

**D. RISK FACTORS**

**A. Risks Related to Indonesia**

**1. Political and Social Risks**

*Current political and social events in Indonesia may adversely affect our business*

Since 1998, Indonesia has experienced a process of democratic change, resulting in political and social events that have highlighted the unpredictable nature of Indonesia's changing political landscape. In 1999, Indonesia conducted its first free elections for parliament and president. Indonesia also has many political parties, without any one party holding a clear majority. Due to these factors, Indonesia has, from time to time, experienced political instability, as well as general social and civil unrest. For example, since 2000, thousands of Indonesians have participated in demonstrations in Jakarta and other Indonesian cities both for and against former President Abdurahman Wahid, former President Megawati, and current President Susilo Bambang Yudhoyono as well as in response to specific issues, including fuel subsidy reductions, privatization of state assets, anti-corruption measures, decentralization and provincial autonomy and the American-led military campaigns in Afghanistan and Iraq. Although these demonstrations were generally peaceful, some turned violent.

Indonesia is facing a couple of critical political events in 2014, namely the legislative election scheduled for April 9, 2014, and the election for President and Vice President scheduled for July 9, 2014. Political tensions are expected to increase during both the legislative and the presidential elections. President Susilo Bambang Yudhoyono is required to step down after having served two terms, thus the presidential election will likely be hotly contested, with an uncertain outcome.

Increased political tensions may cause social and civil disturbances and conflicts to increase. Social conflicts, in particular, may escalate in the lead-up period to the 2014 legislative and presidential election. The dynamics of political maneuvering to win the sympathy of different groups of the public may trigger friction at the grass-root level.

Separatist movements and clashes between religious and ethnic groups have also resulted in social and civil unrest in parts of Indonesia, such as Aceh in the past and in Papua currently, where there have been clashes between supporters of those separatist movements and the Indonesian military, including continued activity in Papua, by separatist rebels that has led to violent incidents. There have also been inter-ethnic conflict, for example in Kalimantan, as well as inter-religious conflict such as in Maluku and Poso.

Labor issues have also come to the fore in Indonesia. In 2003, the Government enacted a new labor law that gave employees greater protections. Occasional efforts to reduce these protections have prompted an upsurge in public protests as workers responded to policies that they deemed unfavorable.

There can be no assurance that social and civil disturbances will not occur in the future and on a wider scale, or that any such disturbances will not, directly or indirectly, materially and adversely affect our business, financial condition, results of operations and prospects.

*Terrorist activities in Indonesia could destabilize Indonesia, which would adversely affect our business, financial condition and results of operations, and the market price of our securities*

There have been a number of terrorist incidents in Indonesia, including the May 2005 bombing in Central Sulawesi, the Bali bombings in October 2002 and 2005 and the bombings at the JW Marriot and Ritz Carlton hotels in Jakarta in July 2009. Although the Government has successfully countered some terrorist activities in recent years and arrested several of those suspected of being involved in these incidents, terrorist incidents may continue and, if serious or widespread, might have a material adverse effect on investment and confidence in, and the performance of, the Indonesian economy and may also have a material adverse effect on our business, financial condition, results of operations and prospects and the market price of our securities.

## **2. Macro Economic Risks**

### *Negative changes in global, regional or Indonesian economic activity could adversely affect our business*

Changes in the Indonesian, regional and global economies can affect our performance. Two significant events in the past that impacted Indonesia's economy were the Asian economic crisis of 1997 and the global economic crisis which started in 2008. The 1997 crisis was characterized in Indonesia by, among others, currency depreciation, a significant decline in real gross domestic product, high interest rates, social unrest and extraordinary political developments, while the global economic crisis that arose from the subprime mortgage crisis in the US put Indonesia's economy under pressure, although not as severely as in 1997. The global financial markets have also experienced volatility as a result of the downgrade of US sovereign debt in 2012 and concerns over the debt crisis in the Eurozone. Uncertainty over the outcome of the Eurozone governments' financial support programs and worries about sovereign finances generally are ongoing. If the crisis becomes protracted, or extends to Asia and Indonesia, we can provide no assurance that it will not have a material and adverse effect on Indonesia's economic growth and consequently on our business.

Adverse economic conditions could result in less business activity, less disposable income available for consumers to spend and reduced consumer purchasing power, which may reduce demand for communication services, including our services, which in turn would have an adverse effect on our business, financial condition, results of operations and prospects. There is no assurance that there will not be a recurrence of economic instability in future, or that, should it occur, it will not have an impact on the performance of our business.

### *Fluctuations in the value of the Rupiah may materially and adversely affect us*

Our functional currency is the Rupiah. One of the most important effects of the Asian economic crisis that affected Indonesia was the depreciation and volatility in the value of the Rupiah as measured against other currencies, such as the US Dollar. The Rupiah continues to experience significant volatility. From 2009 to 2013, the Rupiah per US Dollar exchange rate ranged from a high of Rp8,508 per US Dollar to a low of Rp12,270 per US Dollar. As a result, we recorded foreign exchange losses of Rp210 billion in 2011, Rp189 billion in 2012 and Rp249 billion in 2013. The Rupiah depreciated significantly in 2013. As of December 31, 2013, the Rupiah per US Dollar exchange rate stood at Rp12,170 per US Dollar compared to Rp9,637.5 per US Dollar as of December 31, 2012.

To the extent that the Rupiah depreciates further from the exchange rate as of December 2013, our US Dollar-denominated obligations under our accounts payable and procurements payable, as well as payments for foreign currency-denominated loans payable and bonds payable, would increase in Rupiah terms. A depreciation of the Rupiah would also increase the Rupiah cost of our capital expenditures as most of our capital expenditures are priced in or with reference to foreign currencies, mainly US Dollars and Euros, while a substantial majority of our revenues are in Rupiah. Such depreciation of the Rupiah would result in losses on foreign exchange translation, significantly affect our total expenses and net income and reduce the US Dollar amounts of dividends received by holders of our ADSs. We can give no assurances that we will be able to control or manage our exchange rate risk successfully in the future or that we will not be adversely affected by our exposure to exchange rate risk.

In addition, while the Rupiah has generally been freely convertible and transferable, from time by time, Bank Indonesia has intervened in the currency exchange markets in furtherance of its policies, either by selling Rupiah or by using its foreign currency reserves to purchase Rupiah. We can give no assurances that the current floating exchange rate policy of Bank Indonesia will not be modified or that the Government will take additional action to stabilize, maintain or increase the Rupiah's value, or that any of these actions, if taken, will be successful. Modification of the current floating exchange rate policy could result in significantly higher domestic interest rates, liquidity shortages, capital or exchange controls or the withholding of additional financial assistance by multinational lenders. This could result in a reduction of economic activity, an economic recession, loan defaults or declining subscriber usage of our services, and as a result, we may also face difficulties in funding our capital expenditures and in implementing our business strategy. Any of the foregoing consequences could have a material adverse effect on our business, financial condition, results of operations and prospects.

#### *Downgrades of credit ratings of the Government or Indonesian companies could adversely affect our business*

As of the date of this Annual Report, Indonesia's sovereign foreign currency long-term debt is rated "Baa3" by Moody's (upgraded from "Ba1" on January 18, 2012), "BB+" by Standard & Poor's (upgraded from "bb" on April 8, 2011) and "BBB" by Fitch Ratings (upgraded from "BB+" on December 15, 2011). Indonesia's short-term foreign currency debt is rated "B1/NP" by Moody's, "B" by Standard & Poor's and "B" by Fitch Ratings. On January 18, 2012, Moody's upgraded Indonesia's long-term debt rating to investment grade status.

We can give no assurances that Moody's, Standard & Poor's or Fitch Ratings, will not change or downgrade the credit ratings of Indonesia. Any such downgrade could have an adverse impact on liquidity in the Indonesian financial markets, the ability of the Government and Indonesian companies, including us, to raise additional financing and the interest rates and other commercial terms at which such additional financing is available. Interest rates on our floating rate Rupiah-denominated debt would also likely increase. Such events could have material adverse effects on our business, financial condition, results of operations and prospects.

### **3. Disaster Risks**

#### *Indonesia is vulnerable to natural disasters and events beyond our control, which could adversely affect our business and operating results*

Many parts of Indonesia, including areas where we operate, are prone to natural disasters such as floods, lightning strikes, typhoons, earthquakes, tsunamis, volcanic eruptions, fires, droughts, power outages and other events beyond our control. The Indonesian archipelago is one of the most volcanically active regions in the world as it is located in the convergence zone of three major lithospheric plates. It is subject to significant seismic activity that can lead to destructive earthquakes, tsunamis or tidal waves. From time to time, natural disasters have killed, affected or displaced large numbers of people and damaged our equipment. These events in the past, and may in the future, disrupt our business activities, cause damage to equipment and adversely affect our financial performance and profit.

In recent years, several natural disasters have occurred in Indonesia (in addition to the Asian tsunami in 2004), including tsunamis in Pangandaran in West Java in 2006 and 2010, an earthquake in Yogyakarta in Central Java in 2006, a hot mud eruption and subsequent flooding in Sidoarjo in East Java in 2006 and separate earthquakes in Papua, West Java, Sulawesi and Sumatra in 2009.

On September 2, 2009, an earthquake in West Java caused damage to our assets. On September 30, 2009, an earthquake in West Sumatra disrupted the provision of telecommunications services in several locations. Although our Crisis Management Team in cooperation with our employees and partners was able to restore services quickly, the earthquake caused severe damage to our assets. There were a number of earthquakes detected in 2010 through 2013, although none of them presented significant risks to our business in general.

Flash floods and more widespread flooding occur regularly during the rainy season from November to April. Cities, especially Jakarta, are frequently subject to severe localized flooding which can result in major disruption, and occasionally fatalities. Jakarta experienced significant floods in February 2007 as did in Solo in Central Java in January. In January 2009, torrential rain caused a dam to burst outside Jakarta, flooding hundreds of homes in a densely populated neighborhood, resulting in the death of approximately 100 people. Landslides regularly occur in rural areas during the wet season.

There are numerous volcanoes in Indonesia, any of which can erupt without warning. In October and November 2010, Mount Merapi in Central Java erupted several times, killing an estimated 140 persons, displacing several hundred thousand others in a 20 km radius, causing billions of dollars of property damage and disrupting air travel. Since April 2008, Mount Soputan in North Sulawesi, Mount Egon in Flores Island, Nusa Tenggara, Mount Ibu in North Maluku and Anak Krakatau in the Sunda Strait have shown significant increased volcanic activity. Mount Sinabung, 60 km (40 miles) southwest of Sumatra's main city Medan, erupted on August 29, 2013 after lying dormant for 400 years, and erupted again in November 2013. Ash and acrid smoke from the volcano blanketed villages and crops.

In 2010, our submarine cables forming part of our backbone suffered damage due to a tsunami in West Sumatra and an earthquake in Sumbawa. These were repaired.

Although we have implemented a Business Continuity Plan (“BCP”) and a Disaster Recovery Plan (“DRP”), and test these regularly and we have insured our assets to protect from any losses attributable to natural disasters or other phenomena beyond our control, there is no assurance that the insurance coverage will be sufficient to cover the potential losses, that the premium payable for these insurance policies upon renewal will not increase substantially in the future, or that natural disasters would not significantly disrupt our operations.

There are no assurances that future geological or meteorological occurrences will not have a significant impact on Indonesia and its economy. A significant earthquake, other geological disturbance or weather-related natural disaster in any of Indonesia’s more populated cities and financial centers could severely disrupt the Indonesian economy and undermine investor confidence, thereby materially and adversely affecting our business, financial condition, results of operations and prospects.

*Our operations may be adversely affected by an outbreak of avian influenza, Influenza A (H1N1) virus or other epidemics*

An outbreak of avian influenza, Influenza A (H1N1) virus or a similar epidemic, or the measures taken by the Governments of affected countries, including Indonesia, against such an outbreak, could severely disrupt the Indonesian and other economies and undermine investor confidence, thereby materially and adversely affecting our financial condition or results of operations and the market value of its securities. Moreover, our operations could be materially disrupted if our employees remained at home and away from our principal places of business for extended period of time, which would have a material and adverse effect on our financial condition or results of operations and the market value of its securities.

#### **4. Other Risks**

*Indonesian Corporate Disclosure Standards differ in significant respects from those applicable in other countries, including the United States*

As an IDX, NYSE and LSE listed company, we are subject to regulatory and exchange corporate governance and reporting requirements in multiple jurisdictions. There may be less publicly available information about Indonesian public companies, including us, than is regularly disclosed by public companies in countries with more mature securities markets. As a result, investors may not have access to the same level and type of disclosure as that available in other countries, and comparisons with other companies in other countries may not be possible in all respects.

*Our financial results are reported herein in conformity with IFRS, however, we report our financial results to OJK (as the successor to Bapepam-LK) in conformity with IFAS, which differs in certain significant respects from IFRS, and we distribute dividends based on profit for the year attributable to owners of the parent company and net income per share determined in reliance on IFAS*

In accordance with regulations of OJK and the IDX, we are required to report our financial results to OJK in conformity with IFAS. We have provided to OJK our financial result for the financial year ended December 31, 2013, on March 6, 2014, which we furnished to the SEC on a Form 6-K dated March 19, 2014, which contains our audited Consolidated Financial Statements as of December 31, 2013 and for the year then ended and prepared in conformity with IFAS. IFAS differs in certain significant respects from IFRS, and, as a result, there are differences between our financial results as reported under IFAS and IFRS, including profit for the year attributable to owners of the parent company and net income per share. We distribute dividends based on profit for the year attributable to owners of the parent company and net income per share determined in reliance on IFAS.

Using IFAS results, our profit for the year attributable to owners of the parent company would be Rp12,850 billion and Rp14,205 billion for 2012 and 2013, and our net income per share would be Rp133.84 and Rp147.42 for 2012 and 2013. Dividends declared per share were Rp87.24 for 2012. The dividends declared per share for the year 2013 will be decided at the 2014 AGMS, scheduled for April 2014.

*We are incorporated in Indonesia, and it may not be possible for investors to effect service of process, or enforce judgments, on us within the United States, or to enforce judgments of a foreign court against us in Indonesia*

We are a limited liability company incorporated in Indonesia, operating within the framework of Indonesian laws relating to Indonesian companies with limited liability, and all of our significant assets are located in Indonesia. In addition, our Commissioners and our Directors reside in Indonesia and a substantial portion of the assets of such persons are located outside the United States. As a result, it may be difficult for investors to effect service of process, or enforce judgments on us or such persons within the US, or to enforce against us or such persons in the US, judgments obtained in US courts.

We have been advised by Hadiputranto, Hadinoto & Partners, our Indonesian legal advisor that judgments of US courts, including judgments predicated upon the civil liability provisions of the US federal securities laws or the securities laws of any state within the US, are not enforceable in Indonesian courts, although such judgments could be admissible as non-conclusive evidence in a proceeding on the underlying claim in an Indonesian court. They have also advised that there is doubt as to whether Indonesian courts will enter judgments in original actions brought in Indonesian courts predicated solely upon the civil liability provisions of the US federal securities laws or the securities laws of any state within the US. As a result, the claimant would be required to pursue claims against us or such persons in Indonesian courts.

*Our controlling shareholder's interest may differ from those of our other shareholders*

The Government has a controlling stake of 53.1% of our issued and outstanding shares of common stock and the ability to determine the outcome of all actions requiring the approval of the shareholders. The Government also holds our one Series A Dwiwarna share, which has special voting rights and veto rights over certain matters, including the election and removal of our Directors and Commissioners. It may also use its powers as majority shareholder or under the Dwiwarna share to cause us to issue new shares, amend our Articles of Association or bring about actions to merge or dissolve us, increase or decrease our authorized capital or reduce our issued capital, or veto any of these actions. One or more of these may result in the delisting of our securities from certain exchanges. Further, through the MoCI, the Government exercises regulatory power over the Indonesian telecommunications industry.

As of December 31, 2013, the Government had a 14.3% equity stake in PT Indosat Tbk. ("Indosat") which compete with us, in fixed IDD telecommunications services, and competes with Telkomsel in cellular services. The Government's stake includes the Series A Dwiwarna share which has special voting rights and veto rights over certain strategic matters under Indosat's Articles of Association, including decisions on dissolution, liquidation and bankruptcy, and also permits the Government to nominate one Director to its Board of Directors and one Commissioner to its Board of Commissioners. There may thus be instances where the Government's interests will conflict with ours. There is no assurance that the Government will not direct opportunities to Indosat or favor Indosat when exercising regulatory power over the Indonesian telecommunications industry. If the Government were to give priority to Indosat's business over ours or to expand its stake in Indosat, our business, financial condition, and results of operations and prospects could be materially and adversely affected.

## **B. Risks Related to Our Business**

### **1. Operational Risks**

*A material failure in the continuing operations of our network, certain key systems, gateways to our network or the networks of other network operators could adversely affect our business, financial condition, results of operations and prospects*

We depend to a significant degree on the uninterrupted operation of our network to provide our services. For example, we depend on access to our fixed wireline network ("PSTN") for the operation of our fixed line network and the termination and origination of cellular telephone calls to and from fixed line telephones, and a significant portion of our cellular and international long-distance call traffic is routed through the PSTN. We also depend on access to an internet and broadband network and a cellular network. Our integrated network includes a copper access network, fiber optic access network, BTSs, switching equipment, optical and radio transmission equipment, an IP core network, satellite and application servers.

In addition, we also rely on interconnection to the networks of other telecommunications operators to carry calls and data from our subscribers to the subscribers of operators both within Indonesia and overseas. We also depend on certain technologically sophisticated management information systems and other systems, such as our customer billing system, to enable us to conduct our operations. Our network, including our information systems, IT and infrastructure and the networks of other operators with whom our subscribers interconnected, are vulnerable to damage or interruptions in operation from a variety of sources including earthquake, fire, flood, power loss, equipment failure, network software flaws, transmission cable disruption or similar events.

Although we have a comprehensive BCP and DRP which we test and strive to improve, we cannot guarantee that the implementation of such plans will be completely or partially successful should any portion of network be severely damaged or interrupted. Any failure that results in an interruption of our operations or of the provision of any service, whether from operational disruption, natural disaster or otherwise, could adversely affect our business, financial condition, results of operations and prospects.

*Our networks, face both potential physical and cyber security threats, such as theft, vandalism and acts intended to disrupt operations, which could adversely affect our operating results*

Our networks and equipment, particularly our wireline access network, face both potential physical and cyber security threats. Physical threats include theft and vandalism of our equipment and organized attacks against key infrastructure intended to disrupt operations. In addition, telecommunications companies worldwide face increasing cyber security threats as businesses become increasingly dependent on telecommunications and computer networks and adopt cloud computing technologies. Cyber security threats include gaining unauthorized access to our systems or inserting computer viruses or malicious software in our systems to misappropriate consumer data and other sensitive information, corrupt our data or disrupt our operations. Unauthorized access may also be gained through traditional means such as the theft of laptop computers, portable data devices and mobile phones and intelligence gathering on employees with access.

Although we have not experienced any material successful cyber attacks to date that have affected our operations, our network and our website are frequently targeted by cyber attacks. A successful cyber attack may lead us to incur substantial costs to repair damage or restore data, implement substantial organizational changes and training to prevent future similar attacks and lost revenues and litigation costs due to misused sensitive information, and cause substantial reputational damage. We take preventive and remedial measures, including enhanced cooperation with the police, particularly in areas prone to criminal activity and regular upgrades of our data security measures. However, there is no assurance that our physical and cyber security measures will be successful. Damage to our network, equipment or data and the need to repair such damage resulting from a physical or cyber attack may materially and adversely affect our business, financial condition and operating results. Our networks face potential security threats, such as theft or vandalism, which could adversely affect our operating results.

*We face a number of risks relating to our internet-related services*

In addition to cyber security threats, because we provide connections to the internet and host websites for customers and develop internet content and applications, we may be perceived as being associated with the content carried over our network or displayed on websites that we host. We cannot and do not screen all of this content and may face litigation claims due to a perceived association with this content. These types of claims can be costly to defend, divert management resources and attention, and may damage our reputation.

*A revenue leakage might occur due to internal weaknesses or external factors and if this happened it could have an adverse effect on our operating results*

A revenue leakage is a generic risk for all telecommunications operators. We may face revenue leakage problems, or problems with collecting all the revenues to which we may be entitled, due to the possibility of weaknesses at the transactional level, delay in transaction processing, dishonest customers or other factors.

We have taken some preventive measures against the possibility of revenue leakage by increasing control functions in all of our existing business process, implementing revenue assurance methods, employing adequate policies and procedures as well as implementing information systems applications to minimize revenue leakages. Nonetheless, there is no assurance that in the future there will be no significant revenue leakages or that any such leakages will not have a material adverse affect on our operating results.

*New technologies may adversely affect our ability to remain competitive*

The telecommunications industry is characterized by rapid and significant changes in technology. We may face increasing competition due to technologies currently under development or which may be developed in the future. Future development or application of new or alternative technologies, services or standards could require significant changes to our business model, the development of new products, the provision of additional services and substantial new investments by us. New products and services may be expensive to develop and may result in the introduction of additional competitors into the marketplace. We cannot accurately predict how emerging and future technological changes will affect our operations or the competitiveness of our services. Furthermore, we cannot guarantee that we will be able to effectively integrate new technologies into our existing business model.

As part of our continuing development of our TIMES business, we continue to seek to develop businesses through which we also provide content to our telecommunications subscribers. We do not yet have substantial experience as a content provider therefore we cannot assure you that we will be able to effectively manage the growth of this business.

We cannot assure you that our technologies will not become obsolete, or be subjected to competition from new technologies in the future, or that we will be able to acquire new technologies necessary to compete in changed circumstances on commercially acceptable terms. Our failure to react to rapid technological changes could adversely affect our business, financial condition, results of operations and prospects.

*Our satellites have limited operational life they may be damaged or destroyed during in-orbit operation or suffer launch delays or failures. The loss or reduced performance of our satellites, whether caused by equipment failure or its license being revoked, may adversely affect our financial condition, results of operations and ability to provide certain services*

Our Telkom-1 and Telkom-2 satellites have a limited operational life, currently estimated to end approximately in 2015 and 2020, respectively. A number of factors affect the operational lives of satellites, including the quality of their construction, the durability of their systems, subsystems and component parts, on-board fuel reserves, accuracy of their launch into orbit, exposure to micrometeorite storms, or other natural events in space, collision with orbital debris, or the manner in which the satellite is monitored and operated. We currently use satellite transponder capacity on our satellites in connection with many aspects of our business, including direct leasing of such capacity and routing for our international long-distance and cellular services.

Moreover, International Telecommunication Union ("ITU") regulations specify that a designated satellite slot has been allocated for Indonesia, and the Government has the right to determine which party is licensed to use such slot. While we currently hold a license to use the designated satellite slot, in the event our Telkom-1 and Telkom-2 satellites experience technical problems or failure, the Government may determine that we have failed to optimize the existing slot under our license, which may result in the Government withdrawing our license. We cannot assure you that we will be able to maintain use of the designated satellite slot in a manner deemed satisfactory by the Government.

In anticipation of the growth in demand for satellite services and to support our business strategy with regard to providing TIME services, we signed a contract in 2009 for the procurement of the Telkom-3 Satellite System. However, due to a launch failure in August 2012, the Telkom-3 satellite ended up in an unusable orbit. Although we had fully insured the cost of the satellite, the loss of the Telkom-3 satellite will require us to lease transponder capacity from a third-party provider to fulfill our commitments to our satellite operations customers, with likely lower margins than we would have received from the use of Telkom-3 had it been successfully launched. We are currently in the initial phases for the procurement of a replacement satellite, the Telkom-3S, which is currently planned for launch in 2016. Although the Telkom-1 satellite may still be operational for several years after the end of its currently estimated operational lifespan in 2015, if there is any delay in the development and launch of the Telkom-3S, or if the operational life of the Telkom-1 satellite ends before the Telkom-3S is successfully launched, or damage or failure renders our existing satellites unfit for use, we would need to lease additional transponder capacity from a third party, which would likely increase our costs of operations. Failure to lease adequate satellite capacity from a third-party provider may also result in service interruptions and/or a cessation of our satellite operations. The termination of our satellite business could increase expenses associated with our provision of other telecommunications services, particularly in the eastern parts of Indonesia which currently rely largely on satellite coverage for telecommunications services, and could adversely affect our business, financial condition and results of operations.

## **2. Financial Risks**

### *We are exposed to interest rate risk*

Our debt includes bank borrowings to finance our operations. Where appropriate, we seek to minimize our interest rate risk exposure by entering into interest rate swap contracts to swap floating interest rates for fixed interest rates over the duration of certain of borrowings. However, our hedging policy may not adequately cover our exposure to interest rate fluctuations and this may result in a large interest expense and an adverse effect on our business, financial condition and results of operations.

Changes in the economic situation in the United States, including improvement or expectations of improvement in the U.S. economy, may also have an impact on Southeast Asia and Indonesia. Expectations of the United States Federal Reserve tapering its bond buying program on an improving economy resulted in, among other things, the weakening of equity and bond markets around the world and a number of Asian currencies including the Rupiah since May 2013. In part, in an effort to support the Rupiah, particularly around May and June 2013, Bank Indonesia began raising its benchmark reference rate from a record low of 5.75% which was set in February 2012. The benchmark reference rate has since risen four times between June and November 2013 by an aggregate of 1,175 basis points to 7.5%. The increase of Bank Indonesia reference rate was followed by increases in the JIBOR and Bank Indonesia Certificate ("SBI") interest rates. It is uncertain how the global markets and the Rupiah may be affected as the United States Federal Reserve continues the tapering of its bond buying program. There can be no assurance that the Bank Indonesia reference rate, JIBOR or SBI rate will not continue to rise in the future.

### *We may not be able to successfully manage our foreign currency exchange risk*

Changes in exchange rates have affected and may continue to affect our financial condition and results of operations. Most of our debt obligations are denominated in Rupiah and a majority of our capital expenditures are denominated in US Dollars. Most of our revenues are denominated in Rupiah and a portion is denominated in US Dollars (for example from international services). We may also incur additional long-term indebtedness in currencies other than the Rupiah, including the US Dollars, to finance further capital expenditures.

Overall, our financial risk management program aims to minimize losses on the financial assets and financial liabilities arising from fluctuation of foreign currency exchange rates. We have a written policy for foreign currency risk management, which mainly covers time deposits placements and hedging to cover foreign currency risk exposure for periods ranging from three up to twelve months.

The exchange rate of Rupiah weakened relative to the US Dollar in 2013, and in the future, we can give no assurance that we will be able to manage our exchange rate risk successfully or that our business, financial condition or results of operations will not be adversely affected by our exposure to exchange rate risk.

### *We may be unable to fund the capital expenditures needed for us to remain competitive in the telecommunications industry in Indonesia*

The delivery of telecommunications services is capital intensive. In order to be competitive, we must continually expand, modernize and update our telecommunications infrastructure technology, which involves substantial capital investment. For the years ended December 31, 2011, 2012 and 2013, our actual consolidated capital expenditures totaled Rp14,603 billion, Rp17,272 billion and Rp24,898 billion (US\$2,046 million), respectively. Our ability to fund capital expenditures in the future will depend on our future operating performance, which is subject to prevailing economic conditions, levels of interest rates and financial, business and other factors, many of which are beyond our control, and upon our ability to obtain additional external financing. We cannot assure you that additional financing will be available to us on commercially acceptable terms, or at all. In addition, we can only incur additional financing in compliance with the terms of our debt agreements. Accordingly, we cannot assure you that we will have sufficient capital resources to improve or expand our telecommunications infrastructure technology or update our other technology to the extent necessary to remain competitive in the Indonesian telecommunications market. Our failure to do so could have a material adverse effect on our business, financial condition, results of operations and prospects.



### 3. Legal and Compliance Risks

*If we are found liable for price fixing by the Indonesian Anti-Monopoly Committee and for class action allegations, we may be subject to substantial liability which could lead to a decrease in our revenue and affect our business, reputation and profitability*

On June 17, 2008, the Commission for the Supervision of Business Competition ("KPPU") determined that our Company, Telkomsel, PT XL Axiata Tbk. ("XL"), PT Bakrie Telecom Tbk. ("Bakrie Telecom"), PT Mobile-8 Telecom Tbk. ("Mobile-8") and PT Smart Telecom ("Smart Telecom") had jointly breached Article 5 of Law No.5/1999. We and Telkomsel appealed the KPPU's ruling to the Bandung District Court and the South Jakarta District Court, respectively. On April 12, 2011, the Supreme Court ordered a consolidation of the appeals and appointed the Central Jakarta District Court to handle the appeals. Neither we nor Telkomsel has received any notification from the court with respect to the resolution of this case. See Item 8 "Financial Information - Consolidated Statements and Other Financial Information - Material Litigation". If the District Court issues a verdict against our Company and/or Telkomsel, we could be subjected to the payment of a fine, the amount of which will be subject to the discretion of the District Court, which could have an adverse effect on our business, reputation and profitability.

Class action lawsuits were filed against Telkomsel and Indosat during 2007 and 2008 in the District Court of Bekasi, the Central Jakarta District Court and the Tangerang District Court, relating to Temasek Holdings (Private) Limited's prior cross ownership of shares in Telkomsel and Indosat, alleging price fixing of telecommunications services. The plaintiffs withdrew the lawsuit filed with the District Court of Bekasi. On January 27, 2010, the court dismissed the class action filed with the Central Jakarta District Court on the basis that the plaintiffs did not establish their legal standing and that two members of the plaintiff class did not qualify as class representatives. On May 24, 2010, the court dismissed the class action filed with the Tangerang District Court on the basis that the plaintiffs failed to establish their legal standing as class representatives.

There can be no assurance that other subscribers, people, or partners will not file similar cases in the future. If a District Court in any new class action suit, issues a verdict in favor of such plaintiff, it could have an adverse effect on our business, reputation and profitability.

*Forward-looking statements may not be accurate*

This Annual Report incorporates forward-looking statements that include announcements regarding our current goals and projections of our operational performance and future business prospects. The words "believe", "expect", "anticipate", "estimate", "project" and similar words identify forward-looking statements. In addition, all statements, other than statements that contain historical facts, are forward-looking statements. While we believe that the expectations contained in these statements are reasonable, we cannot give an assurance that they will be realized. These forward-looking statements are subjected to a number of risks and uncertainties, including changes in the economic, social and political situation in Indonesia and other risks described in "Risk Factors". All forward-looking statements, written or verbal, made by us or by persons on behalf of us are deemed to be subject to those risks.

### 4. Regulation Risks

*We operate in a legal and regulatory environment that is undergoing significant change. These changes may result in increased competition, which may result in reduced margins and operating revenue, among other things. These changes may also directly reduce our margins or reduce the costs of our competitors. These adverse changes resulting from regulation may have a material adverse effect on us*

Reformation in Indonesian telecommunications regulation initiated by the Government in 1999 has, to a certain extent, resulted in the industry's liberalization, including removal of barriers to entry and the promotion of competition. However, in recent years, the volume and complexity of regulatory changes has created an environment of considerable regulatory uncertainty. In addition, as the legal and regulatory environment of the Indonesian telecommunications sector continues to change, competitors, potentially with greater resources than us, may enter the Indonesian telecommunications sector and compete with us in providing telecommunications services. Furthermore, it is impossible to anticipate the regulatory policies that will be applied to new technologies.

We derive substantial revenue from interconnection services because we have the largest network in Indonesia and our competitors must pay tariffs to connect to our network. As regulated by the MoCI, interconnection rates have decreased in recent years. The current interconnection rates, effective in 2011, reduced rates by an average of 1.5% to 3.0% compared to the previous rates effective in 2008. See Item 4 "Information on the Company - Distribution and Marketing Strategy - Legal Basis and Regulation - Interconnection".

The termination of Telkomsel's premium SMS services from October 2011 as a result of MoCI Regulation No.1/PER/M.KOMINFO/01/2009 resulted in a substantial reduction in our revenues from these services. These services have been resumed by Telkomsel from August 6, 2013 as allowed under MoCI Regulation No.21 year of 2013 dated July 26, 2013, regarding the Operation of Content Provider Services on Mobile Cellular Network and Local Fixed Wireless Network with Limited Mobility, which replaced MoCI Regulation No.1/PER/M.KOMINFO/01/2009. However, pursuant to the new decree, premium SMS service providers are required to meet stricter requirements that are more difficult to comply with. Accordingly we do not expect revenues from premium SMS services to return to levels seen prior to October 2011.

In the future, the Government may announce or implement other regulatory changes which may adversely affect our business or our existing licenses. We cannot assure you that we will be able to compete successfully with other domestic and foreign telecommunications operators, that regulatory changes will not disproportionately reduce our competitors' costs or disproportionately reduce our revenues, or that regulatory changes, amendments or interpretations of current or future laws and regulations promulgated by the Government will not have a material adverse effect on our business and operating results.

*The entry of additional Indonesian telecommunications operators as providers of international direct dialing services could adversely affect our international telecommunications services operating margins, market share and results of operations*

We obtained a license and entered the international long-distance service market in 2004, and acquired a significant market share for IDD services by the end of 2006. Indosat, one of our primary competitors, entered this market prior to us and continues to maintain a substantial market share for IDD services. Bakrie Telecom was awarded an IDD license in 2009 to provide international long distance service using the "009" access code. There is a possibility that other operators will be granted IDD licenses in the future. The operations of incumbents and the entrance of new operators into the international long-distance market, including the VoIP services provided by such operators, continue to pose a significant competitive threat to us. We cannot assure you that such adverse effects will not continue or that such increased competition will not continue to erode our market share or adversely affect our fixed telecommunications services operating margins and results of operations.

*We face risks related to the opening of new long distance access codes*

In an attempt to liberalize DLD services, the Government issued regulations assigning each provider of DLD services a three-digit access code to be dialed by customers making DLD calls. In 2005, the MoCI announced that three-digit access codes for DLD calls will be implemented gradually within five years and that it would assign us the "017" DLD access code for five major cities, including Jakarta, and allow us to progressively extend it to all other area codes. Indosat was assigned "011" as its DLD access code. We were required to open DLD access codes in all remaining areas on September 27, 2011, by which date our network was ready to be opened up to the three-digit DLD access codes in all coded areas throughout Indonesia.

However, we believe that the cost for operators who have not upgraded their network infrastructure to open their networks to the three-digit access codes to do so is significant. To date, neither of the OLOs have made a request to us to connect their networks to enable their DLD access codes to be accessible, other than with respect to Balikpapan, and as such, we believe that except with respect to Balikpapan, none of the DLD access codes for any of the licensed operators are usable by customers of other operators. However, if they do so in the future, the implementation of any new DLD access codes can potentially increase competition by offering our subscribers more options for DLD services. In addition, the opening of new DLD access codes is expected to result in increased competition and less cooperation among industry incumbents, which may result in reduced margins and revenues, among other things, all of which may have a material adverse effect on us.

*New regulations for the configuration of BTS towers may delay the set up of new BTS towers or changes in the placement of existing towers, and may erode our leadership position by requiring us to share our towers with our competitors*

In 2008 and 2009, the Government issued regulations relating to the construction, utilization and sharing of BTS towers. Pursuant to the regulations, the construction of BTS towers requires permits from the local government. The local government has a right to determine the placement of the towers, the location in which the towers can be constructed, and also to determine a license fees to build tower infrastructure. These regulations also obligate us to allow other telecommunication operators to lease space and utilize our telecommunications towers without any discrimination.

These regulations may adversely affect in the allocation, development or expansion plan of our new BTS towers as setting up of our new towers will become more complicated. They may also adversely affect our existing BTS towers if local governments required any changes in the placement of the existing towers.

The requirement that we share space on our cellular (Telkomsel) towers and our fixed wireless (Telkom Flexi) towers may also disadvantage us by requiring that we allow our competitors to expand quickly, particularly in urban areas where new space for additional towers may be difficult to obtain.

Effective 2011, local Governments are permitted to assess fees of up to 2.0% of the tax assessed value of towers. Although we do not expect the amount of these fees to be material in 2013, there can be no assurance that they will not be substantial in the future.

#### **5. Risks Related to Our Fixed Telecommunication Business**

*We may further lose wireline telephone subscribers and revenues derived from our wireline voice services may continue to decline, which may materially adversely affect our results of operations, financial condition and prospects*

Revenues derived from our wireline voice services continued to decline during the past several years mainly due to the increasing popularity of mobile voice services and other alternative means of communication, such as VoIP. Tariffs for mobile services have declined in recent years which has further accelerated substitution of mobile for wireline voice services. While the number of our fixed wireline subscribers increased by 4.0% at the end of 2012 and by 4.5% at the end of 2013, revenues from our wireline voice services decreased by 8.2% in 2012 and by 8.3% in 2013. The percentage of revenues derived from our wireline voice services out of our total revenues continued to decrease from 12.2% in 2012 to 10.4% in 2013.

We have been taking various measures in order to stabilize our revenues from wireline voice services. However, we cannot assure you that we will be successful in mitigating the adverse impact of the substitution of mobile voice services and other alternative means of communication for wireline voice services or in reducing the rate of decline in our revenues generated from wireline voice services. Migration from wireline voice services to mobile services and other alternative means of communication may further intensify in the future, which may affect the financial performance of our wireline voice services and thus materially and adversely affect our results of operations, financial condition and prospects as a whole.

*Our fixed wireless business is in decline and this decline is likely to continue*

Due to competition and the increasing popularity of mobile cellular platforms, our fixed wireless revenues and ARPU has been declining in recent years.

While fixed wireless tariffs historically were generally lower than GSM mobile cellular tariffs, in part due to regulatory changes in December 2010 in how right-of-use fees are calculated, tariff differences between fixed wireless services and GSM mobile cellular services are now generally negligible. In addition, there is limited frequency bandwidth of 5 MHz available for our fixed wireless platform, and the GSM platform is generally able to make more efficient use of frequency bandwidth. As a result, in 2013, we did not further develop our fixed wireless network (other than optimize existing BTSS for our fixed wireless network), and did not conduct any new product launches or promotional campaigns activities for this service. We do not plan to further develop our fixed wireless network in any significant way in the future.

As a result of above factors, and as we also undertook an exercise to remove inactive Telkom Flexi subscribers in late 2013 so that they are no longer recorded on our system as connections in service, the number of our fixed wireless connections in service declined sharply in 2013, from approximately 14.2 million as of December 31, 2011 and 17.9 million as of December 31, 2012 to 6.8 million as of December 31, 2013.

Our fixed wireless business has also seen lower average tariffs due to intense competition from the cellular market which has led to declining ARPU for Telkom Flexi, with blended monthly prepaid and postpaid ARPU decreasing from approximately Rp9,500 in 2011 to Rp8,700 in 2012 and Rp8,400 in 2013. As a result of the above factors, revenue from our fixed wireless revenue has declined, from Rp1,342 billion as of December 31, 2011 to Rp1,225 billion as of December 31, 2012 and Rp1,051 billion as of December 31, 2013. We expect that this declining trend will continue.

We plan to undertake a strategy to migrate our fixed wireless customers to our mobile cellular platform by offering promotional packages. However, we cannot assure you that we will be successful in this migration, as competition from other mobile cellular providers is intense. If we are not able to successfully migrate our fixed wireless users to our mobile cellular platform as and when they decide to migrate to another platform, it may adversely affect our results of operations, financial condition and prospects as a whole.

*Our data and internet services are facing increasing competition, and we may experience declining margins from such services as such competition intensifies*

Our data and internet services are facing increase competition from other data and internet operators as well as mobile operators.

Wireless broadband access operators that received licenses in 2009 for Wi-Max technology began to establish their businesses in the fourth quarter of 2010 (for instance First Media) and in 2012 (Berca). In 2013, the regulator has permitted the Wi-Max operators to deploy the Long Term Evolution ("LTE") technology. This will adversely affect our market share and revenues from our Speedy broadband service. The number of broadband mobile subscribers have increased with the Blackberry's popularity. The increasing use of mobile broadband services also adversely affects our market share and revenues from our fixed data and internet services.

We have been taking various measures in order to mitigate the impact of intense competition in our data and internet businesses. However, we cannot assure you that we will be successful in mitigating such adverse impact. Competition may further intensify in the future, which may affect the financial performance of our data and internet services and thus materially and adversely affect our results of operations, financial condition and prospects as a whole.

#### **6. Competition Risks Related to Our Cellular Business (Telkomsel)**

*Competition from existing service providers and new market entrants may adversely affect our cellular services business*

The Indonesian cellular services business is highly competitive. Competition among cellular services providers in Indonesia is based on various factors, including pricing, network quality and coverage, the range of services, features offered and customer service. Our cellular services business, operated through our majority-owned subsidiary, Telkomsel, competes primarily against Indosat and XL. Several other smaller GSM and CDMA operators also provide cellular services in Indonesia, including PT Hutchison CP Telecommunications ("Hutchison"), PT Natrindo Telepon Seluler ("Natrindo" or "AXIS"), Smart Telecom and Bakrie Telecom. In addition to current cellular service providers, the MoCI may license additional cellular service providers in the future, and such new entrants may compete with us.

In March 2010, Smart Telecom and Mobile-8 announced the signing of a cooperation agreement to use the same logo and brand under the brand name "Smartfren". On January 18, 2011, Mobile-8 acquired a significant number of shares in Smart Telecom, and on April 12, 2011 PT Mobile-8 Telecom Tbk. changed its name to PT Smartfren Telecom Tbk. In subsequent developments, XL has plans for the acquisition of Natrindo (Axis). On September 29, 2013, XL-Axiata has signed a CSPA with Axis for the acquisition of Axis' shareholders. The strategic acquisition will position XL as the second largest operator while also acquiring additional frequency allocations to facilitate the roadmap to LTE (4G) technology. Further operator consolidation is likely in order to ensure that each operator can remain competitive, reduce operational costs, and also to "rebalance" the broadband mobile frequency spectrum that require wider frequency bandwidth. The MoCI also supports operator consolidation, as it has been reluctant in recent years to issue new licenses for cellular players.

While operator consolidation may lead to improved conditions in the cellular telecommunication industry, it also present challenges for Telkomsel in maintaining its market position.

**7. Risks Related to Development of New Businesses**

We believe that efforts to develop new businesses other than our telecommunication business as well as international expansion are necessary to ensure continuing business growth. We plan to undertake these activities through our subsidiaries, Metra and TII. Risks related to new business development include competition from established players, suitability of business model, the need to acquire new expertise in the new areas of operation, and risks related to online media (such as risks relating to intellectual property, consumer protection and confidentiality of customer data).

Focusing on international expansion is one of our strategic business initiatives. In particular, we have already started expansion into seven countries, namely Hong Kong-Macau, Timor Leste, Australia, Myanmar, Malaysia, Taiwan, and United States of America through our subsidiary, TII. Expanding our operations internationally exposes us to a number of risks associated with operating in new jurisdictions for example, our international operations could be adversely affected by political, or social instability and unrest, by regulatory changes, such as an increase in taxes applicable to our operations, macroeconomic instability, limitations on or controls on the foreign exchange trade, competition from local operators, difference in consumer preferences and a lack of expertise in the local markets in which we will be operation. Any of these factors could cause our expected returns from our expansion to be limited and could have a material and adverse effect on our business, results of operations and financial condition.

**ITEM 4. INFORMATION ON THE COMPANY**

**A. HISTORY AND DEVELOPMENT OF THE COMPANY**

We are a limited liability company incorporated under the laws of Indonesia and domiciled in Bandung. We trade under the legal name “Perusahaan Perseroan (Persero) PT Telekomunikasi Indonesia Tbk” and with the commercial name “Telkom”. We were converted from a state agency to a State-Owned Enterprise on September 24, 1991 and obtained status as a legal entity on November 19, 1991 for an indefinite period of time. Our registered office is located at Jl. Japati No.1, Bandung 40133, Indonesia, and our telephone number is +(62) (21) 521 5109. Our agent for service of process in the United States with respect to our ADSs is Puglisi & Associate at 850 Library Avenue, Suite 204, Newark, DE, 19711. Our corporate website may be accessed at [www.telkom.co.id](http://www.telkom.co.id). The information found on our corporate website does not form part of this Form 20-F and is not incorporated by reference herein. Information about the legislation under which we operate is provided elsewhere in this Form 20-F. A description, including the amount invested, of our principal capital expenditures and divestitures (including interests in other companies), since the beginning of our last three financial years and information concerning our principal capital expenditures is contained elsewhere in this Form 20-F.

A description of our principal capital expenditures and divestitures, since the beginning of the last three financial years to the date of this Annual Report is set forth in Item 5 “Operating and Financial Review and Prospects – Liquidity – Capital Expenditures”. Information concerning our principal capital expenditures and divestitures currently in progress is also described in Item 5 “Operating and Financial Review and Prospects – Liquidity – Capital Expenditures”.

We are a State-Owned Enterprise that operates in the telecommunications and network services sector in Indonesia. Our history and certain information required by Item 4 of Form 20-F is as follows:

**History of Telkom**

**1856-1882**

On October 23, 1856, the Dutch colonial government deployed the first electromagnetic telegraph in Indonesia, connecting Batavia (Jakarta) with Buitenzorg (Bogor).

**1906-1965**

The Dutch colonial government established a government agency to operate post and telecommunications services in Indonesia. In 1965, the post and telecommunications services were separated and brought under the control of two state companies, PN Pos and Giro and PN Telekomunikasi.

**1974**

PN Telekomunikasi was split into two divisions, PT Industri Telekomunikasi Indonesia (“PT INTI”), which manufactured telecommunications equipment, and Perusahaan Umum Telekomunikasi (“Perumtel”), which supplied domestic and international telecommunication services.