Indonesian State-Owned Enterprises: The Challenge of Reform

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The Indonesian Government has been struggling to find ways to manage its more than one hundred state-owned enterprises (SOEs). Only in his last administration did the New Order long-time leader Soeharto realize that there must be a concerted strategy to bring out the potential of the SOEs, long known only for being inefficient, mismanaged and cash cows for political groups and individuals. Democratization that came with the fall of Soeharto has brought pressure for reform of Indonesian SOEs. At the same time, however, democratization has also made the reform process difficult as more groups of stakeholders have a say in the process.

Neoliberal doctrine perceives ownership of companies by the state as suboptimal, if not destructive to the companies' value. Therefore, privatization of SOEs is seen not only as a means of generating revenue for the state budget — as that seems to be the primary aim of the Indonesian Government — but also as putting SOEs under market discipline as the driver for efficiency. In many of the privatization processes in Indonesia, the role of foreign parties has been quite significant in acquiring SOEs' shares divested by the Indonesian Government. The main reason is that after the 1997–98 financial crisis, not many big Indonesian businesses — especially the conglomerates most severely hit by the crisis — had the capital to acquire the divested shares.

However, economic nationalism seems to be the dominant theme in Indonesia's response to globalization. Article 33 of Indonesia's 1945 Constitution states that "Sectors of production that are important for the country and affect the life of the people shall be controlled by the State" (sub-para. 2) and "The land, the waters

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and the natural riches contained therein shall be controlled by the State and exploited to the greatest benefit of the people" (sub-para. 3). The above article serves as the main basis for economic nationalists to argue that foreign ownership over certain sectors — such as telecommunication,[1] most obviously shown by the Indosat case — should be limited.

This chapter aims to analyse the condition of Indonesian SOEs, the challenges they are facing in implementing good corporate governance, and the masterplan of the Indonesian Government to restructure, "profitize", and privatize the SOEs. Taking into account political changes and globalization, special attention is given to a plan to set up a national holding company for the SOEs, which would emulate the style of government-owned investment holding companies such as Temasek Holdings in Singapore and Khazanah Nasional in Malaysia. In a strategy that has been mapped out since 1998, the masterplan seems to have made significant progress in 2007, though caution has still prevailed because of political complexities.

It is also important to review the privatization process that took place in 2007 in several SOEs. A number of these privatization cases have used public offerings as the means, making them less subject to nationalistic sentiments compared with strategic sales.

Finally, it is also imperative to highlight leadership change at the helm of the Indonesian State Ministry for State-Owned Enterprises (MSOE). After being shifted from the position of Minister for Communication and Information, Dr Sofyan Djalil is the fifth person to hold the position of State Minister for State-Owned Enterprises within an nine-year timeframe. This chapter begins with a historical brief of the leadership changes and their political implication, especially in relation to the goal to have the MSOE replaced with a national holding company for Indonesian SOEs.

Dr Sofyan Djalil, the Fifth Minister of SOEs in Nine Years[2]

The appointment of Sofyan Djalil in 2007 as the new Minister for SOEs seemed to bring a number of breakthrough decisions with regard to the management of Indonesian SOEs. His statement that newly appointed directors of SOEs would not automatically serve their five-year term, but would be subject to a one-year probationary period instead,[3] was the latest of a string of measures aimed at exerting discipline and work ethic at the SOEs. In accordance with good corporate governance practices (the current central theme of the ministry), these SOE directors would be measured by a set of key performance indicators (KPIs) aimed at boosting

SOEs' performance, known to be poor compared with their private sector peers. The ministry would also seek capable and experienced individuals from the private sector to serve as members of the board of commissioners at the SOEs. These professionals are expected to inject credibility, independence, and professionalism into SOEs by controlling the performance of the directors. However, the idea of hiring experts to the board based on professionalism regardless of nationality still faces nationalistic reservations and has been dismissed as "merely a discourse".[4]

In the area of privatization, the most politically sensitive issue related to SOEs, Sofyan intends to increase the number of SOEs to be privatized from the fifteen planned for 2007.[5] Toll operator Jasa Marga, Bank Negara Indonesia (BNI), and construction company Wijaya Karya were the priorities. Sofyan also said that wherever possible, he would make SOEs into public companies.[6] The government has decided to slash the number of its 139 SOEs into half by 2009[7] through merger, divestment, and liquidation. It also planned to further slash the number to fifty by 2012 and twenty-five by 2015, in what has been dubbed the "rightsizing" scenario. See Table 1.

Many within the circle of Indonesian business and politics do not see these steps as a surprise. First, Sofyan has a strong capital market background. An Acehnese with undergraduate degree in business law, he then went to study at Tufts University, Massachusetts, obtaining two masters degrees — in public policy and law and diplomacy — and a Ph.D. in international financial and capital market law and policy. Following that, he has been a professional, managing his own consulting firm and advising various SOEs on issues related to good corporate governance, and an academic, teaching at various universities. In short, he is equipped with the right training and experience for the job.

TABLE 1
Indonesian SOEs Rightsizing Scenario

Year	*Number of SOEs*
2006	139
2007	102
2008	87
2009	69
2012–2015	50
>2015	25

Source: MSOE 2007.

Secondly, he is one of the few non-politicians in President Susilo Bambang Yudhoyono's Cabinet. Out of the thirty-six ministers in the current Cabinet — dubbed the United Indonesia Cabinet to reflect the nature of coalition across various political parties — only about a third are not from political parties, and Sofyan is one of them. This is a significant factor to consider, especially for the post of Minister for SOEs. It is well known that SOEs — not only in Indonesia — are potential cash cows for political parties facing elections. Having somebody from outside a political party is therefore important.

However, it remains unclear whether Sofyan, despite not being a member of any political party, enjoys the support of political parties, which can be seen as a double-edged sword. Without the support, the minister might not be able to get key policies, such as privatization, through Parliament, a necessity in Indonesia's contemporary multiparty democracy. However, political party support can also be perceived as a negative factor for a Minister for SOEs, as the person is expected to be neutral in maintaining principles of professionalism in managing the SOEs. The case of Sugiharto[8] whom Sofyan replaced — who actually had the backing of political parties but finally had to be replaced when the parties deserted him — serves as an important reminder of the mixed blessing of party backing.

Sofyan's actions so far are not seen as a surprise since he was one of the deputy ministers under the pioneering Minister for SOEs, Tanri Abeng. In fact, the masterplan for SOEs to be put under a holding company was first prepared by Tanri, with Sofyan as one of his right-hand men, especially tasked with the issue of socialization and communication.[9] Tanri Abeng — someone who has many years of professional experience with multinational companies but relatively little political flair — was appointed as the Minister for Empowerment of SOEs in the short-lived last Soeharto Cabinet in 1998. His initial main task was to find ways to unlock the potential and value of SOEs, which were seen by Soeharto as the last resort to pay Indonesia's mounting foreign debt.[10] Tanri stayed on for another term under Habibie's Cabinet after the *reformasi* wave that ended Soeharto's term of thirty-two years as the longest-serving leader in Southeast Asia. The masterplan for setting up a holding company structure to manage the SOEs was prepared with the help of a number of consulting firms.[11]

Thus, Sofyan is expected to continue implementing the masterplan and to be committed to it. The three SOE ministers that came in between them — Laksamana Sukardi, Rozy Munir and Sugiharto (see Table 2) — were either too distracted with heavier politically loaded agendas, or simply not too fond

TABLE 2
Indonesian State Minister for SOEs: Chronological Changes

No.	*Name*	*Year*	*Presidency*
1.	Tanri Abeng	1998–1999	Soeharto (March–May 1998) B.J. Habibie (May 1998–October 1999)
2.	Laksamana Sukardi	1998–2000 2001–2004	A. Wahid (October 1998–April 2000) Megawati (July 2001–October 2004)
3.	Rozy Munir	2000–2001	A. Wahid (April 2000–July 2001)
4.	Sugiharto	2004–2007	SB Yudhoyono (October 2004–May 2007)
5.	Sofyan Djalil	2007–	SB Yudhoyono (May 2007–)

of the masterplan.[12] That made continuity of the ministry's policy difficult to sustain. Political changes can always happen beyond a five-year timeframe or even before, reminding us that we should not be too excited yet about Minister Sofyan Djalil's appointment.

Three-Step Strategy of Restructuring, Profitization and Privatization of the SOEs

When appointed as the State Minister for Empowerment of SOEs by Soeharto in 1998, Tanri Abeng outlined a three-step strategy to unleash the potential of Indonesian SOEs: restructuring them, making them profitable, and privatization. In view of the huge foreign debt Indonesia was burdened with, Soeharto thought the SOEs could be used to repay the debts. Soeharto himself tried to conduct privatization, but was only partially successful. It was against this backdrop that Tanri was tasked to lead the new ministry. However, Tanri had preferred a national holding company for the SOEs rather than a new ministry. The lack of legislation to regulate such a holding company forced him to opt for this second-best option, something that has proven to be part of the problem in managing SOEs.

Out of the three steps in the strategy to restructure-profitize-privatize the SOEs, it was obvious that privatization was the most difficult step. One contributing factor was the state of the capital market. Privatizing a company through public offering was certainly not an easy task when the capital market was not in good shape. In the case of Indosat's privatization, which drew the biggest public outcry, it was obvious that the strategic sale was done because of the bearish condition of the Jakarta Stock Exchange.[13] Another factor was nationalistic sentiment. Despite efforts by Sugiharto to emphasize that the goal of privatization is distribution of share ownership[14] and not "selling off state assets", it was difficult to change public opinion that privatization creates a likelihood that strategic sectors of the economy will fall into the hands of foreign parties, a politically sensitive issue in Indonesia. The issue would always cause controversy because of the diverse and sometimes conflicting interests of stakeholders, including the government, employees, investors, and the public.[15]

Apparently with this in mind, after his appointment as Minister in 2004, Sugiharto mentioned that privatization should only be the last resort, mainly to cover the deficit of state budget. This was also backed by the statement of Vice-President Jusuf Kalla that selling government stakes in SOEs was the "lowest priority" for the government.[16]

However, in 2007, the government seemed to reverse this stance and targeted to gain 3.3 trillion rupiah (about US$350 million)[17] from privatization. Of this money, about 1.3 trillion rupiah was intended to be reinvested as capital placement in eight bleeding SOEs in need of more capital, including national carrier Garuda Indonesia, while the remaining 2 trillion rupiah would go to the state coffers. Up to fifteen SOEs were on the table for the privatization plan,[18] as outlined in Table 3.

Starting from 2008, funds generated from the privatization programme will not go to the state budget, but instead will be reinvested to finance the growth of SOEs.[19] This is a positive signal for Indonesian economy for two reasons: it means that the fiscal balance is getting better, and privatization is perceived as a means to improve performance of SOEs. In 2008 privatization is predicted to contribute only about 1 trillion rupiah (about US$110 million).

Out of the above, there is potential for backlash in the case of Garuda. The airline is regarded as a national icon, despite the tragic accident of GA200 in Yogyakarta on 7 March 2007.[20] The accident reflected the need for better governance of the company, which was burdened with mounting debt. However, ironically, 2007 was the first year that Garuda was expected to make a profit after incurring losses for the previous three consecutive years.[21]

Lawmakers signalled that they would oppose the sale of Garuda, despite it being in default on a US$55 million principal debt payment due at the end of

TABLE 3
List of SOEs for Privatization in 2007

No.	*SOEs*	*State ownership (%)*	*Planned method for privatization*	*Share to be divested*
1.	PT Jasa Marga (Persero) — toll operator	100	Initial Public Offering (IPO)/ Dilution/Divestment	Gradually up to 49%
2.	PT Bank BNI Tbk — the second biggest state bank	99.12	Secondary Offering (Dilution/Divestment)	Up to 20%, plus 20% of the enlarged capital (state should retain at least 51%)
3.	PT Permodalan Nasional Madani (Persero) — trust funds to develop SMEs	100	Strategic Sales (SS) (Divestment/Dilution)	Up to 30%
4.	PT Wijaya Karya (Persero) — construction	100	IPO/Dilution (issuing new shares)	Up to 35%
5.	PT Industri Soda Indonesia (Persero) — consumer goods	100	Strategic Sales/Divestment	Up to 100%
6.	PT Garuda Indonesia (Persero) — airline	100	Strategic Sales/Dilution	Up to 49%
7.	PT Merpati Nusantara Airlines (Persero) — airline	93.20	Strategic Sales/Dilution	Up to 40%
8.	PT Industri Gelas (Persero) – consumer goods	63.82	Strategic Sales/Divestment	Up to 63.62%
9.	PT Cambrics Primissima (Persero) — textiles	52.79	Strategic Sales/Divestment	Up to 52.79%
10.	PT Jakarta International Hotel Development (JIHD) Tbk	1.3	Over The Counter (through capital market)	Up to 1.3%
11.	PT Atmindo — engineering	36.6	Strategic Sales/Divestment	Up to 36.6%
12.	PT Intirub — tyre manufacturers	9.99	Strategic Sales/Divestment	Up to 9.99%
13.	PT Prasadha Pamunah Limbah Industri	5.00	Strategic Sales/Divestment	Up to 5.00%
14.	PT Kertas Blabak — paper	0.84	Strategic Sales/Divestment	Up to 0.84%
15.	PT Kertas Basuki Rahmat — paper	0.38	Strategic Sales/Divestment	Up to 0.38%

Source: MSOE, 19 February 2007.

2005. Dradjad Wibowo, a senior legislator from PAN (National Mandate Party) who sits on the parliamentary commission in charge of budgetary affairs and who has also shown strong opposition to the ownership of Indosat by ST Telemedia, mentioned that since the country's strategic sectors such as telecommunications, banking, and mining were already controlled by foreign companies, Garuda must not be sold to foreigners. Privatization of six SOEs on the list including Garuda and Merpati, the other state-owned airline, has yet to be approved by the DPR, the Parliament.[22]

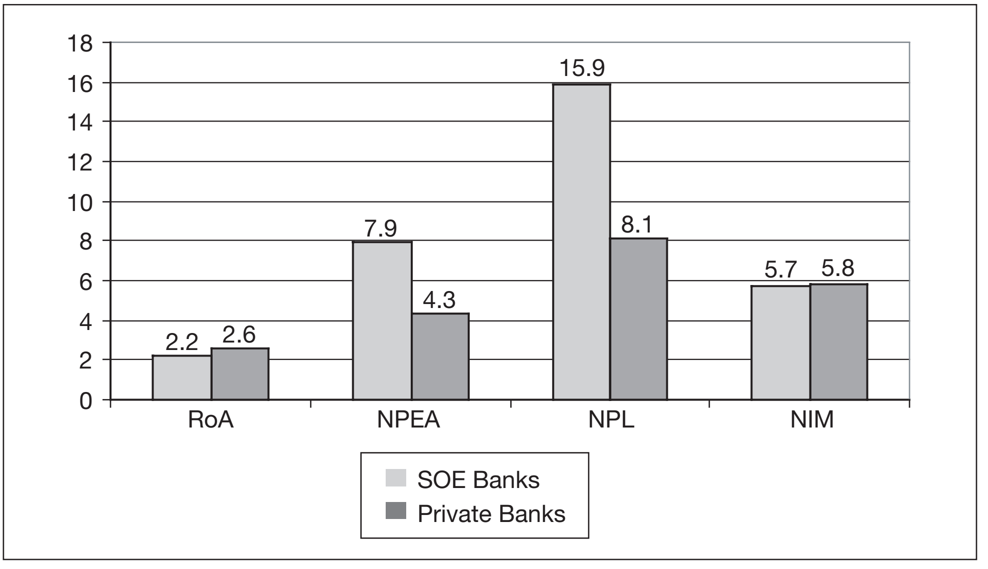
Notwithstanding the glitches, the government managed to push through with privatization of the biggest target, Bank BNI, despite lower gains than expected due to the weakening of the Indonesian rupiah against the U.S. dollar as a result of the sub-prime mortgage crisis in the United States.[23] Toll operator Jasa Marga and construction firm Wijaya Karya, the other big targets for privatization, were successfully privatized in 2007. Jasa Marga's shares were publicly listed on 12 November 2007, and Wijaya Karya was listed on 29 October 2007. In a nutshell, key priorities for privatization in 2007 were successfully achieved, though many of the numerical targets were still unmet because of over-optimism in planning and political and social complexities of implementation

Good Corporate Governance for Indonesian SOEs: Going Beyond Internal Reform

Having ranked poorly in various ratings on corporate governance,[24] it is seen as imperative for Indonesian companies to improve the practice of good corporate governance. This becomes even more important for the Indonesian SOEs, whose total market capitalization of 493.26 trillion rupiah is equal to 40.23 per cent of the total market capitalization at the Jakarta Stock Exchange.[25]

However, performance of SOEs generally lags behind their private sector counterparts. Out of 139 SOEs in 2006, about twenty were making losses amounting to about 2.27 trillion rupiah (close to US$250 million), and 114 were profitable,[26] with total net profit of about 54.42 trillion rupiah (almost US$6 billion). Benchmarking efficiency indicators with private sector counterparts in certain key industries such as banking and plantations showed that SOEs were lagging behind. In the banking sector, state-owned banks showed lower rates of return on assets (ROA) (2.2 per cent, in comparison with 2.6 per cent for private banks) but higher non-performing loans (NPLs) and non-performing earning assets (NPEAs) compared with the private banks as shown in Figure 1.

FIGURE 1
Performance of Indonesian State-owned Banks versus Private-owned Banks
(In percentages)



Note: NIM stands for net interest margin.
Source: Bank Indonesia, November 2006.

In the plantation sector, the performance of the state plantation companies (known as PTPN, with a total area of 1.4 million hectares) showed an improving trend, but it was still lower than key players in the private sector plantation industry such as PT Astra Agro Lestari, which has about 300,000 hectares of land. This is especially true for the upstream business. Table 4 compares the performance of PTPN against Astra Agro Lestari.

In the mining industry, one of the key sectors with state ownership, it can be seen that generally the performance is improving. The performance of state mining firm PT Aneka Tambang (ANTAM) is comparable with that of private nickel company PT Inco Indonesia (INCO). However, both are listed companies. In fact, ANTAM had better return on equity (ROE) and net profit margin (NPM), though it still underperformed INCO in ROA for the year 2005 (see Table 5).

The above comparisons make it imperative for SOEs to embark on a good corporate governance (GCG) programme. Various government laws and regulations[27] have been introduced for the programme, but apparently the devil is more in the detail and implementation than in the letter, not an uncommon occurrence in Indonesia. As Simanjuntak (2006)[28] puts it, the gap between the spirit and letter of

TABLE 4
State-owned Plantation Firm PTPN versus Industry Leader Astra Agro Lestari
(In billion rupiah)

	Astra Agro Lestari			*PTPN*		
Indicators	*2003*	*2004*	*2005*	*2003*	*2004*	*2005*
Net sales	2,543.2	3,472.5	3,370.9	13,136.0	15,404.8	17,906.8
Gross profit	995.4	1,526.0	1,463.4	3,082.7	4,429.4	4,931.9
Operating profit	753.0	1,284.8	1,198.6	1,071.0	1,537.8	2,342.1
Net profit	280.7	800.8	790.4	238.0	581.9	1,196.5
Total asset	2,844.7	3,382.8	3,191.7	14,352.9	16,011.5	18,537.2
Total liability	1,138.1	1,028.3	426.6	7,986.2	9,444.4	11,560.0
Total equity	1,515.5	2,065.3	2,622.6	6,362.8	6,549.6	6,841.6
Operating income margin	29.6%	37.0%	35.6%	29.6%	29.6%	29.6%
Net profit margin	11.0%	23.1%	23.4%	1.8%	3.8%	6.7%
ROA	9.9%	23.7%	24.8%	1.7%	3.6%	6.5%
ROE	18.5%	38.8%	30.1%	3.7%	8.9%	17.5%

Source: MSOE, 19 February 2007.

TABLE 5
State-owned Mining Firm Aneka Tambang versus Private-owned INCO
(In billion rupiah)

	INCO		*ANTAM*	
Indicators	*2004*	*2005*	*2004*	*2005*
Net sales	7,318.1	3,370.9	15,404.8	17,906.8
Gross profit	4,010.2	1,463.4	4,429.4	4,931.9
Operating profit	3,853.1	1,198.6	1,537.8	2,342.1
Net profit	2,624.2	790.4	581.9	1,196.5
Total asset	14,959.6	3,191.7	16,011.5	18,537.2
Total liability	4,389.0	426.6	9,444.4	11,560.0
Total equity	10,570.6	2,622.6	6,549.6	6,841.6
Operating income margin	37.0%	35.6%	38.4%	34.6%
Net profit margin	23.1%	23.4%	28.3%	25.6%
ROA	17.5%	16.4%	13.4%	13.1%
ROE	24.8%	20.9%	33.2%	27.8%

Source: MSOE, 19 February 2007.

the laws and practices is by no means the only obstacle to corporate governance reform in Indonesia, but is clearly the principal hindrance.

A three-step action plan is in place with regard to GCG implementation: socialization, assessment, and review. Socialization of GCG is aimed at creating understanding and preparing SOEs for the implementation of GCG. Assessment of GCG is aimed at identification and evaluation of GCG in SOEs. Review of GCG is an action plan to describe and explain to the public the current state of development and implementation of GCG at SOEs. Out of 139 SOEs, 102 received socialization, 68 had been assessed, and 40 had been reviewed by June 2006.[29] Improvements have taken place; for example, the International Monetary Fund (IMF) indicated in its Country Report 2006[30] that Indonesia has a sound corporate governance framework. However, instances of corporate governance scandals in SOEs such as the one at PGN (Perusahaan Gas Negara), the state-owned gas company,[31] still marred the Ministry's record on GCG implementation. The scandal — reportedly caused by irregularities in its annual report — caused the share price of PGN to plunge 23.32 per cent overnight.

Implementation of GCG is also aimed at eradicating the practice of corruption, collusion, and nepotism (known by its Indonesian acronym KKN or *korupsi*, *kolusi*, *nepotisme*). In the struggle against KKN, GCG uses two approaches: preventive and repressive action. Preventive action is mainly conducted by providing training and workshops on KKN eradication for SOEs managers. Repressive action is focused on urging the SOEs to be more proactive in responding to complaints and reports from the public on indications of corrupt practices. As argued by Hamilton-Hart (2001),[32] such internal reform programmes that aim to improve organizational self-discipline have received much less attention in anti-corruption strategies in Indonesia. The focus has been mainly on moves to introduce monitoring and sanctioning mechanisms that are external to the particular organizations.

It remains to be seen whether such moves would be adequate, because as described in the next section, there is an even more persistent problem in Indonesian SOEs, which lies in the ownership by the state. Wong (2004)[33] argued poor performance in many SOEs — not only in Indonesia — can be attributed to three main challenges facing SOEs' governance in comparison with private sector enterprises. Table 6 lists the differences in governance between private firms and SOEs.

It is against this backdrop that the Indonesian Government developed the masterplan to build a national holding company for the SOEs, along the line of Temasek Holdings in Singapore[34] and Khazanah Nasional Berhad in Malaysia. The holding structure is also believed to be able to serve as a layer shielding

TABLE 6
Differences in Governance between Private Firms and SOEs

	Key Issues	*Private sector firms*	*SOEs*
1.	Objectives	Clear focus on value maximization	Pursue commercial and non-commercial objectives
2.	Agency issues	Single agency; concerned about self-interested behaviour by managers	Double agency; concerned about self-interested behaviour by managers and politicians/bureaucrats
3.	Transparency	High level of disclosure (for publicly listed private firms)	Low level of disclosure

Source: Simon Wong, "Improving Corporate Governance in SOEs: An Integrated Approach", *Corporate Governance International* 6, Issue 2 (June 2004).

SOEs from politics and government intervention. As Wong (2004) has stated, the three stumbling blocks of SOEs' governance are multiple conflicting objectives, political intervention, and inadequate transparency. The holding structure seems to serve the purpose of remedying the first two problems, while transparency can be improved by access of ownership to public.

Indonesian SOE Masterplan: Building a Temasek-style Holding Company

The Indonesian SOE masterplan mainly consists of a restructuring strategy that classifies the SOEs into three categories: stand-alone companies, companies slated for merger, and sectoral holding companies. It is aimed at emulating the success of Temasek Holdings, the investment holding company of the Singapore Government. The sectoral holding companies, with plantation, mining, and cement sectors as the immediate priorities, would then build the foundation for the super-holding company, just like Temasek is the holding company for the Singapore government-linked companies (GLCs).

The main argument for building a holding structure for Indonesian SOEs is strategy alignment and synergy creation. It can be done by knitting various SOEs of different sectors into one strategy, operational or financial, as mapped in Table 7. Economies of scale is another key consideration. Such holding structures would be able to pool resources, lower risks, and provide access to lower cost financing. The Ministry confidently stated that combined assets of Indonesian SOEs can reach US$400 billion to US$500 billion, far bigger than Temasek's US$75 billion and Khazanah's US$20 billion.[35]

The Ministry has also identified five companies as "SOE champions" that can grow and compete globally. They are the plantation holding and mining holding companies, telecommunication company PT Telkom (to be transformed through diversification and growth), national energy company PT Pertamina (through internal restructuring), and state gas company PT Perusahaan Gas Negara (PGN) (through growth). Along with the intention of having only about twenty-five SOEs by 2015 as a result of the "rightsizing" masterplan, having SOE champions is the long-term vision of the Indonesian Government.

The masterplan, announced by Sofyan just a few weeks after being sworn in as the new minister for SOEs, is not something new. It had initially been mapped out under Tanri Abeng's restructure-profitize-privatize strategy. The creation of holding companies has been stated as a priority in the restructuring.[36] Key sectors in this respect are plantations, mining, cement, fertilizer (which already has a holding company, but with performance below expectations) and, depending on the outcome of central bank regulation on ownership,[37] the banking sector. Table 7 shows a review of the development of some SOEs sectoral holding companies.

Plantation SOE Holding Company: The Challenge of Scattered Locations

The holding companies for plantation and mining were expected to be formed before the end of 2007,[38] though there was little visible progress. With assistance from financial advisers Danareksa Securitas and Bahana Securitas, the plantation holding company would aim at value creation by improving capital structure and enhancing financing capacity through the synergy effect of a holding company. One issue remained a potential obstacle: the lack of legal basis for the holding company. The creation of regulations for this was therefore a priority for the government.

There have been critics of the plan to form this holding company. The most prominent critic, Faisal Basri,[39] argued that the plantation holding company would not be effective in improving PTPN's competitiveness because the plantations are scattered across the archipelago. Therefore, expected savings on average cost in the long run would be difficult to achieve, due to differences in soil conditions, social factors and port infrastructure.

TABLE 7
Indonesian SOEs Masterplan: Stand-Alone Companies, Holding Companies, and Mergers

Industry	*Stand-Alone Companies*	*Holding Companies*	*Mergers*
Agro and Consumer	Salt, Soda, Iglas, Bio Farma	15 plantation and 2 fertilizer	2 pharmaceutical, 4 fisheries, and 2 seedlings
Telco and Media	Telkom, TVRI		2 printing companies
Forestry and Paper			5 forestry into 3, and 2 paper manufacturers into 1
Construction		2 cement manufacturers	9 construction into 3, and 5 civil engineering into 2
Mining		4 mining: Bukit Asam, Timah, Aneka Tambang, Sarana Karya	
Logistics	Survey Penas, Pos Indonesia, Jasa Marga, Sarinah, Pengerukan, BGR, VTP, Berdikari, PPI, Sandang, Nusantara, Primisima	4 shipping companies, and 5 industrial areas management	4 ports, 3 surveyors (Sucofindo, SI, BKI), 4 ship industries (DKB, DPS, PAL, Industrial Kapal Indonesia), KAI & INKA (merged)
Energy	Koneba	Pertamina, PLN and PGN	
Travel and Tourism	Garuda, Merpati	3 tourism companies	2 airport companies
Financial services	All state banks, ASKES, Danareksa, PNM, PPA, Kliring		Jamsostek and Jasa Rahardja (merged), Asuransi Ekspor Indonesia and Askrindo (merged), and 5 insurances
Strategic industry	DI, Pindad, Dahana, Boma Bisma Indra, Krakatau Steel, LEN Industri, Inti, Barata		

Source: MSOE, 2005.

Integrated Resource Company (IRC) as Holding Company for Mining SOEs

The holding company for mining SOEs would be formed on the basis of a plan drawn by Citigroup and a local firm as financial advisers. To be named the IRC (Integrated Resources Company), the company would hold shares of the three mining SOEs: PT Aneka Tambang (ANTAM), the metal ores mining company; PT Timah (TIMAH), the tin mining company; and PT Tambang Batubara Bukit Asam (PTBA), the coal mining company. In addition, the plan envisages putting the government's share in Freeport under this holding company to achieve sizeable value.

As in the case of the plantation holding company, the legal basis for the firm has to be prepared by the government, as well as organizational arrangements between the planned holding company and the mining SOEs that would be its subsidiaries.

Faisal Basri also argued against the formation of this holding company, stating that the key to competitiveness would be to reap benefits from the whole value chain of the mining industry — especially in the areas of financing and trade, since this is where the biggest potential value-added will be.

Building a Holding Company for Cement SOEs: Turning Conflicts into Synergy

The cement holding company, which would hold shares of the three state-owned cement manufacturers Semen Gresik, Semen Padang, and Semen Tonasa, has already existed in the form of Semen Gresik as the operating holding company for the three companies, reportedly to be named PT Semen Indonesia.[40] The decision has been approved by shareholders and will be implemented in 2008.[41]

A key goal to be achieved is to reduce potential conflict between the three companies — as shown in the case of pressure for spin-off of Semen Padang from Semen Gresik based on nationalistic and primordial sentiments from interest groups[42] — and increase synergy.

However, issues on tax and commercial and legal implication of the holding company are yet to be resolved.[43] For the moment though, efforts at synergy creation have resulted in improving performance of Semen Gresik in the last two years,[44] with profits almost tripling from 500 billion rupiah (US$55 million) in 2004 to 1.3 trillion rupiah (US$142 million) in 2006.

Holding Company for SOE Banks: Potential Implication of Single Presence Policy (SPP) Ownership Banking Regulation

The holding company for SOE banks might be formed on the basis of a regulation by the central bank that prohibits shareholders from holding controlling stakes in more than one bank. In order to adjust to the new regulation, the central bank has asked banks to consolidate by 2010, either through mergers, acquisitions or setting up a holding company, or through the divestment of their stakes. State banks and private national banks will be affected by the policy, but foreign lenders and joint venture banks will be exempted, in line with international banking practice. This is known as the "single presence policy".[45]

This makes it imperative for the government, which currently owns four banks, to consider the option it should take by 2010. Building a holding company for SOE banks is a plausible option, especially since merging would eliminate the overlapping functions of these banks. Bank Mandiri and Bank Negara Indonesia (BNI) are the two largest lenders by assets. The former aims to position itself as a "dominant multi specialist and regional champion bank",[46] signalling its aspiration to be the lead Indonesian player within the bigger context of the regional market. BNI has the same aspiration, but the government wants BNI to play the role of a development bank.[47] Bank Rakyat Indonesia (BRI) is positioned as a micro-financing bank, with credit portfolio mostly for SMEs, while Bank Tabungan Negara (BTN) focuses on financing low-cost housing mortgages.

However, the implementation of the holding company is currently not the government's priority. Developing growth and improving the health of the banking system severely hit by the financial crisis take priority over the creation of the holding company. For example, lowering the rate of NPLs and improving capital adequacy ratio (CAR) at state banks are considered more important.[48]

Democracy and Yudhoyono's Presidency: Challenge and Opportunity in Managing Indonesian SOEs

The holding company structure as a way to manage "state assets under one roof" is now a global trend. In Southeast Asia, other than Singapore and Malaysia, Vietnam has also recently set up a holding company for its SOEs. It is well understood that Indonesia plans to take the same path. The holding company structure would be the way to build a "sense of corporation" and to minimize the sense of bureaucracy that is prevalent in a government structure like the Ministry for SOEs.[49]

However, it is clearly too simplistic to think that Indonesia can simply follow what Singapore and Malaysia have done in order to transform its SOEs. It is a challenge for Indonesian SOEs to define their role and responsibility in the context of the Indonesian socio-political mindset. The term "Badan Usaha" (profit-making institution) is unfortunately less emphasized than "Milik Negara" (state-owned) in the context of Indonesian SOEs. It is difficult to shake off the assumption that the government — or even other political elites — can interfere in SOEs' decision-making process[50] on the pretext of protecting state interests.

Democratization in Indonesia has become even more important in the context of balancing shareholder value and stakeholder interests. It is not only that the political process has become more participative with higher number of stakeholders, but also that the trade-offs between interests of various stakeholders are more likely. It is imperative for Indonesia to find a balance in managing its SOEs amidst globalization and democratization — with pressure from shareholders to deliver value and with more stakeholders interests needing to be taken into account. The Parliament is a clear example of these stakeholders — dubbed by some as "stakeholders eager to play the role of shareholders"[51] — who often have their say in decisions regarding SOEs. The problem is that decisions regarding SOEs, notwithstanding arguments that they should be commercially driven, have always been political ones.

Take the issue of nomination and appointment of SOE heads as an example. A closed recruitment process within the company's circle is preferred by the government but some parliamentarians argue that a more open and public process is necessary. The government says the enterprises' business interests must be protected, while Parliament insists that all agencies with state money should be subject to public scrutiny.[52]

The masterplan of SOE restructuring to form sectoral holding companies is also subject to scrutiny by the Parliament. Though well intentioned, particularly in view of past experiences of efforts to build holding companies for fertilizers and "strategic" industries that did not yield the expected results, Parliament's involvement with SOEs might have to be limited to a certain extent, especially as the government expects SOEs to act more like autonomous corporations in the future, without the need for a special ministry.[53] Though some might doubt whether it is really the case, the success of Temasek Holdings is due to its principle of running the business from a commercial view point, without political interference from Singapore's Ministry of Finance.[54]

The presidency of Susilo Bambang Yudhoyono can be seen as an opportunity for the SOEs to reform themselves. Having been elected on the platform of fighting corruption, he has urged heads of SOEs to put this high on their agenda.[55] However, he has also said that the government's commitment to wiping out corruption, collusion and nepotism should not make the managements of state firms afraid and hesitant in implementing existing programmes, as such fear would adversely affect the companies` performance.

This is an important statement since there is the general feeling that a heavy-handed anti-corruption drive is the cause of low government expenditure and decreased lending to the real sector, resulting in a lack of development.[56] The president has assured SOE chiefs that SOEs' losses in doing business will not be considered as corruption, unless there is misuse of funds and authority for self-interest.[57] Though helpful, this however might not be sufficient assurance given the fact that corruption charges have become a weapon for political groups to fight each other. He also increased pressure on SOEs to generate profits, telling some to end their record of loss-making performances.[58]

However, he also advised that profits should not be achieved through the use of pressure.[59] This refers to the need to have a level playing field between SOEs and private sector firms with regard to access to financing, marketing of products as well as equitable treatment of shareholders, which are among the principles for corporate governance of state-owned enterprises.[60]

In a nutshell, high hopes seem to have been placed on the leadership of President Yudhoyono and SOEs Minister Sofyan Djalil in transforming Indonesian SOEs into professional and profitable corporations. The masterplan for streamlining the number of SOEs to achieve the "right size" is appropriate, inspired also by the way neighbouring countries manage their government-linked companies. However, caveats need to be put in place due to the higher complexity of decision-making in the context of democratic governance in Indonesia. It remains a challenge for the Indonesian Government to use democratic governance as the basis for good corporate governance of its enterprises.

Notes

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[6] Joe Cochrane, "Indonesia relaunches privatization drive", *Financial Times*, 7 June 2007.

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[9] Author's interview with Tanri Abeng, former Minister of SOEs, 18 March 2007.

[10] "Tanri Abeng: Saya Tidak Rela Menjual Obral BUMN" [Tanri Abeng: I Did Not Agree to Cheap Sales of SOEs], Interview with Tanri Abeng by Eben Ezer Siadari, Agung Widayatmoko, and Alfian Kartim in *Warta Bisnis*, 11 July 2003.

[11] Tanri Abeng, *Indonesia, Inc.: Privatizing State-Owned Enterprises* (Singapore: Times Academic Press, 2001).

[12] Laksamana Sukardi was a politician in Megawati's PDI-P (Indonesian Democratic Party — Struggle), Rozy Munir is an aide of Abdurrahman Wahid from PKB (National Awakening Party), and Sugiharto, though a professional, joined Yudhoyono's Cabinet as a member of PPP (United Development Party) and was later backed by PKS (Prosperous Justice Party).

[13] Author's interview with Laksamana Sukardi, former Minister of SOEs, 24 March 2007, and "Laksamana: Harga di Bawah Rp12 Ribu, Divestasi Indosat Batal" [Laksamana: If the Price Goes Below 12000 rupiah, We'll Cancel Indosat's Divestment], Tempo Interaktif, 20 November 2002.

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[25] Total market capitalization of twelve listed SOEs and two listed companies with government's minority shares [PT Indosat and Bank Bukopin] as of 28 December 2006. Data from MSOE, 19 February 2007.

[26] Five SOEs have not tendered report to the Ministry, data from MSOE on 19 February 2007.

[27] Among others, Law No. 19/2003 on SOEs, Law No. 8/1996 on Capital Market, Law No. 1/1995 on Listed Company, Minister of SOEs Decree No. 117/M-BUMN/2002 on Implementation of Good Corporate Governance.

[28] Djisman Simanjuntak, "Indonesia's Tolerated Low-Speed Reform of Corporate Governance", in *Reforming Corporate Governance in Southeast Asia: Economics, Politics and Regulations*, edited by Ho Khai Leong (Singapore: Institute of Southeast Asian Studies, 2006), pp. 157–79.

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