Luhut dan Susi kembali berseteru soal benih lobster,” Apr. 4, 2019. P.2

Nevertheless, this information has finally reached President Jokowi. Upon hearing this information, the President instructed all officials to support Susi's policy in eradicating illegal fishing, and personally asked the minister to postpone her leave of absence. Susi was buoyed by President Jokowi's support and canceled her leave request.

Moreover, data from the Maritime Affairs and Fisheries Ministry show that the number of illegal fishing vessels caught in the last two months has increased. One of the apprehended vessels even had illegal lobster seeds onboard. Now, the only job left for Susi is to make sure auctions do not undermine her efforts.

Caught red-handed twice: A case of KHF 1980

Fishing vessel KHF 1980 was caught red-handed twice by the Illegal Fishing Vessel Eradication Task Force led by the Maritime Affairs and Fisheries Ministry.

1st Capture: In August 2017, the task force apprehended a Malaysian-flagged fishing vessel that did not have a legal permit to operate in Indonesian waters, with four crew members from Thailand and led by Captain Phet Endu.

2nd Capture: In February 2019, KHF 1980 was recaptured for the same reason. The ship had a different crew and captain, with five crew members and led by Captain Winai Bunphichit.

- ➔ KHF 1980 was auctioned by the Belawan State Court in 2017 but recaptured two years later.
- ➔ The case sparked suspicion from the Maritime Affairs and Fisheries Ministry that the auctioning off of illegal ships – first promoted by the Office of Coordinating Maritime Affairs Minister – was a just a smokescreen to maintain illegal fishing activities.
- ➔ The allegation first came out in June 2014. Tempo and the ministry's investigation team discovered that some Indonesian shipowners were just proxies of the real foreign owners.
- ➔ Ever since Susi took office, she has prohibited the operation of vessels that were previously foreign-flagged in Indonesian waters, because many of these ships are still under the control of the previous foreign owners, despite being registered as Indonesian property.

Source: [Koran Tempo](#)

Commentary: RI-Britain sign new FLEGT-VPA agreement

The Indonesian government is optimistic wood exports to the United Kingdom would increase in the coming years following the signing of a bilateral agreement on Law Enforcement, Governance and Trade Voluntary Partnership (FLEGT- VPA) between the two countries last week.

Indonesian Environment and Forestry Minister Siti Nurbaya Bakar and UK Ambassador to Indonesia Moazzam Malik signed the agreement on Friday. According to the minister, the Indonesian wood can enter the UK without a due diligence process even if the country eventually withdraws from the European Union.²²

²²*Bisnis Indonesia*, "Kesepakatan FLEGT: Eksporkayu ke Inggris lebih mudah," Mar. 30, 2019.

<https://tinyurl.com/yy8b593c>

Indonesia signed the FLEGT-VPA agreement with the EU in 2016 but a new agreement would be needed if Britain quits the EU, a process known as Brexit. The UK has endorsed a full replication of the EU's FLEGT in its bilateral FLEGT-VPA agreement with Indonesia.²³

Indonesia's wood exports to the UK comprised 25.5 percent of its total wood exports to the EU. The value of wood exported to the UK has grown to US\$275 million in 2018 from \$132 million in 2013. The ministry's wood marketing and processing director Rudi'ie said the move would put Indonesia in a better position compared to its competitors in the region, namely Vietnam and China. The two countries have been Indonesia's rivals in exporting wood to Europe and Britain particularly.

Insight: The signing of the bilateral agreement on FLEGT-VPA between Indonesia and the UK is a consequence of Brexit. The EU has something like 40 trade agreements around the world that UK companies benefit from and if the UK was to leave the EU without a mechanism in place to preserve them, the UK would have to redo each of the agreements with all partners, such as the FLEGT-VPA with Indonesia.

For Indonesia, replicating the FLEGT-VPA with the UK is important as Indonesia's wood exports to that country comprised 25.5 percent of its total wood exports to the EU. With the FLEGT-VPA, Indonesian wood would be able to enter the UK without going through a due diligence process, which would save Indonesian businesses up to US\$2,500 per shipment to the UK.²⁴

It is not surprising that Indonesia and the UK took a much shorter time to finally agree to sign the FLEGT-VPA, considering that the UK had been involved since the beginning in the FLEGT-VPA negotiations between Indonesia and the EU that took almost 10 years to complete. Indonesia is the first country in the world to issue FLEGT licenses based on its own timber legality assurance system, called SVLK, for its timber products exported to the EU and now the UK, too, to automatically meet the EU and UK's strict legality requirements.

Last year's finding that illegally felled timber from Papua and West Papua enter into the SVLK system is a strong test of its integrity.²⁵²⁶ Nonetheless, the SVLK is not a failure. Rather, the case shows that the system works as intended. As a system that relies on private initiatives, the participation of civil society and environmental groups under the banner of the Independent Forest Monitoring Network (JPIK) is crucial to safeguard the integrity of the SVLK.

It is such an independent monitoring mechanism that keeps the EU and now the UK trusting the SVLK system as the basis for issuing the FLEGT licenses. Therefore, it is important for Indonesia to maintain the integrity of the SVLK so that its wood exports to these two markets would continue to increase.

²³ EUFLEGT, "Indonesia-EU Voluntary Partnership Agreement," accessed on Apr. 1, 2019. <https://tinyurl.com/yyako37g>

²⁴ EUFLEGT, "Indonesia-EU Voluntary Partnership Agreement," accessed on Apr. 1, 2019. <https://tinyurl.com/yyako37g>

²⁵ Mongabay.co.id, "Koalisi temukandugaan pelanggaran 7 perusahaan bersertifikat kayu legal di Papua." 29 November 2017 <https://tinyurl.com/y9et9bj6>

²⁶ Tempo.co, "Mesincucikayuilegal." 21 December 2018 <https://tinyurl.com/y8c88zcv>

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