

# Indonesia

## Archipelago of Opportunity

### Balancing *the* Energy Equation

Indonesia's energy sector is experiencing a steady growth in demand and witnessing a revival in private investment and investor opportunity. How much can be achieved the year before a general election largely depends on the rate the government's new strategy for energy management can be implemented.

As Indonesia moves inexorably closer to becoming the world's seventh largest economy, and its voters to the polling booth, the state owned energy companies and the Ministry of Energy are looking to ensure that subsidies are kept under control and that the nation has a constant energy supply,

"The large number of attendants for tenders shows that Indonesia's investment climate is still attractive for upstream oil and gas investors in the midst of global economic downturn," commented the Minister

of Energy and Mineral Resources, Purnomo Yusgiantoro in his awards announcement of nine oil and gas block tenders earlier in the year.

"This is a big country and transforming it is not simple," says Mr. John Prasetyo of CBA ASIA and KADIN. "What is important is for government to remain consistent and not to create a divide between public and private sectors."

Dr. Setiawan, Director General of Mining and Geothermal, endorses this view, "We don't need to convince people to come to Indonesia for our resources; they already know our potential. The most important thing for us is to have a good policy for investment. We want all sectors

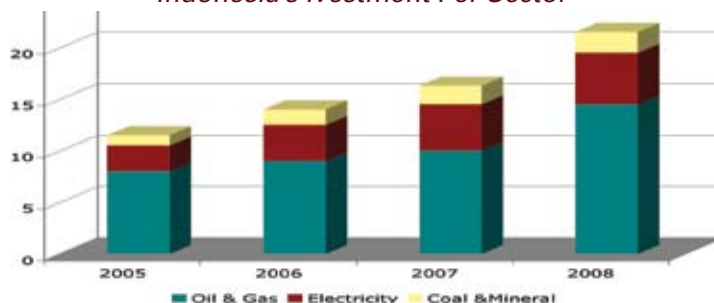
to work hand in hand."

"Oil is still the backbone of our state revenue," says Doctor Evita Legowo, Director General of Oil and Gas, "but our oil reserves are depleted. We have a plan. We can see the milestones and route map for each source of energy. We have a blueprint."

With policy changes and new incentives on the agenda there is a new cohesion of thought within the state energy sector, and the message being sent out to investors is: Come and discuss what you need and we will tell you what our national needs are.

"We have a new finance decree for exploration so, broadly speak-

*Indonesia's Investment Per Sector*



ing, upstream investors do not have to pay tax as well as import duties on their equipment,” explains Dr. Legowo of some of the investor incentives already in place, “This is not only for oil and gas but also for geothermal. Secondly, we need to increase our use of gas and we are working to replace the subsidy for kerosene with a subsidy for LPG.”

#### THE WAY FORWARD

The new energy law commits the government to a National Energy Council. It will have fifteen members, seven from the government and eight from non-government stakeholders. The council will have a mandate to discuss energy

“Indonesians should be very proud of their country, they should be forward-looking and they deserve to have confidence.”  
—John Holmes

policy, update the national energy plan, monitor the implementation of policy for each energy sector, and discuss how all forms of energy will work in unison to keep supply constant.

One target is to increase renewable energy to 15% of the national mix by 2025. Of this, 5% will be bio-fuel, 5% geothermal and 5% from other renewable sources.

“We are in the process of having the production capacity to make bio-diesel and bio-ethanol,” says Purnomo Yusgiantoro, “and their use will be mandatory for the power, industry and transportation sectors.”



← **Dr. Ir. Bambang Setiawan,**  
*Director General of Mineral, Coal and Geothermal, Ministry of Energy and Mineral Resources.*



*Clockwise:*  
**John Holmes,** *Ambassador, Embassy of Canada in Indonesia*

**J. Purwono,** *General Director of Electricity and Energy Utilization, Ministry of Energy and Mineral Resources, Indonesia*



**Dr. Ir. Evita H. Legowo,** *General Director of Oil and Gas, Ministry of Energy and Mineral Resources, Indonesia*

Dr. Setiawan believes increased transparency will further encourage investor confidence. “We are introducing a new Mineral and Coal Mining Bill for greater national control over the issue of licenses and contracts. Companies listed on the stock market must be transparent in their financial reports, but I would like all companies to follow the Extractive Industry Transparency Initiative (EITI),” he says.

Transparency will also ease anxieties in the minds of voters. According to Mr. Purwono, Director General for Electricity, there is one

very simple way to do that. “Our number one task at PLN is to keep the lights on,” he says.

With the energy sector hard at the work of reform, John Holmes, Ambassador for Canada in Indonesia, feels that now is the time for Canadian investors to act. “What I am saying to Canadian companies in the energy sectors is to investigate the market now,” he says “because the government of Indonesia wants to accelerate its reforms, and when these changes happen, there will be flood of investors from other countries.” ●

# PGN DOESN'T MIND THE HEAT

Looking at investment in the Indonesian energy sector is deficient without a thorough look at Perusahaan Gas Negara. PGN is the state-owned gas utility that buys natural gas from reliable upstream suppliers at long-term fixed rates. The company also transports gas through its own transmission pipelines to Indonesia's primary energy companies and to Singapore.

PGN is exploring plans to buy liquid natural gas (LNG), and process coal bed methane (CBM) to augment its present natural gas supply, and to develop compressed natural gas (CNG) business.

PGN also manages 91% of the distribution of natural gas to industrial, commercial, and household users within Indonesia. The CEO of PGN is Hendi Priyo Santoso, formerly of JP Morgan and Citigroup. "I joined PGN because the company has a major part to play in the future of Indonesia. We have one of the largest proven natural gas reserves in Asia, and are probably the largest exporter of LNG globally. The country ought to be more gas reliant as gas remains a key commodity that Indonesia can manage well," he says.

Mr. Santoso's recent shift from the banking sector to the energy sector has come at a time when viable oil resources are in decline, coal is becoming more expensive, and clean energy such as gas and renewables are ready to step up to the plate. "Three years ago coal was cheap but with the recent volatility in the price of crude oil, it is now in global demand and its price reflects this demand. Coal is also mined in difficult landscapes and its transport in Indonesia is a logis-

tical nightmare. As for oil, Indonesia's crude production continues to decline. We need to accelerate the conversion of oil-based consumption to natural gas."

As a listed blue chip company, PGN is confident it merits its top-four position of state-owned companies in Indonesia. It has a clean bill of health from its auditors, one of the "big four" auditing firm, and is comfortable with the transparency of its operations. Now, the Company's number one priority is to further its commercial viability. "Our future growth is based on the gas fields in South Sumatra and we have built a pipeline to connect Java with South Sumatra. We are also exploring the plan to build a LNG receiving and re-gasification plant in Java, jointly with several major energy sector companies in a consortium, to ensure continuity of supply and that we have the capacity to receive LNG and convert it back to natural gas," says Mr. Santoso.

Burning gas in an electricity generating turbine is an efficient process and PGN have used this advantage as leverage to broker a new supply agreement with the government-owned electricity provider PLN. "PLN used to be burning diesel for some of its power

plants, at a cost many times higher, in terms oil price and energy efficiency, than gas," say Mr. Santoso. "Now we can help PLN saves more than \$2 billion annually."

PGN is robust and ready to play its part as one of the key foundations for Indonesia's continuing transition to full development. ●

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—Hendi Priyo Santoso



# We are

expanding our share in the growth of the natural gas market  
while positioning ourselves to continue leading the industry in Indonesia



# PGN

Growing with the Nation

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# PEOPLE ARE THE PRIORITY

Indonesia has the greatest geothermal energy potential in the world—an abundant source of clean, sustainable energy to complement its hydrocarbon reserves.

“We are significant niche players in oil and gas,” explains Bret Mattes, the relatively new CEO of Star Energy, who has a background in oceanography, and is an experienced economist and businessman in the field of oil and gas exploration.

Star Energy has a 31.25% interest in the Kakap PSC, producing oil and exporting gas to Singapore, and a 100% interest in the Banyumas PSC drilling exploratory wells. At Sebatik, the company holds a 75% interest and it recently won Sekayu PSC in central southern Sumatra, with oil and natural gas potential and coal seam methane development under an agreement with Shell.

“Our policy has stood us in good stead, but now we want to be initiators, we want to develop projects and stand out in our second line of attack, which is geothermal.”

Star bought its geothermal asset Wyang Windu in 2005 and has since doubled capacity and is looking to triple it by 2011. “This is the single best steam field that has ever been used,” says Mattes, “The geothermal industry here is terrific.”

The Government wants growth in geothermal to rise from 3-5% of the primary energy mix. Geothermal is virtually free of any green house gas emissions. It is expensive to install but as an infinite natural resource, becomes progressively cheaper. One of the major capital costs is that a lot of wells must be drilled to get enough steam into the turbine.



**Bret Mattes,**  
*CEO of Star Energy*

Star’s expansion into geothermal is well in line with its commitment to a strong environmental policy. As one of a handful of companies holding both ISO 14001 and

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—*Bret Mattes*

OHSAS 18001, Star is well aware of obligations for sustaining the future of the country through its “green” practices.

Thanks to the excellent groundwork established by the previous CEO, Supramo Santosa, Star Energy continues to work with the government to reduce red tape and improve the climate for acquiring new exploration acreage.

Says Mattes: “I think the guys that started this company had a great vision. What is really focusing people’s attention now is not only Star’s corporate responsibility but also our social responsibility and environmental management.”

The Indonesian government awards best environmental practice, and recently, Star Energy became the first company in Indonesian history to receive the highest accolade. They were awarded the Gold PROPER award for its Kakap operations and their efforts in education improvement specifically in the area of healthcare for local communities.

Auditors Goldman Sachs and Ernst & Young have predicted that Indonesia will move up the world economic rankings provided it can get its health and educational package right.

“We are getting Star involved as a sponsor of certain things even though there is no real commercial gain for us to do that,” explains Mattes, “Things like educational infrastructure, places of worship, improved health and sanitation, small business development and recreational opportunities.”

The Company has a straight talking, foreign CEO, but it is an Indonesian company at its heart, here to stay, and developing better solutions for the future. ●



Only one company in Indonesia  
has ever received a gold PROPER award  
and a gold PADMA award  
for environmental protection and  
commitment to community development...



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## THE CLEAR challenge AHEAD

Government-owned PLN is the only downstream provider of electricity to 37 million customers in Indonesia. It also controls the upstream energy mix that supplies its electricity.

"This is very challenging for me," says Fahmi Mochtar, President Director of PLN. "We are facing a dilemma of status between public service obligations, versus business opportunity, versus commodity."

At present, 34% of powered production comes from oil power plants and 41% from coal powered plants.

"We want a major reduction in our reliance on oil. Coal will increase due to the on-going 10,000MW project, and we want more power to be supplied by renewables, that is hydro, wind, and solar cells as well as geothermal."

To this end, PLN has a new financial roadmap and bureaucracy is being reduced. "There is more confidence in Indonesia now, and we need our partners to work with us," Mochtar explains.

PLN currently purchases 4,200MW of electricity from independent partners but has raised the ceiling to a potential of 26,000MW as it edges towards a greener future agenda while meeting its current obligation to supply affordable electricity. ●



## ADARO – DIGGING IN

Adaro Energy is currently Indonesia's second-largest thermal coal producer, operates the largest single coal mine in Indonesia, and is a significant supplier to the global seaborne thermal coal market. The company has approximately 2.8 billion tons of coal reserves and resources and is integrated from exploration through to marketing. The company's vision is to be the most efficient, integrated coal mining and energy company in South East Asia.

Adaro began marketing its sub-bituminous coal in 1990, and today the coal is widely known around the world under the trademark "Envirocoal" because of its unique environmental qualities. Marketing

"I think our vision is responsible. We want to be the most efficient in all ways".  
—Garibaldi Thohir

efforts were first focused in Europe and the U.S. where regulations limiting the emissions of coal-fired power plants had been introduced. Soon thereafter, the company focused its attention on Asian markets taking advantage of the geographical proximity, which lowers transportation costs for customers.

The majority of Adaro's coal is supplied directly to end-users and the rest via trading firms. The company has 40 customers, which are mostly high quality power utilities, located in 18 countries.

The demand for Envirocoal is strong and all of Adaro Indonesia's planned production for the fourth quarter of 2008 and 2009 is already contracted under term coal supply agreements. In the third quarter

of 2008, Adaro entered into three new long-term coal supply contracts with international customers to cover the increased production planned for 2009.

Adaro Energy will continue expansion plans to boost production to 42-45 million tons in 2009. The company or its contractors had prepared over 90% of the necessary equipment (including equipment which has yet to be delivered) and associated funding.

However, given the current economic slowdown, the company's focus is on consolidating core business and preserving shareholder value. Says Adaro's President, Mr. Garibaldi Thohir: "Until we can properly assess the full impact of the financial crisis, we are going back to basics, focusing on our core business, and preserving cash, with a view to keeping the operations running on target to meet our volume and revenue goals. We are on track to produce 38-39 million tons of coal this year."

Due to the difficult credit conditions, the board of directors decided to temporarily suspend work on the financial aspects of Adaro Energy's expansion plans. However, Adaro Energy is on target to have infrastructure in place for 2009 and 2010 growth plans. For 2011 and beyond, the company is reviewing how to best achieve growth targets. Adaro Energy remains confident of the fundamentals of the expansion plans and the long term targets remain the same.

As for corporate social responsibility, Mr. Thohir says, "It is one of our major strengths. We have mobile clinics that go out to villages and perform operations. We also promote health care, education, and social programs. Without this hard-earned social acceptance from the communities in the vicinity of our mines we could not operate or expand." ●