# Indonesia's Coal Production Up 11 Percent in 2003


## Summary

Indonesia's coal production increased 11 percent in 2003, despite continued uncertainty in the mining industry over legal and tax issues. China's decision to halt coal exports, coupled with rising Japanese coal imports, caused the production increase by raising international coal prices. High tax rates, divestment concerns and the lack of a new mining law are driving large Western companies out of the coal sector, while Chinese companies are stepping in to fill the void. The GOI must address these policy issues in order to increase investment and restore the long-term health of the industry.


Coal production reached 114 million metric tons (MT) in 2003, an increase of nearly 11 percent over the year before. Rising coal prices drove the production increase. Between April 2003 and December 2003 the price of coal rose nearly 60 percent, from $22.75 per metric ton (MT) to $36.00/MT. To take advantage of the higher prices, all major coal producers boosted production, with the exception of Kaltim Prima Coal (KPC) in East Kalimantan. Following the company's sale by co-owners Rio Tinto and BP to local company Bumi Resources, KPC workers went on strike for three weeks in September 2003, disrupting operations and causing the company to declare force majeure.

### Coal Production Statistics (in thousands MT)

| Company | 2001 | 2002 | 2003 | %Change |
|---|---|---|---|---|
| PTBA (state-owned) | 10,212 | 9,482 | 10,027 | 5.8 |
| Adaro Indonesia | 17,708 | 20,819 | 22,523 | 8.2 |
| Kaltim Prima Coal | 15,528 | 17,577 | 16,203 | -7.8 |
| Kideco | 10,381 | 11,500 | 14,056 | 22.2 |
| Arutmin | 9,532 | 10,557 | 13,615 | 29 |
| Berau Coal | 6,750 | 7,123 | 7,360 | 3.3 |
| Indominco Mandiri | 4,435 | 5,335 | 6,327 | 18.6 |
| Other CCOWs | 12,195 | 14,168 | 16,217 | 14.5 |
| Local cooperatives | 5,806 | 6,811 | 8,282 | 21.6 |
| **TOTAL** | **92,546** | **103,372** | **114,610** | **10.9** |

*Note: CCOW refers to companies with coal contracts of work. Local cooperatives are small coal mining firms that obtain concessions at the regional level.*

*Source: Directorate of Mineral and Coal Enterprises*

## Coal Exports Up 15 Percent

Coal exports also jumped by 13 million tons, Indonesia's entire production increase. This increase, however, is just a small portion of the estimated 100 million tons taken out of the international market by China's 2003 decision to halt coal exports. PT Bumi Resources, which owns KPC as well as the Arutmin coal mine, is now Indonesia's leading coal producer and exporter. Japan and Taiwan remain Indonesia's primary coal markets, accounting for over 40 percent of exports, followed by South Korea, the Philippines, Hong Kong and Malaysia (the U.S. receives about one percent of Indonesian coal exports).

### Coal Export Statistics (in thousands MT)

| Company | 2001 | 2002 | 2003 | %Change |
|---|---|---|---|---|
| PTBA (state-owned) | 1,895 | 1,855 | 2,239 | 20.7 |
| Kaltim Prima Coal | 15,079 | 16,629 | 16,034 | -3.6 |
| Adaro Indonesia | 11,446 | 12,688 | 15,187 | 19.7 |
| Arutmin | 9,247 | 9,858 | 13,772 | 40.2 |
| Kideco Jaya Agung | 7,321 | 6,750 | 8,942 | 32.5 |
| Indominco Mandiri | 4,371 | 5,334 | 4,887 | -8.4 |
| Berau Coal | 4,415 | 5,072 | 5,349 | 5.5 |
| Other CCOWs | 8,770 | 9,954 | 12,216 | 19.7 |
| Local cooperatives | 3,971 | 4,314 | 7,055 | 21.2 |
| TOTAL | 66,517 | 72,454 | 85,681 | 15.5 |

*Source: Directorate of Mineral and Coal Enterprises*

## Coal-Fired Power Drives Domestic Demand

Domestic coal demand rose five percent to 30.7 million MT in 2003. Coal-fired power plants remained the single largest consumers, accounting for about 19.5 million MT, or 64 percent of total demand. Cement plants were the second largest consumers at about 16 percent. The pulp industry registered a surprising 240 percent jump in coal use, from 500,000 tons to 1.7 million tons. One pulp company accounted for nearly all of the coal use increase; however, there was with no corresponding rise in pulp production. Industry observers speculate the company may have sold the $25/ton, domestically-purchased coal on the international market for profit.

The desire to profit from this price difference has affected the domestic power industry as well. When PTBA suffered coal transport problems from its South Sumatra mine to West Java's large Suralaya coal-fired plant in December 2003, East Kalimantan coal companies were reluctant to help. The companies complained that shifting potential exports for domestic use would hurt their profits. As a result, the Suralaya plant has only averaged 2200 out of 3400 megawatts of power generation between December 2003 and May 2004. This greatly reduced Java's power reserve margin and increased the frequency of rotating power outages on the Java-Bali grid.

## Westerners Out, Chinese In?

The coal sector witnessed the departure of two large Western firms last year. In October, Australia's Rio Tinto and Anglo-American BP sold their ownership in Indonesia's largest coal exporter, KPC, to local firm PT Bumi Resources for $500 million. The sale followed two years of combative, unsuccessful negotiations between KPC's Western owners and the GOI to divest 51 percent of the coal company's shares as required in its first-generation Coal Contract of Work (CCOW). Their decision to sell illustrates the difficult operating and investment climate for even established mining companies in Indonesia.

The Chinese, however, seem ready and willing to do business in this high-risk climate. Local firm PT Indika Inti Corpindo, with backing by power giant China Huadian Group, seeks to acquire major stakes in East Kalimantan companies Berau Coal and Kideco Jaya Agung. Indika may buy 60 percent of Berau Coal from United Tractors for $45 million and a 36 percent stake of Kideco for an undisclosed amount. The two companies account for 19 percent of Indonesia's coal production. In Central Kalimantan, China Xinshidai Holding Ltd will reportedly manage a local coal mine in Lahei. Meanwhile, China's state-owned mining company China Mining Corporation has been in on-again, off-again talks with Indonesia's state-owned PTBA to explore the large Ombilin coal mine in South Sumatra.

## Systemic Problems Threaten Long-Term Health

Another issue that continues to hurt the coal mining industry is the government's tax policy on coal. A government regulation in 2000 changed coal from a taxable to a non-taxable commodity. The regulation prohibits coal producers from charging value added tax (VAT) to end-users even though producers must pay VAT for imported capital goods and services. First generation coal contract companies have VAT reimbursement rights and have withheld over Rp 4 trillion ($470 million) since 2001 in government royalty payments to compensate for the regulation. Newer coal contracts do not have VAT reimbursement rights, effectively adding 8-10 percent to these companies' production costs. Indonesia's Supreme Court has the authority to annul the regulation. However, in April 2004, the Court merely issued an opinion that the regulation be annulled, an act which has no legal force.

The net effect of these policies, as well as continued delays in producing a new and transparent mining law, has resulted in a steady drop in investment. Coal investment (foreign and domestic) plunged from $778 million in 1997 to $135 million in 2001. According to the Energy Ministry, coal investment did rise between 2002 and 2003, from $61 million to $90 million, primarily to capitalize on higher coal prices. However, the general trend is one of decline, and the Indonesian Association of Coal Mining Companies reports that without significant policy improvements, greenfield investment will continue to drop, hurting the sector's long-term growth.

## Comment

The coal industry's bright production statistics are somewhat misleading. Recent growth is export-driven and vulnerable to outside factors. If China resumes coal exports, or should its economy slow down, international coal prices will drop. What the coal and greater mining sector needs is a comprehensive new mining law, clear regulations and investment-friendly policies that promotes the clean and rational development of this resource. Indonesians who worry about the environment, health and safety should be concerned about the departure of some Western companies from the mining sector. Absent legal and policy improvements to attract Western companies, Indonesia's future coal development could be left in the hands of quick-dealing parties uninterested in the long-term health of the country’s coal industry.