



INTERGOVERNMENTAL FORUM  
on Mining, Minerals, Metals and  
Sustainable Development

IGF Guidance For Governments:  
Leveraging Local Content Decisions  
for Sustainable Development

## CASE STUDY

# INDONESIA: DOWNSTREAM LINKAGES

## USING EXPORT RESTRICTION POLICIES TO MOVE DOWNSTREAM

### OVERVIEW

#### LEVEL OF OPERATION:

National

#### GOVERNMENT ROLE:

Regulator

#### LINK TO POLICY ADOPTED:

see [Mineral and Coal Mining law](#) (non-official English translation)

#### KEY COMMODITIES:

Petroleum, nickel, copper, tin<sup>1</sup>

#### TOTAL NATURAL RESOURCE RENTS (AS % OF GDP) (2015):

2.3 per cent<sup>2</sup>

#### NATIONAL EXTRACTIVES COMPANY:

Pertamina; Antam; PTB; Inalum

#### UNDP HUMAN DEVELOPMENT INDEX VALUE (2016):

0.689 (Global Rank 113)<sup>3</sup>

Indonesia is the largest exporter of nickel ore and tin in the world and ranks among the biggest for copper and gold production. To add value to these minerals, Indonesia imposed an export ban which has recently been relaxed due to private sector pushback and falling revenues. While the short-term costs of the ban are apparent, the long-term impacts remain unclear.

When establishing the export ban, the Government of Indonesia was willing to accept short-term revenue losses in exchange for long-term gains. These losses were exacerbated due to falling commodity prices. The resulting redundancies and economic downturn for regions dependent on bauxite, nickel and copper extraction turned out to be too drastic for the ban to be politically feasible. The policy U-turn within a few years has tarnished Indonesia's credibility with investors and miners. Given that the ban is still in place and the granting of export permits continues to depend on investments in smelting facilities, Indonesia will be

<sup>1</sup> Central Intelligence Agency (CIA). (2017). *The world factbook*. Washington, DC: CIA. Retrieved from <https://www.cia.gov/library/publications/the-world-factbook/fields/2111.html>

<sup>2</sup> World Bank Group. (2017). *Total natural resource rents (% of GDP)*. Washington, DC. Retrieved from <https://data.worldbank.org/indicator/NYGDPTOTLRTZS>

<sup>3</sup> United Nations Development Programme. (2016). *Human Development Reports: Indonesia*. Geneva, Switzerland. Retrieved from <http://hdr.undp.org/en/countries/profiles/IDN>



an interesting case to follow to better understand the short- and long-term costs/benefits of downstream beneficiation policies.

The Indonesia case study highlights the need to target downstream policies by sector and the shortcomings of blanket regulations. For nickel and copper, where Indonesia boasts world-class reserves, companies have largely remained and are more likely to build processing facilities. Indonesia's weaker position in bauxite has meant that a lot of operations have shut down and investors have left due to the export ban.<sup>4</sup>

## THE EXPORT BAN

The 2009 Mineral and Coal Mining law foresaw the need to add value and process domestically. Based on this law, in January 2014 a presidential

decree was passed that imposed an export ban on unprocessed minerals. More specifically, the ban included the following provisions based on two types of minerals that are defined as follows:<sup>5</sup>

- Type 1 minerals (bauxite, nickel, tin, chromium, gold and silver) are required to be processed and refined prior to export.
- Type 2 minerals (copper, iron, lead, manganese, ilmenite, titanium and zinc) could be exported as concentrates without further refining until January 2017 if the companies could demonstrate the construction of processing and smelting facilities individually or collectively. This differentiation was agreed after 66 companies, including the heavyweights Freeport McMoRan and Newmont, lobbied the government to provide them with more

**Figure 1. Progressive export duty tariffs for Type 2 minerals**

No. Mineral		Export duty tariff					
		2014		2015		2016	
		From 12 January to 30 June	From 1 July to 31 December	From 12 January to 30 June	From 1 July to 31 December	From 12 January to 30 June	From 1 July to 31 December
1	Copper concentrate (>=15% Cu)	25%	25%	35%	45%	50%	60%
2	Iron concentrate (>=62% Fe)	20%	20%	30%	40%	50%	60%
	Iron concentrate (>=51% Fe and Al <sub>2</sub> O <sub>3</sub> +SiO <sub>2</sub> >=10%)	20%	20%	30%	40%	50%	60%
3	Manganese concentrate (>=49% Mn)	20%	20%	30%	40%	50%	60%
4	Lead concentrate (>=57% Pb)	20%	20%	30%	40%	50%	60%
5	Zinc concentrate (>=52% Zn)	20%	20%	30%	40%	50%	60%
6	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, 2014.<sup>8</sup>

<sup>4</sup> Home, A. (2015, March). Bauxite and the limits of resource nationalism. *Reuters*. Retrieved from <http://www.reuters.com/article/us-indonesia-bauxite-ahome/bauxite-and-the-limits-of-resource-nationalism-andy-home-idUSKBNOMN2B620150327>

<sup>5</sup> Indonesia-Investments. (2014, April). *ICRA Indonesia: Analysis of economic impact of raw minerals export ban*. Retrieved from <https://www.indonesia-investments.com/finance/financial-columns/icra-indonesia-analysis-of-economic-impact-of-raw-minerals-export-ban/item1901?>



time to build up processing capacity.<sup>6</sup> Until January 2017 companies were subject to progressive export taxes that started at 20 per cent in 2014 depending on the mineral and gradually increased to 60 per cent by 2016 (see Figure 1).<sup>7</sup>

## IMPACT OF THE BAN

Until 2013 Indonesia hosted only one copper smelter where the biggest mining companies of the country, namely Freeport McMoRan and Newmont, had been smelting 40 per cent and 25 per cent of their copper production respectively.<sup>9</sup> In January

In 2014, it was reported that more than 100 mining companies had either reduced or shut down their operations. Consequently, thousands of mine workers were laid off ahead of the ban being implemented, triggering protests in Jakarta by the National Mine Workers Union. The Indonesian Mineral Entrepreneurs Association threatened to challenge the ban in the Supreme Court.<sup>11</sup> Accenture (2015) estimated that the ban led to a 20 per cent decline in Indonesia's mining revenues, with the bauxite and nickel sectors most impacted, and that the mining sector's contribution to GDP dropped from 11 per cent in 2010/2012 to about 7.2 per cent in 2015. The ban also negatively impacted other industries with strong forward linkages with the mining sector.<sup>12, 13</sup>

**Despite this investment wave, insufficient smelting capacity was built by the time the export ban was to take its full effect.**

While the Government of Indonesia anticipated these short-term losses (the Minister of Finance, for example, stated that this policy would reduce government revenues by USD 820 million in 2014 through lost royalties and taxes), it was convinced that the policy would

2017, most miners missed the government's deadline to build smelters and stockpiled lower-grade nickel ores, bauxite, copper concentrates and other metals.<sup>10</sup> As revenues fell due to the loss of the export business and the sharp decline in commodity prices, most miners struggled to keep operating, let alone invest in processing facilities.

result in a net positive impact in the medium to long term. This belief was based on the fact that already in 2013, 25 companies had invested USD 6 billion in processing facilities.<sup>14</sup> In 2016, Chinese investments into nickel smelting capacities amounted to USD 15 billion, with Chinese nickel pig iron producers appreciating the higher metal content of the Indonesian nickel compared to

<sup>6</sup> GRT Lawyers. (2014). *Indonesia's mineral ore export ban takes effect*. Retrieved from <https://www.grtlawyers.com/indonesias-mineral-ore-export-ban-takes-effect/>

<sup>7</sup> PwC Indonesia. (2014). *Export ban on unprocessed minerals effective 12 January 2014—three-year reprieve for some, but uncertainty remains* (Energy, Utilities and Mining, NewsFlash no. 50). Retrieved from <https://www.pwc.com/id/en/publications/assets/eumpublications/newsflash/2014/eumnewsflash-50.pdf>

<sup>8</sup> Ibid.

<sup>9</sup> Forbes. (2014, April). *Freeport McMoRan's proposed Indonesian smelter may not be ready by 2017*. Retrieved from <https://www.forbes.com/sites/greatspeculations/2014/04/07/freeport-memorans-proposed-indonesian-smelter-may-not-be-ready-by-2017/#5843a1e8342a>

<sup>10</sup> Rusmana, Y., & Listiyorini, E. (2017, February). *Indonesia's export ban flip-flop sows confusion*. QuickTake Q&A. BloombergMarkets. Retrieved from <https://www.bloomberg.com/news/articles/2017-02-14/indonesia-s-export-ban-flip-flop-sows-confusion-quicktake-q-a>

<sup>11</sup> GRT Lawyers (2014), Id. note 6.

<sup>12</sup> We can't determine the extent to which the Accenture study has neutralized the impact of decline in prices on mining revenues.

<sup>13</sup> Pillay, S. (2016, February). *The impact of Indonesia's raw mineral ore export ban on global mining*. Accenture.com, Retrieved from <https://www.accenture.com/us-en/blogs/blogs-impact-indonesia-raw-mineral-ore>; see also: Kartini, M. (2017, March). *Why investor confidence is low in Indonesia's mining industry*. *Indonesia Expat*. Retrieved from <http://indonesiaexpat.biz/business-property/investor-confidence-low-indonesias-mining-industry/>

<sup>14</sup> Bellefleur, D. (2014, February). *Indonesia: Mining industry, Indonesia export ban*. *Tractus* Issue ID. 2. Retrieved from <http://docplayer.net/53180573-Indonesia-export-ban.html>



neighbouring countries.<sup>15</sup> Also, Freeport McMoRan initiated partnerships with Indonesian companies to build smelters.<sup>16</sup>

Despite this investment wave, insufficient smelting capacity was built by the time the export ban was to take its full effect. Companies complained about the lack of access to reliable power to build smelters. As a result of mounting pressure, increasing unemployment and a fall in government revenues, the President of Indonesia announced the scaling back of the ban in March 2017 (just two months after it came into effect).

**The relaxation of the export ban is aimed at allowing miners to reconstitute their financial capacity to be able to invest in smelting facilities**

## THE REFORM OF THE BAN

The permit to export semi-processed metals (Type 2 minerals) has been extended for five years, subject to the following conditions:

- Progress needs to be shown toward building processing facilities.
- Only ore with nickel content less than 1.7 per cent and certain grades of bauxite can be exported without further processing.
- Miners should supply domestic smelters with enough low-grade ore to meet 30 per cent of their capacity.
- Companies such as Freeport McMoRan (which owns and operates the giant Grasberg gold/copper mine) are required to convert their “contract of work” into a “special mining business license.”<sup>17</sup> To secure

its export permit, Freeport McMoRan was required to yield a 51 per cent share in the Grasberg project to the government (compared to the current mandatory 30 per cent) as well as to pay taxes from which it had been exempt—a request that Freeport McMoRan recently agreed to.<sup>18</sup>

While most mining companies welcomed the delay of the ban, Indonesia’s smelting industry and those companies that had heavily invested in processing facilities during tough financial years protested. These investments were performed under the expectation that they would receive a guaranteed supply of ore. Now non-compliance was rewarded, and domestic smelters would likely only receive the lowest-grade ore, thereby reducing their margins. These investors are jointly reviewing legal steps against the Indonesian government for this change in regulation.<sup>19</sup>

Mining operators elsewhere fear a depression of prices by the release of more metals on the market. Following the announcement that Indonesia delayed the export ban, nickel and copper prices fell<sup>20</sup> significantly, affecting the shares of major producers. Vale’s shares, for example fell by 15.9 per cent in one day.<sup>21</sup>

<sup>15</sup> Jensen, F., & Burton, M. (2014, January). As smelters weigh cost, Indonesia’s ore export ban may backfire. *Reuters*. Retrieved from <http://www.reuters.com/article/indonesia-minerals-smelters/as-smelters-weigh-cost-indonesias-ore-export-ban-may-backfire-idUSL3NOKY20P20140127>

<sup>16</sup> Forbes (2014), Id. note 9.

<sup>17</sup> These terms are specific to Indonesia’s legal regime for mining. For more information see PwC. (2017). *Mining in Indonesia: Investment and taxation guide*. Retrieved from <https://www.pwc.com/id/en/energy-utilities-mining/assets/mining/mining-guide-2017-web.pdf>

<sup>18</sup> Asmarini, W., & Munthe, B.C. (2017, January). Indonesia eases export ban on nickel ore, bauxite. *Reuters*. Retrieved from <http://www.reuters.com/article/us-indonesia-mining-exports/indonesia-eases-export-ban-on-nickel-ore-bauxite-idUSKBN14W1TZ>. See also Jamasmie, C. (2017, August). Freeport to yield control of giant Grasberg copper mine to Indonesia. *Mining.com*. Retrieved from [http://www.mining.com/freeport-to-lead-control-of-giant-grasberg-copper-mine-to-indonesia/?utm\\_source=digest-en-mining-170829&utm\\_medium=email&utm\\_campaign=digest](http://www.mining.com/freeport-to-lead-control-of-giant-grasberg-copper-mine-to-indonesia/?utm_source=digest-en-mining-170829&utm_medium=email&utm_campaign=digest)

<sup>19</sup> Asmarini, W. & Jensen, F. (2017, January). Nickel smelters consider suing Indonesia after ore export ban U-turn. *Reuters*. Retrieved from <http://www.reuters.com/article/us-indonesia-mining/nickel-smelters-consider-suing-indonesia-after-ore-export-ban-u-turn-idUSKBN14X12A>

<sup>20</sup> Grey, E. (2017, March). Arrested development: Why Indonesia lifted its mining export ban. *Mining Technology*. Retrieved from <http://www.mining-technology.com/features/featurearrested-development-why-indonesia-lifted-its-mining-export-ban-5760809/>

<sup>21</sup> Asmarini, & Jensen (2017), Id. note 19.



The relaxation of the export ban is aimed at allowing miners to reconstitute their financial capacity to be able to invest in smelting facilities<sup>22</sup> and to raise tax revenues from the mining sector. It is hoped that this delay will also reestablish the balance sheet of the state-owned nickel company Antam, whose profits plummeted after the ban was introduced (Antam lost its ability to export without the possibility to sell to smelters to compensate for the export losses).<sup>23</sup>

It remains to be seen if companies will build the required smelting capacity by the new deadline this time around. The lack of infrastructure access is still a significant constraint to the construction of processing facilities that has yet to be addressed. There has also been criticism that the processing policy is leading to increased corruption. It is alleged by some that political connections and payoffs are a key determining factor of receiving an export permit.<sup>24</sup>

## KEY LESSONS

- A blanket ban is a blunt instrument that does not take into account project economics. Changing market dynamics like the recent fall in commodity prices can derail downstream beneficiation policies and harm investor confidence.
- The geological quality is what determines the ability to force the sector to move downstream (bauxite investments have left Indonesia while the nickel and copper investments have remained).
- Short-term losses may turn into long-term benefits. However, the latter are hard to foresee and quantify.
- Downstream policy measures that are not clear, consistent and transparent may lead to corruption opportunities.

<sup>22</sup> Rusmana, & Listiyorini (2017, February), Id. note 10.

<sup>23</sup> Burton, E. (2017, Oct.–Dec.). The life and death of Indonesia's mineral export ban. *Inside Indonesia*. Retrieved from <http://www.insideindonesia.org/the-life-and-death-of-indonesia-s-mineral-export-ban>

<sup>24</sup> Interviews with Indonesian experts, November 2017.



### FOR MORE INFORMATION CONTACT

Secretariat@IGFMining.org  
1100-220 Laurier Avenue W.  
Ottawa, Ontario  
K1P 5Z9 Canada

**IGFMining.org**  
**@IGFMining**
**@IGFMining**

Written by Perrine Toledano and Nicolas Maennling

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