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PERSPECTIVE

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Indonesia's Export-Proceeds Holding Policy: A Preliminary Assessment

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Containers are being loaded and unloaded at Tanjung Priuk Port in Jakarta, Indonesia, on 12 February 2024. Photo by Darryl Ramadhan/NurPhoto/NurPhoto via AFP.

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EXECUTIVE SUMMARY

- To ensure that sufficient export payments are kept within Indonesia's banking system for a longer period, the government introduced a Natural Resource Export Proceeds (Devisa Hasil Ekspor or DHE) policy, effective from 1 August 2023.

- Implementation of this policy is currently limited to natural resource exporters in mining, plantation, forestry and fisheries. This approach is driven by two key objectives. First, it aims to bolster the country's financial reserves in order to support the Rupiah and improve USD liquidity in the local money markets. Second, it is to steer natural resource exporters towards more downstream value-added activities within their respective supply chains.

- Preliminary results have been favourable, showing a high level of compliance and sizeable collection of export funds. But the affected exporters have voiced concern over their cashflow challenges and are calling for more flexible and lenient policy terms. Since exporters already suffer cashflow problems in a favourable commodity price market, there is concern that the policy will not be sustainable during a commodity down cycle.

- Acceding to the exporters' appeal for flexible and lenient terms would imply a reduction of the export earnings to be held within designated Indonesian banks. One alternative option is to reduce the amount and tenure of holdings, but extend this policy to all exporters, with follow-up provisions for sufficiently attractive yields and tax arrangements to incentivise the collection of sufficient volume and longer term holding of export funds. This alternative does not address the government's goal of promoting downstream activities, but this might be better addressed in a separate and more pertinent policy.

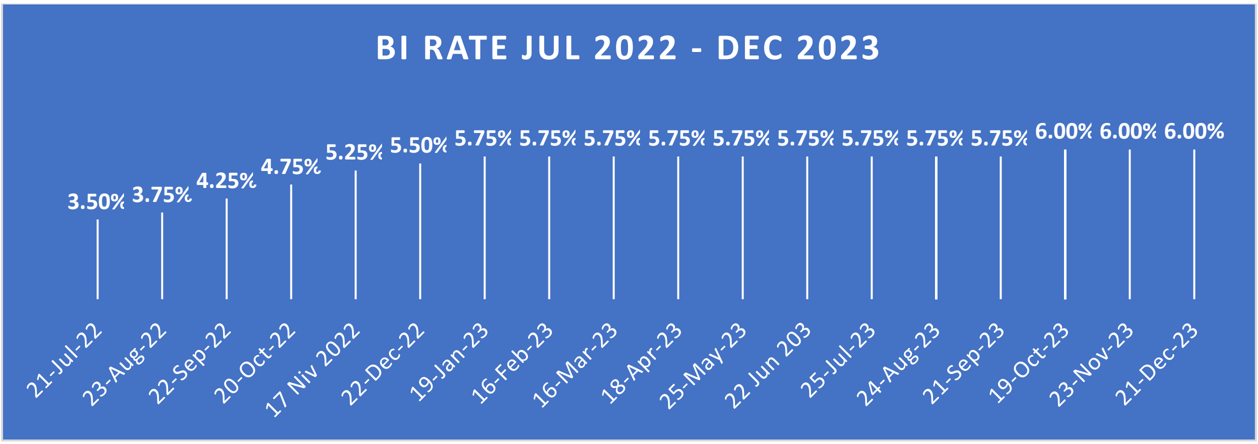
ISSN 2335-6677

INTRODUCTION

Prolonged high global interest rates, driven as they are by the US Federal Reserve's tight money policy for cooling down inflation, are causing many central banks to follow suit. As investors shift into higher-yielding USDs, central banks are struggling to stabilise their own currencies. Aside from raising their own interest rates, monetary authorities are also sparingly dipping into their reserves to support their currencies. In addition to geopolitical tensions in Ukraine, Gaza and the Taiwan Straits as well as rising political uncertainty due to the numerous elections being held this year, the high global interest rate environment is forcing governments to scale down their 2024 economic outlook.

In Indonesia, the Bank Indonesia (BI) has already raised its benchmark Rupiah interest rate several times from 3.75% in July 2022 to a high 6% in October 2023.[1] A month before the country's presidential election in February this year, BI decided to maintain this rate.

Graph 1: Bank Indonesia Benchmark Interest Rate 2022-2023

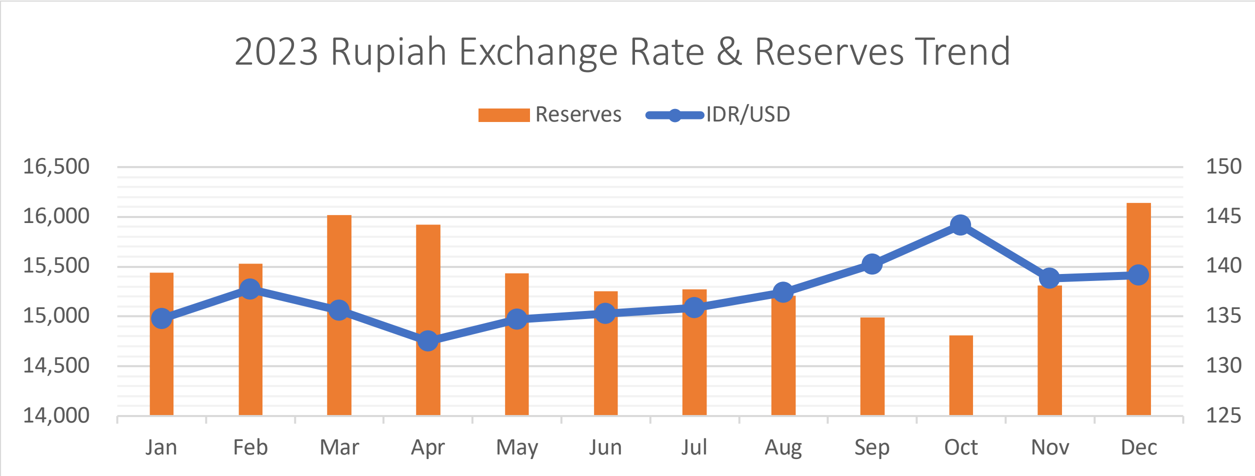


Source: https://www.bi.go.id/en/statistik/indikator/bi-rate.aspx

BI has also struggled to stabilize the Rupiah. The currency began in 2023 at the Rp 15,000 per USD level, then momentarily strengthened to Rp 14,750 in April, before continuously weakening and nearly touching Rp 16,000 in October.[2] That month, the country's reserves dipped to USD 132 billion from a USD 145 billion peak in March, and USD 135 billion in September. This led BI to move up its Rp benchmark rate by another 25 basis point to its current 6.0 per cent; this helped the currency recover for the remaining months and close the year at Rp 15,400 per USD, while reserves correspondingly rose to USD 146.4 billion.[3]

ISSN 2335-6677

Graph 2: 2023 IDR/USD and Reserves Trend



Source: https://www.bi.go.id/en/statistik/indikator/indikator-moneter.aspx

On August 1, 2023, in order to help stabilize its reserves the government made effective its "Export Proceeds" (Devisa Hasil Ekspor or DHE) policy. The policy requires natural resource exporters to hold a portion of their export proceeds at a designated bank in Indonesia for 3 months. This policy is still only six months old, so a proper assessment is premature. But the government has recently announced preliminary policy results and impacted exporters have also provided some meaningful feedback. This Perspective briefly reviews the background and details of this policy. It will then assess its effectiveness, highlight exporters feedback and conclude with a look at policy options ahead.

POLICY BACKGROUND AND DETAILS

An earlier 2019 version of the DHE policy came out just before the Covid pandemic and as a result was not strictly enforced. The current updated version, which is formally known as Government Regulation No. 36 of 2023 on natural resources export proceeds,[4] carries more detailed terms and became effective August 1, 2023.

In line with the post-pandemic 2022 recovery, Indonesia's export commodity prices rose to an all-time high that year, especially its mineral exports. In 2023, coinciding with the DHE policy, commodity prices have slightly retreated from its peak, but remain above their long-term average prices. It seems that natural resource exporters are still enjoying profit margins sufficient enough for them to bear the compliance cost of this policy.

The DHE policy has roughly two unrelated objectives. One is to collect a portion of exporter proceeds, including those still parked overseas, and place these funds within the local banking system for a longer period, thus helping strengthen the country's reserves. This would also improve USD liquidity in the local money markets, and keep export proceeds parked at banks overseas to a minimum.

The second objective is to deter interested local and foreign investors who are merely seeking to extract raw natural resource, and to encourage them to expand and invest in downstream

ISSN 2335-6677

activities as well. This ties in with the government's longer-term downstreaming programme and explains the policy's fixation with natural resource exporters operating in mining, plantations, forestry and fisheries.

To achieve the above objectives, a few key DHE policy terms have been decided, and are as follows:

- The policy currently applies only to natural resource exporters in mining, plantation, forestry and fisheries sectors. Those exporters that have downstream exported products are exempted.
- The value of exports impacted are those above USD 250,000, thus exempting smaller natural resource exporters.
- The funds held must amount to at least 30% of total export proceeds and must be kept for a minimum 3 months in special accounts with OJK-designated banks in Indonesia, or invested in financial instruments issued by these banks, the state-owned Export-Import Bank and/or Bank Indonesia.
- Exporters are given some flexibility in using the 30% funds held in banks for imports, capital investments, loan repayments, export duties and other levies.
- Loan repayments being made through escrow accounts must now use designated banks in Indonesia. Bank escrow accounts are set up by borrowers to collect their revenue proceeds and ensure priority for loan servicing and repayments, before funds can be used for operations. Those repaying their loans through escrow accounts at banks overseas must now open and use escrow accounts with designated banks in Indonesia. This is to ensure repatriation of export proceeds placed overseas.
- Incentives for impacted exporters in the form of tax facilities on income generated from export proceeds have yet to be announced[5].

A PRELIMINARY ASSESSMENT

In December 2023, the government's preliminary review noted that preliminary DHE policy results show a significant level of compliance (non-compliance of just 1%) among impacted exporters and the collection of a sizable level of DHE funds held in designated banks.

Table 1: Export Proceeds Collected and Held with Indonesian Banks under the new DHE policy

	Natural Resource Exports	**Amount Collected and Held in Designated Banks**
August 2023	USD 10.5 bn	USD 2.7 bn
September 2023	USD 9.0 bn	USD 2.3 bn
October 2023	USD 10.2 bn	USD 2.9 bn

Source: https://kumparan.com/kumparanbisnis/evaluasi-kebijakan-devisa-hasil-ekspor-sda-diperpanjang-hingga-februari-2024-21i2yweUjTl

The next government review will be made in early 2024.[6] Based just on the two top natural resource exports, coal and crude palm oil (CPO), which for 2022 totalled USD 74.5 bn,[7] the

30% amount collected and held at designated banks for 3 months could annually reach a sizable USD 22.4 bn. Clearly, the potential volume of export proceeds locked in Indonesia for a longer term will be substantial.

Although BI's decision to raise its benchmark rate to 6.0% in October last year was perhaps more critical in reversing the Rupiah's weakening trend from a low Rp 15,911 per USD level to then close the year at a stronger Rp 15,400 per USD level, the export proceeds collected and held during this period should have added to the country's reserves, thus allowing BI access to sufficient reserves for supporting the Rupiah, whenever needed.

The objective of repatriating export proceeds by requiring exporters to move their loan repayment escrow accounts to banks in Indonesia might be less impactful, though. This is because global and regional banks have already been moving away from lending to natural resource companies that do not meet stringent ESG (Environment, Social and Governance) requirements. For example, coal and CPO plantation financing are increasingly being done by local banks and therefore most loan repayment escrow accounts are already with Indonesian banks.

So far, impacted exporters have mostly complied with the new DHE policy, but they have voiced their concern about cashflow problems stemming from this policy.[8] Setting aside 30% of export revenue for 3 months has become a major challenge for them. The policy has a provision that exporters can still use the 30% bank-held funds for their operations, but to do so, they need to arrange back-to-back loans secured by these funds, which carries an added charge ranging from 50 to 100bp.[9]

Further complicating exporters' cashflow management has been the government's royalty and levy charges, which are paid upfront or on shipment before export proceeds are received. Furthermore, the rates of these charges have increased along with the rise in commodity prices. For coal exporters, the royalties paid upfront on coal export shipments are in the 14-28% range.[10] These coal royalties are administered and collected by the Ministry of Energy and Mineral Resources (ESDM), while for CPO exporters, the export levy is fixed and has recently risen to USD 74.0 per tonne.[11] Having to pay upfront export royalties and levies and tie-up 30% of their export revenue for 3 months has been a major problem for exporters. If natural resource exporters are already struggling with DHE cashflow problems in the current favourable commodity price environment, how they would cope in a downward cycle, raises concerns about this policy's long-term sustainability.

POLICY OPTIONS AHEAD

Impacted exporters are already suggesting more flexible terms under the current DHE policy. One idea is to raise the threshold to above USD 500,000, up from the current USD 250,000. Another is to reduce the portion held from the current 30% of export proceeds and to shorten the current minimum 3-month tenor to either 1 or 2 months, during tight cashflow conditions.[12] The third point regards making the yields on the special accounts or security instruments sufficiently attractive to lure back these funds. Discussions on these are currently still ongoing. The only problem with the above proposals is that they would reduce the amount and tenure of natural resource export proceeds held, thus making the policy less effective.

It might be advisable to promote the government's downstream policy with a separate more detailed policy; the DHE policy alone may not be sufficient to encourage natural resource players to go downstream. An effective downstreaming programme would require not just the right scarce natural resource, but also the appropriate human capital and institutional set up, which requires time to develop. Only then would this programme have the desired impact of creating jobs and providing growth opportunities.

By limiting the DHE policy's focus to its reserve-stabilizing objective, the emphasis is more to the collecting and holding of a sizable amount in Indonesia's banking system for a longer period. One potential option to this is a more lenient DHE policy that is applied to all exporters. Taking into account the impacted exporters' feedback, and in order to make the policy more sustainable and palatable to all exporters, the portion of export proceeds held needs to be sufficiently low for exporters to bear, including for commodity exporters during a downturn. But conversely it should also be high enough to meet the government's reserve stabilization needs.

Then, to incentivize exporters to hold more of their export proceeds for a longer period, the interest yields on the special DHE accounts, or the securities offered, should be competitive and set progressively higher the longer the funds are placed. In other words, the longer the tenor, the higher the yields. Since the government wishes to attract exporter funds parked overseas, the yields should at least reflect the country's risk premium or its interest differential. For instance, the interest differential between the BI benchmark rate and the US Fed Fund rate during the 2019-2022 period was around 3.0-4.0%. But since 2023, the interest differential has narrowed to 1.0-0.5%, which explains the downward pressure on the Rupiah.

The government has yet to come out with their yield scheme on security instruments that would be part of the DHE policy. Setting yields that compare favourably with those provided by international financial centres, and taking into account the country's sovereign risk premium would more effectively attract not only Indonesian exporter funds but also funds from global portfolio investors.

In the current election year, and before a new government cabinet is formed, adjusting the BI benchmark rate upward to widen the current IDR and USD interest rate differential in line with Indonesia's sovereign risk premium, would be politically difficult. So far, export trends and commodity prices still remain favourable, and the government's latest January 2024 reserve position stands at USD 145.3 billion. This is sufficient to cover 6.4 months of imports and the government's debt servicing payments.[13] It will be interesting to see what incentives the government eventually comes out with and whether these will be attractive enough to exporters without BI having to raise its benchmark rate.

ENDNOTES

[1] https://www.bi.go.id/en/statistik/indikator/bi-rate.aspx
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ISSUE: 2024 No. 20
ISSN 2335-6677

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