Day 2
Focus Discussion 1

Balancing Interests of Upstream and Downstream in Determining Indonesia Domestic Gas Price Policy

Present at this FGD as resource persons were Arief S. Handoko, President Director of Pertamina Gas Negara, Aris Mulya Azof, Chairman of the Indonesian Gas Society, Kurnia Chairi, Deputy of Finance and Commercialization of SKK Migas and Triani from the Directorate of Upstream Chemical Industry-Indonesian Ministry of Industry.

As an introduction to the discussion, Mr. Kevin Moore, representing the IPA (Indonesia Petroleum Association), presented a comprehensive overview of the gas resources situation in Indonesia. Gas plays a critical role in ensuring energy security in Indonesia. In 2022, the country produced 5.6 BCF/D (Billion Cubic Feet per Day) of gas, with 68% of it being used domestically to meet the energy demands of various sectors. Currently, gas constitutes 19% of Indonesia's national energy mix. However, there are forecasts suggesting that its share will increase to 24% by the year 2050.

The Indonesian government has set ambitious goals to boost domestic gas production. By the year 2030, they aim to increase gas production to 12 BCF/D. However, despite various ongoing projects like Tangguh Train 3, IDD (Indonesia Deepwater Development), and Masela, the combined gas output will only reach 8.8 BCF/D. This highlights the need for further exploration and development efforts to bridge the gap between current and targeted gas production levels.

The Indonesian government has taken significant steps to enhance the competitiveness of domestic gas-using industries. One of the key measures implemented was the introduction of a gas price cap of $6/MMBTU at the plant gate, specifically targeted at seven vital industries. This policy was initiated in 2016 and has been further clarified under Minister Regulation no. 91/2023.

The industries benefiting from this price cap include fertilizer, petrochemicals, olefins, rubber gloves, ceramics, steel, glass, and power. By providing a controlled and affordable gas price to these sectors, the government aims to stimulate economic growth. increase tax revenue and job creation as well as bolster industrial competitiveness.

The effect on the upstream oil and gas industry from the government's initiatives, including the capped gas price, has been a mixed one. While the government's efforts to maintain contractor revenue share for existing developments at contract prices by reducing government royalty share has provided some stability for existing projects, it has also posed challenges for new developments.

The capped gas price, which is being used as a benchmark for new development approvals, has created a discouraging environment for exploration and development of new gas fields. This is because the capped price may not adequately reflect the increasing exploration and development costs due to inflation in the upstream oil and gas industry since 2016. Despite the government's efforts to provide incentives to the industry can lead to a decreased interest in investing in new upstream exploration activities.

The initial discussion began with various factors affecting gas user end-product's price structure, and how effective is the Domestic Gas Price policy (HGBT) in improving domestic industry's competitiveness.

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Arief S. Handoko, President Director of Pertamina Gas Negara conveyed that the most effective way to increase demand from industries is by offering an attractive price for gas and ensuring easy access to gas infrastructure, while also guaranteeing gas supply sustainability. One practical approach to achieve this is by providing uninterrupted gas supply for an extended period, such as 7 to 9 years, for instance for encouraging fertilizer plant investments.

Aris Mulya Azof, Chairman of Indonesian Gas Society believes that the primary objective behind supporting natural gas usage in various manufacturing industries is to bolster national economic development and sustain a yearly economic growth rate of over 5%. As a crucial energy source, natural gas plays a vital role in powering manufacturing processes across different sectors, contributing to industrial growth and overall economic prosperity.

Yet, in order to encourage the adoption of natural gas, the government should play a significant role by covering the implementation of carbon taxes. In an industry where costs can be dynamic due to various factors such as geopolitical events, market fluctuations, and changes in production techniques, maintaining a fixed price for natural gas can pose challenges. This predicament can impact the profitability of gas producers and potentially lead to supply uncertainties, affecting the stability of the overall market.

Triani from Directorate of Upstream Chemical Industry stated that balancing upstream and downstream gas prices brings several benefits, especially concerning affordability and productivity. The affordability of gas prices is influenced by multiple factors, starting with the availability of production factors such as raw materials and natural resources. Additionally, market conditions within the country play a crucial role, as does the state of infrastructure that enables the distribution of gas. Moreover, supportive policies in the industry sector can also impact gas affordability. Finally, external factors like government initiatives and the occurrence of calamities can further influence gas prices.

With the government's proactive stance in reducing gas prices, an immediate positive effect on production costs can be observed. The current gas price of 6 USD is expected to be continued, creating a more conducive environment for various industries. As a result, seven industry sectors are set to experience a boost in productivity, which is particularly significant given the challenges posed by the COVID-19 pandemic. This reduction in gas prices not only enhances the survival prospects of these sectors during and post-pandemic but also stimulates investment. The investment influx, amounting to a substantial 35 trillion rupiahs in 2022, is a clear indicator of the positive impact of reduced gas prices on the growth and development of these industry sectors.

Nonetheless, preparing for potential increases in energy prices is crucial for industries to ensure their sustainability and competitiveness. The past example of the sudden gas price increase in the ceramic industry in 2011 serves as a stark reminder of the significant impact such price fluctuations can have on businesses. The sudden gas price hike forced many companies to shut down their plants. This resulted in disruptions to production, loss of jobs, and an overall negative impact on the industry's growth and contribution to the economy.

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Next discussion is about how investors perceive the HGBT policy for their investment decisions and what efforts can the Government make to maintain upstream oil and gas economics in the HGBT environment.

Aris Mulya Azof, Chairman of Indonesian Gas Society acknowledged that the Covid-19 pandemic has had far-reaching consequences on economies in Indonesia. In this challenging context, the implementation of HGBT becomes a critical consideration to support industries and facilitate economic recovery. However, its execution demands careful evaluation, taking into account its potential impact on various economic indicators. Introducing HGBT can affect the output and profitability of industries. By granting access to lower energy prices, industries may experience increased production output and improved profit margins. This could bolster economic growth and foster job creation.

Nevertheless, the Indonesian government must conduct comprehensive evaluations, taking into account the effects on output, profit, added value, tax income, and fiscal revenues. While reduced energy prices may initially result in lower tax revenues, the overall growth and expansion of industries could eventually offset these losses through increased economic activity. Reduced energy prices can trigger multiplier effects in the economy. As industries benefit from cost savings, they can reinvest in expansion, creating demand for goods and services. While there may be a temporary sacrifice of government income to protect the seven industry sectors, the aim is to create a sustainable and resilient economic environment that benefits both the industries and the nation as a whole.

Further discussion was whether the recent changes made in Permen ESDM 15/2022 and Kepmen ESDM 91/2023, namely allowing the delivered gas price to US$6.5 - 7/MMBtu could improve oil and gas investor economics and attract more investment.

Arief S. Handoko, President Director of Pertamina Gas Negara explained PGN's strategy to meet the increasing upstream demand for gas involves integrating midstream infrastructure using a combination of LNG and pipelines. This approach aims to ensure a consistent gas supply to the various industry sectors.
To effectively execute this strategy, PGN requires clarification from SKK MIGAS regarding the specific volume allocation from LNG and gas pipelines. By combining the allocation of LNG and gas pipelines, PGN can accurately calculate the clear gas volume and communicate this information to its customers. This transparency allows for better determination of gas prices for end buyers.

However, the concern lies with the potential risk of end buyers having to pay higher gas prices. PGN has existing agreements (SPAs) with fertilizer and oil companies that follow a specific price formula. With the implementation of HGBT, if the gas price exceeds the previous formula-based price, these companies could face dire consequences.

To address this issue, PGN acknowledges the necessity of recalculating the existing price formula and directly linking it to the gas price calculation. This adjustment aims to ensure that the formula remains responsive to fluctuations in gas prices, providing more stability and predictability for both PGN and its customers. By recalibrating the pricing formula and integrating midstream infrastructure with LNG and pipelines, PGN seeks to secure a sustainable and efficient gas supply for the increasing demand from industry sectors. This approach also aims to strike a balance between offering competitive prices to end buyers while safeguarding the interests of PGN and its contractual agreements with key customers in the fertilizer and oil sectors.

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Kurnia Chairi, Deputy of Finance and Commercialization SKK Migas stated that SKK Migas is always considering the linkage between upstream, midstream, and downstream aspects of the gas industry and agreeing to reevaluate the implementation of HGBT. This approach is likely to create a more holistic and integrated gas supply chain, which can lead to better efficiency and coordination.

By observing and coordinating with the Ministry of Energy and Mineral Resources to build infrastructure using the State Budget, SKK Migas aims to have more control over gas prices and ensure a stable supply of gas. This control can help to mitigate price fluctuations and ensure a more predictable market for both producers and consumers.

The ongoing case of infrastructure developed outside the State Budget occurs because SKK Migas need to explore other avenues to fund the development of necessary gas supply infrastructure. This could involve seeking private investors or finding buyers who can afford the overall production price, making it financially feasible for all parties involved.

Overall, the collaborative efforts between SKK Migas, Ministry of Energy and Mineral Resources and Ministry of Industry, along with the development of infrastructure and long-term contracts, can contribute to a more stable and efficient gas industry in Indonesia. By working together and considering various aspects of the gas supply chain, the aim is to achieve a balanced approach that benefits all stakeholders involved.

Triani, Directorate of Upstream Chemical Industry believes that the cooperation between the Ministry of Industry and PGN to facilitate the linkage between PGN pipeline and industries is a crucial step towards enhancing gas accessibility and affordability for the industrial sector. To support this linkage, the Ministry of Industry takes the initiative to promote the Industrial Estates developments. These estates serve as strategic locations where industries can establish their facilities in close proximity to PGN pipelines. By locating industries near the pipeline infrastructure, the transportation and delivery of gas become more efficient and cost-effective.

The development of Industrial Estates not only benefits industries by providing them with easier access to gas supply but also fosters economic growth in specific regions. Concentrating industries in these estates can lead to economies of scale and synergies among businesses, which in turn, can attract further investment and development.

To ensure a smooth and standardized process for industries to connect to the PGN pipeline, the Ministry of Industry, in coordination with PGN, provides guidelines for industries to follow. These guidelines outline the necessary steps, requirements, and technical specifications for developing their infrastructure link to the PGN pipeline.

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Q & A

1. **Why has gas demand continued to increase after the implementation of HGBT and how is gas prices recovering after the Covid-19 pandemic?**

   The HGBT policies have been instrumental in supporting seven sectors and boosting the Indonesian economy during the Covid-19 pandemic. While the market-driven approach can be advantageous, the government's objectives to create multiplier effects in downstream industries may lead to specific price considerations. However, policymakers must remain attentive to changing circumstances, and the policy's long-term sustainability may need reassessment in the future. (**Arief S. Handoko**)

2. **Has the 6 USD/MMBTU price cap contributed to hindering the development and adoption of CCS/CCUS technology?**

   It's unfortunate that the CCS initiatives potentially could be stalled since the implementation of HGBT. Therefore, SKK Migas and the Ministry of Finance have engaged in discussions to address this issue and offer certain incentives.

   To support and incentivize CCS initiatives, the government could consider revising Government Regulations number 27 and 53 to include fiscal incentives. These revisions may involve providing tax benefits or subsidies for companies that actively participate in carbon capture and storage projects. Such incentives can encourage more companies in the upstream industry to adopt environmentally friendly practices, despite the current gas price of 6 USD. (**Kurnia Chairi**)

   The 6 USD gas price can be discouraging for the upstream industry, especially when they are required to implement costly CCS/CCUS initiatives to mitigate their carbon emissions. Achieving a balance between upstream and downstream considerations is indeed a significant issue in the gas industry. While downstream industries may benefit from the lower gas prices, upstream companies face the challenge of meeting environmental regulations and investing in sustainability measures. Midstream companies, like PGN, play a critical role in addressing this balance. As they are responsible for transporting and distributing gas from the upstream to the downstream sectors, they need to ensure that gas allocation is determined in a way that considers both economic and environmental factors. (**Arief S. Handoko**)

3. **Has the Government evaluated the effect of HGBT to the productivity and development of the downstream industry?**

   The capped gas price has been promoting increased productivity in the seven industrial sectors. By limiting the gas price, these industries are encouraged to improve their utilization and enhance their productivity. This, in turn, can have positive effects on their competitiveness and overall economic growth.

   One significant advantage of the HGBT policy is that it does not hinder innovation in the Research and Development of Renewable Energies. With the cost savings achieved through the capped gas price, the seven sectors can redirect their funds towards improving their production systems and investing in innovation. By being able to save money on energy costs, these industries have more financial resources available to explore new technologies and adopt sustainable practices. This enables them to remain competitive. (**Triani**)