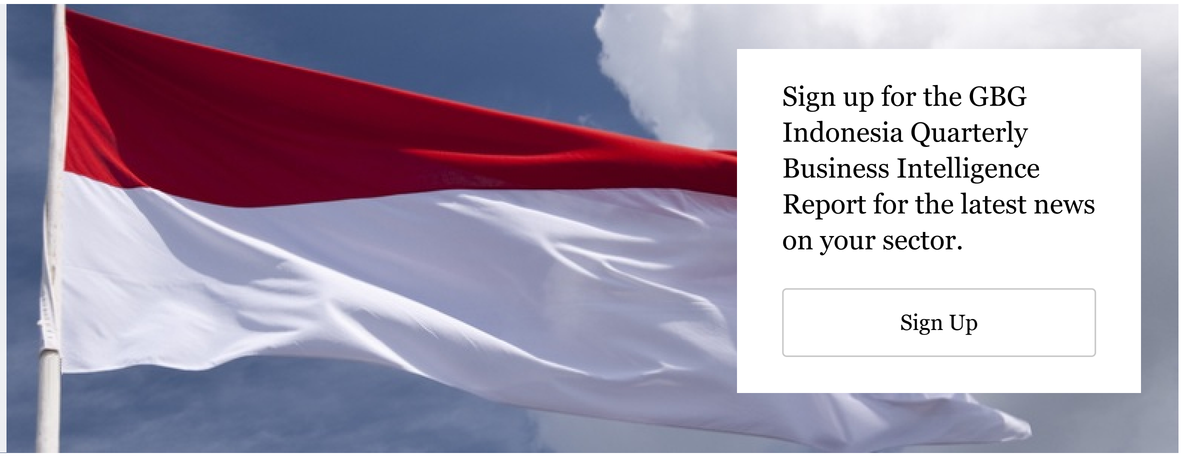



# BUSINESS UPDATES | The Question Of Indonesia's Unprocessed Ore Export Ban – Updated

Faced with a swelling current account deficit, the Indonesian government is in the process of revising its stance on existing and impending regulations that would see a ban on the export of unprocessed mining products by 2014. As approximately 17% of the country's exports by value are derived from the mining sector, government officials have been forced to question the viability of introducing an export ban on unprocessed mineral and metal ores in 2014 given its potential to exacerbate the widening gap between exports and imports. Though a complete reversal in regulation is unlikely, several intermediate options have been tabled, including a proposed delay to the export ban with the caveat that the government would increase export levies up to 50% on unprocessed ore from the current 20%. A further proposal currently being mulled by the Ministry of Industry is granting companies that have already made binding agreements to process ore in Indonesia or have broken ground on smelter projects, the right to engage in limited exports of unprocessed commodities.

Placing the current issue within its historical context of a shifting regulatory landscape; in 2012 the Indonesian government enacted a number of amendments to the export-friendly Law No. 04 of 2009 regarding Mineral and Coal Mining. Motivated by a need to guarantee the availability of raw materials for domestic purposes and thus develop the country's value added processing sector, this was followed by Ministry of Energy and Mineral Resources regulations ('EDSM Regulation No. 07/2012' and 'EDSM Regulation No.11/2012'). Such regulations require mining companies in Indonesia to refine and/or smelt unprocessed mineral ore domestically instead of exporting it to be processed abroad, in lieu of the impending export ban scheduled for implementation in January 2014.

Industry analysts have voiced their concerns over the negative impact of regulatory uncertainty in the mining sector on much needed foreign investors. While the ongoing uncertainty will lead to reluctance among foreign investors in the upstream sector for the immediate term, this should not dampen enthusiasm for the potential of Indonesia's downstream minerals and metals sector. Nor should this be regarded as a departure from the government's overarching strategy to develop value added processing of mining products and its willingness to provide incentives for doing so. The current situation and widely predicted easing of export restrictions and nationalist minded policies may well provide the much needed leeway required to further promote the development of the downstream processing industry. This could avoid the inevitable bottlenecks that a blanket ban would bring about given the lack of readily available processing and smelting facilities.

## Indonesia Snapshot

Capital: Jakarta
Population: 259 million (2016)
Currency: Indonesian Rupiah
Nominal GDP: $936 billion USD (IMF, 2016)
GDP Per Capita: $3,620 USD at Current Prices (IMF, 2016)
GDP Growth: 5.0% (2016)
External Debt: 36.80% of GDP (BI, Q2 2016)
Ease of Doing Business: 91/190 (WB, 2017)
Corruption Index: 90/176 (TI, 2016)

## Interview Highlights

**Gunung Putri Graha Mas**
Mr Wisnu Sanjaya
Fibreglass

**DEN Indonesia**
Mr Mugi Rahardjo
Boiler Manufacture & Engineering Services

**Thaha Engineering**
Mr M.H. Thaha
Engineering, Procurement & Construction

The challenge faced by the mining industry is that the volume of unprocessed metals and minerals being produced exceeds the capacity of existing processing infrastructure. Greenfield smelter projects are also highly capital intensive, while the potential margins on the processing of metals such as copper offer poor commercial prospects. However, the Indonesian market does offer considerable scope for growth in the domestic consumption of a number of key downstream mining products. Driven by rapid urban development and a plan to implement a construction-intensive infrastructural connectivity program by 2025, Indonesia's annual steel consumption reached 10.4 million MT in 2012 (Indonesia Iron and Steel Industry Association), making it the second largest consumer in the ASEAN. Opportunities in other industries are equally promising, with stainless steel consumption in Indonesia projected to increase from 1 kg per capita in 2010 to a level on par with that of China and South Korea at 25 kg per capita (World Steel Organisation). The government has also introduced a number of incentives to attract foreign investors into the sector which is classified as a pioneer industry (See New Tax Incentives for Investors in Indonesia). As per the Negative Investment List, smelters may be 100% foreign owned and unlike upstream mining license holders, investors are not required to divest shares to Indonesian stakeholders after the prescribed five and ten years. Multinational as well as local companies have been swift to take advantage of the potentially lucrative opportunities on offer such as a Singaporean mining firm Ibris Group's $1.8 billion USD nickel pig iron smelter plant and a $1 billion USD nickel pig iron smelter as a joint venture between PT Sulawesi Mining Investment and China's Tsingshan Group.

Despite the short term uncertainty and backtracking on existing policies, the Indonesian government remains committed to the development of the downstream processing sector as part of its long term strategy to move Indonesian industry up the value chain. Furthermore, postponing the complete export ban on unprocessed commodities while actively incentivising investment in the sector will facilitate the development of a competitive domestic value added industry better prepared for the task of processing the entirety of Indonesia's mining output. Foreign investors should also be buoyed by the recent market corrections of the Rupiah that are advantageous to companies seeking export oriented opportunities in South East Asia's largest economy.

**Updated - 2nd January 2014**

Indonesia is fast approaching a 12th January 2014 deadline by which it must resolve issues that continue to plague the country's implementation of amendments to Law No. 04 of 2009 regarding Mineral and Coal Mining. Should the deadline pass without any further revisions or additions to existing regulations, a blanket ban will be placed on all mineral ore exports irrespective of whether a company already processes and smelts some of its ore domestically. As such, mounting pressure to postpone or revise the all-encompassing ban is being led by Freeport Indonesia and Newmont Nusa Tenggara. Both insist that their existing agreements to supply concentrate to local smelters should grant them the right to export the rest of their unprocessed ore given the lack of smelting and processing facilities in Indonesia ready to take on additional metal concentrate.

Aware of the implications that the ban will have on the economy if it comes into effect as is, the government has sought to ease the impending regulation where possible. On 27th December 2013, Minister of Energy and Mining Mr Jero Wacik reported that the export ban would only apply for mining companies that still do not process and smelt in Indonesia and that firms already supplying local smelters would receive exemptions. It was also explained that the government was in the midst of working on a new regulation to be introduced prior to 12th January that will act as the legal basis for this revision.

However, on 2nd January 2014, Mr R. Sukhyar, Director General of Coal and Mineral Resources at the Ministry of Energy and Mining, asserted that no exemptions were going to be made prior to the upcoming deadline and that it was a non-negotiable fact that mineral ore from Indonesia could not be exported under any circumstances unless processed domestically. Meanwhile, representatives from the mining industry have sought consultation from the Supreme Court to provide clarity as to whether the government plans to introduce a special regulation prior to the ban coming into effect. As the deadline looms ever closer, this situation promises to come to a conclusion shortly and will have a significant bearing on the economy's prospects and outlook for 2014.

**Updated - 30th June 2014**

Indonesia on 12th January 2014 formally put into effect a series of regulations that curb the export of unprocessed minerals following the implementation of Government Regulation No. 1/2014, Ministry of Energy and Mineral Resources (MoEMR) Regulation No. 1/ 2014 and Ministry of Finance (MoF) Regulation No. 6/2014. Though these laws mandate a complete and immediate ban on raw ore exports, they also allow for the continued export of several mineral concentrates, which are instead subject to a rise in export duties. In steering clear of a blanket ban on all unprocessed mineral exports, this course of action has by and large been viewed as a compromise that provides exporters of mineral concentrates with more time to establish smelters.

The specific details of the export duties levied against mineral concentrates are laid out in the aforementioned MoF Regulation No. 6/2014. Though less of a challenge to export oriented mining companies in Indonesia compared to a full ban; the new export duty is by no means inconsequential - starting from 20-25% of export revenues with incremental hikes every semester until July 2016 when it reaches 60%. Moreover, mineral concentrates will become subject to a full export ban on 11th January 2017; bringing to an end a three year period in which mining companies are expected to develop their own smelting operations. The timetable for the progressively increasing export duty, which varies for different types of mineral concentrates, can be seen in the table below:

**Export Duty on Mineral Concentrates as per MoF Reg. No. 6/2014**

| | Export Duty Tariff | | | | | |
|---|---|---|---|---|---|---|
| | 2014 | | 2015 | | 2016 | |
| Mineral | Sem. 1 | Sem. 2 | Sem. 1 | Sem.2 | Sem. 1 | Sem. 2 |
| Copper concentrate (> = 15% Cu) | 25% | 25% | 35% | 40% | 50% | 60% |
| Iron concentrate (> = 62% Fe) | 20% | 20% | 30% | 40% | 50% | 60% |
| Iron concentrate (> = 51% Fe and $Al_2O_3 + SiO_2$ > = 10%) | 20% | 20% | 30% | 40% | 50% | 60% |
| Manganese concentrate (> = 49% Mn) | 20% | 20% | 30% | 40% | 50% | 60% |
| Lead concentrate (> = 57% Pb) | 20% | 20% | 30% | 40% | 50% | 60% |
| Zinc concentrate (> = 52% Zn) | 20% | 20% | 30% | 40% | 50% | 60% |
| Ilmenite concentrate (> = 58% iron sand and 56% pellet) | 20% | 20% | 30% | 40% | 50% | 60% |
| Titanium concentrate (> = 58% iron sand and > = 56% pellet) | 20% | 20% | 30% | 40% | 50% | 60% |

*Source: PwC Indonesia, Ministry of Finance*

Resistance to the rise in export duties put forward in MoF Regulation No. 6/2014 has been led by Freeport-McMoRan Copper & Gold Inc and Newmont Mining Corp., who claim that paying any additional taxes would violate their mining contracts. In response to this, the government in June 2014 intimated that it would draft a new mining export tax set at a rate less than half of the export tariff under current regulation. Most importantly, to incentivize domestic mineral processing activity, only firms that have made progress in building a smelter would be eligible for the lower tax, which is levied on a sliding scale depending upon the extent of said progress.

Initial reports from the Director General of Minerals and Coal at the MoEMR suggest that the new export duty tariff will be set at a rate below 10%. Mining companies yet to have made progress in building a smelter are to continue to be taxed in accordance with MoF Regulation No. 6/2014. Having previously refused to accept additional export tariffs of any kind, it remains to be seen as to whether the mining industry's largest players will agree to this lower export tariff.

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