ISEAS YUSOF ISHAK INSTITUTE

ISSUE: 2021 No. 63
ISSN 2335-6677

PERSPECTIVE

RESEARCHERS AT ISEAS – YUSOF ISHAK INSTITUTE ANALYSE CURRENT EVENTS

Singapore | 5 May 2021

Indonesia's First Sovereign Wealth Fund (INA): Opportunities and Challenges

*Manggi Taruna Habir**

The Indonesia Investment Authority (INA) will initially focus on attracting private investment into key infrastructure sectors such as toll roads, seaports and airports. In this picture, this aerial picture shows a light rail transit (LRT) station (L) undergoing construction in Jakarta on March 25, 2021. Picture: ADEK BERRY, AFP.

** Manggi Habir is Visiting Fellow with ISEAS – Yusof Ishak Institute.* *The author would like to thank the three presenters from the ISEAS webinar on 10 March 2021 - Mr Anton Gunawan, Dr Reza Y. Siregar, and Dr Darwin Cyril Noerhadi, - for sharing their ideas and for permission to use their presentation materials for this essay. The usual caveat applies.*

ISSUE: 2021 No. 63
ISSN 2335-6677

EXECUTIVE SUMMARY

- The Indonesian government is stepping up its efforts to kickstart its economic recovery by attracting more direct investment into the country. The 2019 Omnibus Law and the recent launch of the Indonesia Investment Authority (INA), the country's first sovereign wealth fund, are deliberate steps in that direction.

- INA is largely modelled after India's SWF. It is primarily a government-owned fund for attracting external co-investors into Indonesian entities and projects.

- INA will initially focus on attracting private investment into key infrastructure sectors such as toll roads, seaports and airports.

- If INA succeeds in its initial co-investor role of luring investment into expanding Jokowi's infrastructure projects, the government should consider broadening its role to become a more traditional SWF.

- The original objective of creating a holding company to protect SOE's from political influence, through increased transparency and accountability, is critical to the improvement of strategic SOE's operating performance and competitiveness.

ISSUE: 2021 No. 63
ISSN 2335-6677

INTRODUCTION

On 19 April 2021, Indonesia's State-Owned Enterprise (SOE) Minister, Erik Thohir, announced regulations that would determine the criteria and process for the sale of SOE assets to the country's newly established sovereign wealth fund (SWF), the Indonesia Investment Authority (INA). Such asset sales effectively pave the way for SOEs to alleviate their debt burdens. Large state-owned construction companies are expected to sell some of their toll road projects to INA and its co-investors. The latter include Hutama Karya (Trans-Sumatera project), Jasa Marga (North Sumatera, Java, East Kalimantan, North Sulawesi and Bali projects) and Waskita Karya (West, Central and East Java projects).[1] The announcement also brought some clarity to the future operations of INA.[2]

This essay seeks to explain the origins, goals, organisation and operational challenges of INA. It traces the events leading up to its establishment, and follows that up with a discussion of INA's objectives, organisation, and governance structure. The final section will examine some challenges involved in the implementation of the Omnibus Law as well as INA's ability to attract much-needed investments amid an evolving Covid-19 pandemic.

INDONESIA'S MUCH-DELAYED SWF PLAN

The idea to set up a sovereign wealth fund in Indonesia is not new. An early initiative was undertaken during the last years of the Suharto government when, on 16 March 1998, a new SOE Ministry was established with Tanri Abeng as its first minister.[3] That ministry was given oversight over all SOEs. Tanri, who had been a senior executive for Union Carbide's Indonesian operations and was later CEO of the Bakrie Group, was one of the first professionals from the private sector appointed to a cabinet minister position. The plan was to classify SOEs into groupings, each with its own holding company. A super holding company would then be formed to oversee all these holding companies.[4] However, the plans never materialised in the aftermath of the 1997/98 Asian Financial Crisis or after the Reformation Era.

With subsequent governments, from the Habibie to Yudhoyono administrations, the SOE structure remained largely the same, except for the formation of a few sectoral holding companies and the privatisation of several commercially-oriented SOEs through Indonesia's stock market.[5] This relative absence of SOE reforms could have been due to strong opposition from various stakeholders. SOE workers have been worried about layoffs due to such reforms. SOE management and supervisory bodies are concerned about their positions in a potential rationalising and merger exercise. Suppliers and distributors who are part of the SOE ecosystem also do not want reforms that affect their role in the SOE supply chain. Bureaucrats are also protective of their turf, especially the technical ministries that oversee each their related SOEs. Finally, elected politicians are also concerned that SOE reforms will reduce the benefits enjoyed by their constituencies under the current arrangement.

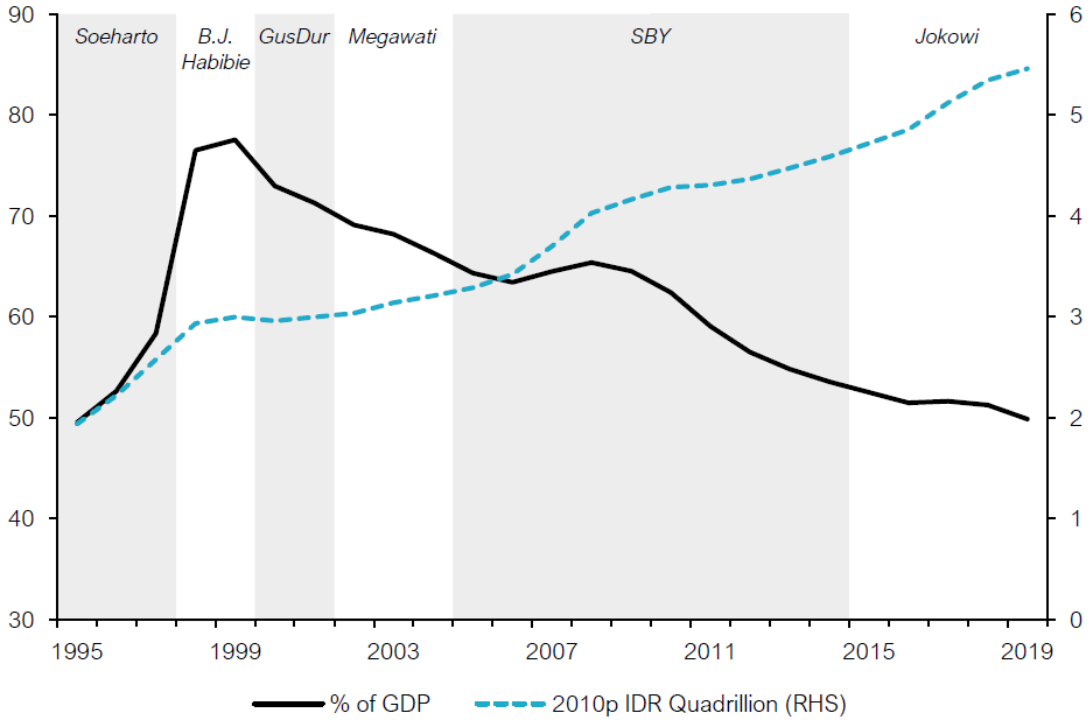
Despite the opposition to SOE reforms, Rini Soemarno – the SOE Minister during President Joko Widodo's (Jokowi) first term (2014-2019), began to revisit the earlier idea of a SOE super-holding company, and began forming more sectoral holding companies. By the end of Jokowi's first term, six sectoral holding companies had been formed and there were plans for seven more.

ISSUE: 2021 No. 63
ISSN 2335-6677

The plan to form a super holding company was however subsequently abandoned by Erik Thohir, who replaced Rini Soemarno as the SOE Minister in Jokowi's second term. Instead, the minister decided to just focus on completing the formation of sectoral holding companies.

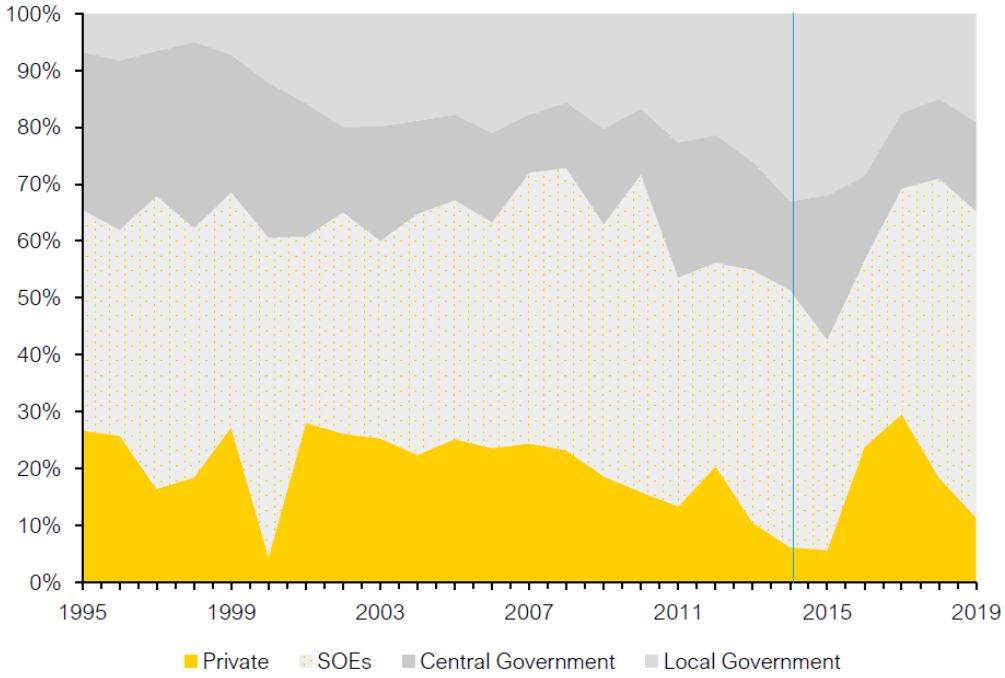
An important factor influencing the trajectory of SOE reforms is infrastructure investment. During Jokowi's first term, the government spent heavily on building infrastructure by recapitalising the construction SOEs and having them raise funds for infrastructure construction. The President realized that to attract private investments, he needed to improve the country's much neglected infrastructure. For example, Anton Gunawan (2021) showed that although the nominal value of capital stock increased over time, infrastructure stock as a percentage of GDP has been declining since 1999 (**Figure 1**). He also argued that much of the spending on infrastructure were primarily undertaken by the SOEs (**Figure 2**) and funded primarily through debt. Furthermore, the debt-to-equity position of many of these companies has risen significantly between 2014 and 2019 (**Table 1**).

Figure 1: Infrastructure Capital Stock in Indonesia



Source: Gunawan (2021)

Figure 2: Infrastructure Investment Flow by Source



Source: Gunawan (2021)

Table 1: Debt-to-Equity Positions of SOEs

Company	Debt-to-Equity (%)		
	2014	2019	Δ%
Waskita Karya	114.4	**243.4**	112.8
Jasa Marga	121.0	**185.2**	53.1
Hutama Karya	124.9	**182.6**	46.2
Adhi Karya	138.3	**154.0**	11.4
Pelabuhan Indonesia III	101.6	**127.0**	25.0
PP	132.7	**95.5**	-28.0
Wijaya Karya	62.2	**78.5**	26.2
Perusahaan Listrik Negara	222.0	**48.9**	-78.0
Telekomunikasi Indonesia	27.3	**44.4**	62.6

Source: Gunawan (2021)

The rising trend in SOE debts, which began in Jokowi's first term, has clearly become a major concern in the second term, with the SOEs' debt-to-equity ratios having reached potentially unsustainable levels. More recently, this problem was further exacerbated by the impact of the Covid-19 pandemic on the Indonesian government's fiscal space. The government has reoriented fiscal expenditures to deal with the pandemic. It will also need to reduce its budget

ISSUE: 2021 No. 63
ISSN 2335-6677

deficit going forward. Under these circumstances, and with SOEs involved in infrastructure projects having reached their debt limits, there is an urgent need to attract private investments (both local and foreign) to fund the country's neglected infrastructure in the future.

In this regard, Indonesia had before the pandemic already implemented some reforms to increase private investment. Reza Siregar (2021) notes that during Jokowi's first term, the government launched 16 policy reform packages to attract private sector investment. Even though this was done piecemeal, Indonesia was able to climb up the World Bank's "Ease of Doing Business" rankings by 30 positions to 73rd position last year. The packages were followed by a landmark fuel subsidy reform in 2015. Overall, these reforms were designed to streamline regulations, support private investment, and make wage setting more flexible.

During Jokowi's second term, the government began to realise that the piecemeal approach adopted in the past to attract private investment was inadequate. Thus, it embarked on designing and issuing a major bill that would consolidate, harmonise and simplify the country's unwieldy, and often conflicting and overlapping, investment laws. This bill, with an all-encompassing coverage, was called the Omnibus Law which was passed by parliament on October 8, 2020. The new legislation consists of 79 laws and 1,245 articles. It focuses on four essential areas: (i) ease of doing business, (ii) simplification of investment requirements, (iii) strengthening the labour market's competitiveness, and (iv) boosting micro, small and medium enterprises. These four areas are further divided into 11 clusters.[6] One of the clusters – the Investment and Government Project cluster – includes the plan to set up the Indonesia Investment Authority.

INVESTOR-FRIENDLY AND FLEXIBLE

The main goal of the Indonesia Investment Authority (INA) is to attract private investment into the country. In the early phase, INA's priority is to attract private investments into the government's infrastructure projects. In a sense, the role envisaged for INA is more limited compared to the earlier idea of establishing a super-holding company for SOEs in the country.

Dr Darwin Cyril Noerhadi (2021), a member of INA's Board of Supervisor, explained that INA is modeled more closely to India's National Investment and Infrastructure Fund (NIIF). This makes it different from SWFs from countries such as Singapore and Norway (**Table 2**).

In general, SWFs invest their country's surplus funds or reserves overseas to diversify and grow their assets. INA, in contrast, is more inward-looking, and builds on the government co-investing with private investors (local and foreign) in Indonesia-based projects or entities.

Funding for SWFs in general comes from internal surpluses or from the country's reserves, while INA's funds, as with NIIF, may come from government surpluses, but also from foreign co-investments into local companies and projects.

ISSUE: 2021 No. 63
ISSN 2335-6677

Table 2: Comparisons of Sovereign Wealth Funds in Norway, Singapore and India

Dimension	Norwegian Oil Fund (NOF), Norway	Government of Singapore Investment Corporation (GIC), Singapore	National Investment & Infrastructure Fund (NIIF), India
Fund Size	USD 1,099 Bn	USD 440 Bn	USD 3 Bn
Source of Funds	Internal (Oil Revenues)	Internal	Internal + FDI
Investment Objectives and Criteria	• Financial returns • Focuses primarily on listed entities, equities and bonds) globally outside of Norway • Wealth creation / preservation for future generation(s); also when needed to support government budget during time of needs	• Financial returns • Focuses on publicly listed companies' long-term investments • Multiple asset classes: global equities, bonds, private equity and real estate	• Financial returns and inviting FDI • Focuses on long-term sustainable infrastructure development (wide range of infrastructure sub classes)
Entity and regulatory Framework	• Established via Government Petroleum Fund Act (by Storting / Norwegian parliament) • An entity under the Norwegian central bank	• Established through Singapore Companies Act, 1981 • Reserve management entities other than Monetary Authority of Singapore (MAS) and Temasek	• Trust form co-investment by Government of India and private (Global and domestic) funds • Supervised by MoF

Source: Noerhadi (2021)

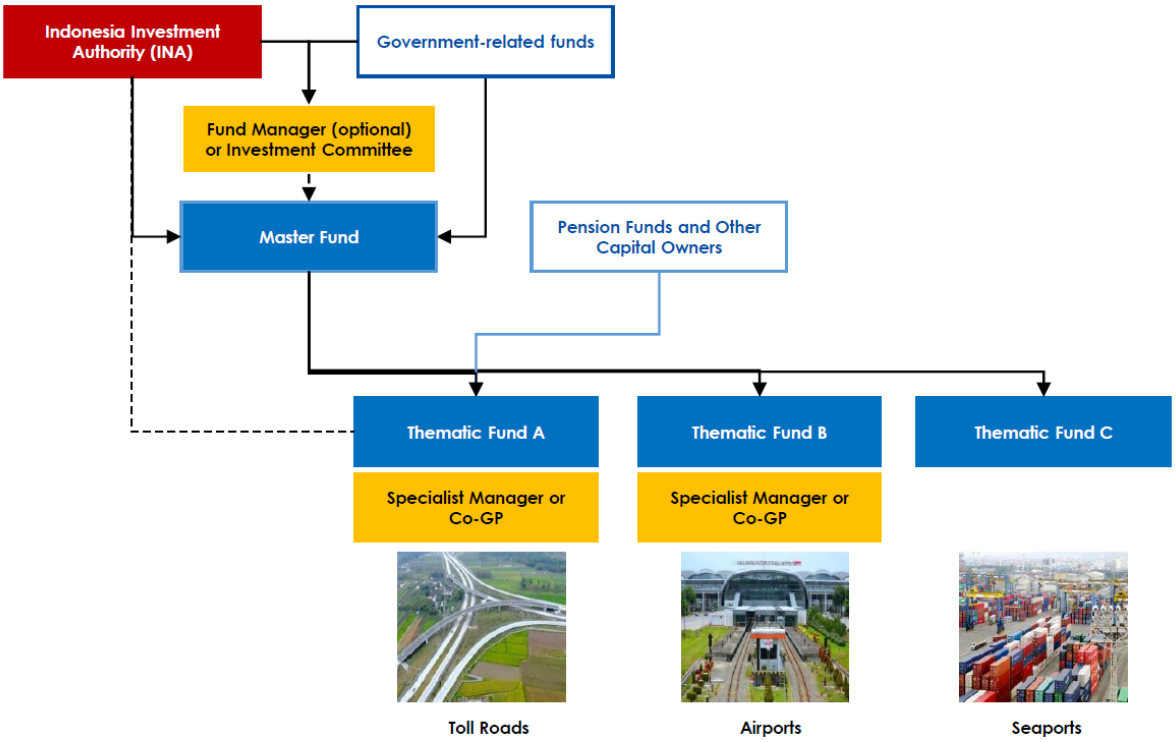
The investment objectives of SWFs are similar when it comes to financial or commercial returns. However, the focus can be different across SWFs. For the usual SWF, the emphasis is on wealth creation done through investing in a diversified portfolio of assets, both domestic and overseas. In contrast, INA and NIIF focus on attracting external funds for domestic infrastructure projects.

As a result, INA's features are designed to be investor-friendly and flexible, with a focus on commercial returns. Similar to private companies in Indonesia, INA has a two-tier board governance structure, comprising the Board of Directors (Management), which is overseen by the Board of Supervisors. This Board of Supervisors reports directly to the President. The five-person Supervisory Board consists of the Minister of Finance and the Minister of State-Owned Enterprise (SOE), and three professionals from the private sector. The current Board of Directors consists of five independent professionals selected and vetted by the Supervisory Board to run the SWF.[7]

Under the 2020 state budget, a total of IDR15 trillion has been allocated as INA's capital. Another IDR 15 trillion will come from the 2021 state budget. The plan is to boost INA's total capital to IDR 75 trillion by 2021 year-end. This is expected to come from various sources, ranging from cash funds, state property to government shares in SOEs.

Noerhadi (2021) has noted that the initial co-investment activity will focus on infrastructure projects such as toll roads, airports, and seaports. One possible investment participation structure involves the creation of an INA-managed master fund that is further split into designated thematic funds for co-investment with interested participating investors (**Figure 3**). Investors wanting control over their investments would take a majority share, with INA taking a minority stake. To ensure flexibility, the location and jurisdiction of these co-invested funds could reside in Indonesia or abroad, depending on the investors' preference.

Figure 3: An Example of INA's Co-Investment Fund Structure



Source: Noerhadi (2021)

CHALLENGES AHEAD

The Omnibus Law has thus far attracted more street protests than investments, however: Labour unions have opposed this new bill especially on the reduction of severance pay terms; environmental groups are not happy with the less stringent environmental protection; and provincial governments are questioning the shift of authority on investment licenses to the central government. The implementation of the law will remain a challenge since it is opposed by the above three important constituents.

INA's ability to attract investments into toll roads, seaports and airports will indeed be tested in the second half of this year. Only after INA has delivered on what it set out to do in this area will consideration be given to broadening its role to a holding company of strategic SOEs. Some will consider it a pity if this does not materialise, given the country's long and arduous 20-year journey to set up the SWF.

However, INA can become unwieldy and costly if it becomes a super holding company of all SOEs (through their sectoral holding companies). It might be preferable for INA to be a more focused holding company for selected strategic SOEs, especially those that would benefit from heightened transparency and accountability, similar to the existing 28 publicly-listed SOEs.

A public listing would improve transparency and accountability, allowing managers to better focus on operating efficiency and performance with less political interference.The government's perennial concern over control, could be addressed by the maintaining of majority ownership and through special voting-right shares.

In a recent interview, Tanri Abeng opined that a holding company is essential to protect the SOE from political influence.[8] The current SOE Deputy Minister, Pahala Mansury, has mentioned that, in addition to the toll roads being sold by the state-owned construction companies, several SOE subsidiaries are being planned for sale to INA before or during an IPO public listing. These include PT Pertamina Geothermal Energy (a subsidiary of PT Pertamina) and a sub-holding company covering marine logistics.[9] It would be interesting if INA can also help bring about the public listing of PT Pertamina (Persero).

References

Gunawan, Anton. (2021). "Tapping Private Investment with SWF: Indonesian Investment Authority", presentation at ISEAS – Yusof Ishak Institute, 10 March.

Noerhadi, Cyril. (2021). "Envisioning Indonesia Investment Authority (INA): Game Changer for Indonesia's Investment", presentation at ISEAS – Yusof Ishak Institute, 10 March.

Siregar, Reza. (2021). "Reform Roads to Finance Growth", presentation at ISEAS – Yusof Ishak Institute, 10 March.

---

[1] "Ini Dia! Erik Thohir Keluarkan Aturan Jual Aset BUMN ke SWF", Emir Yanwardhana, CBNBC Indonesia, Market, 19 April 2021.

[2] Earlier, at an ISEAS webinar on 10 March 2021, Cyril Noerhadi, an INA Supervisory Board member, together with two senior economists, Anton Gunawan and Reza Siregar, discussed INA's set up and dismissed a few misconceptions on Indonesia's first sovereign wealth fund. This misconceptions were partly due to Indonesia's longstanding plan to establish a SWF, which goes back to the last years of President Suharto's term. The initial plan was to establish a holding company for its SOEs modeled after Singapore's Temasek and Malaysia's Khazanah, which many thought the new INA would resemble.

[3] Kompaspedia.kompas.id, Kementerian Badan Usaha Milik Negara (BUMN), by Topan Yunarto, 3 February 2021.

[4] Sejarah Super Holding: Usul Tanri Abeng ke Soeharto, by Achmad Dwi Afriyadi, detikFinance, 15 April 2019.

[5] A recent ADB review of Indonesia's SOEs noted that there are 118 SOEs spread across 13 sectors. Most are in manufacturing, transport, and financial services, with the largest employers being in agriculture, forestry, and fisheries. Some 28 SOEs are listed on Indonesia's Stock Exchange (IDX), accounting for just 4% of listed companies but for a sizable 25% of IDX's total market capitalization. For more details, see Yougesh Khatri and Mohamad Ikhsan's chapter 3 on Indonesian SOEs in

Edimon Ginting and Kaukab Naqvi (eds), Reforms, Opportunities, and Challenges for State-Owned Enterprises, July 2020, Asian Development Bank, Manila. (https://www.adb.org/publications/reforms-opportunities-challenges-state-owned-enterprises).

[6] see Ringkasan UU Cipta Kerja 7 Oktober 2020 www.ekon.go.id

[7] https://fulcrum.sg/indonesias-new-sovereign-wealth-fund-professionals-provide-some-comfort-but-challenges-remain/

[8] Sejarah Super Holding: Usul Tanri Abeng ke Soeharto, by Achmad Dwi Afriyadi, detikFinance, 15 April 2019.

[9] "Sebelum IPO, Perusahaan BUMN Incar Kerja Sama dengan SWF INA" dan "Wamen Pahala Beberkan BUMN yang Siap Ditawarkan ke SWF", CNBC Indonesia, Market, 14 April 2021.

ISEAS Perspective is published electronically by: **ISEAS - Yusof Ishak Institute** 30 Heng Mui Keng Terrace Singapore 119614 Main Tel: (65) 6778 0955 Main Fax: (65) 6778 1735 Get Involved with ISEAS. Please click here: https://www.iseas.edu.sg/support	ISEAS - Yusof Ishak Institute accepts no responsibility for facts presented and views expressed. Responsibility rests exclusively with the individual author or authors. No part of this publication may be reproduced in any form without permission.	Editorial Chairman: Choi Shing Kwok Editorial Advisor: Tan Chin Tiong Managing Editor: Ooi Kee Beng Editors: William Choong, Malcolm Cook, Lee Poh Onn, and Ng Kah Meng Comments are welcome and may be sent to the author(s).