Indonesia-China Energy Trade: Analyzing Global and Domestic Political Economic Significance in Indonesia-China LNG Trade

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Abstract

Indonesia had been the largest LNG exporter for almost three decades since 1977 to 2005. During 1970s and 1980s, Indonesia's energy industry boosted its economic growth that valued 80% of the country's annual exports and 70% of its annual revenues. Meanwhile, Indonesia presents an exceptional case since it decreases its LNG export while it has been developing its largest LNG plant in Tangguh due to prioritizing domestic energy demand. But, since Indonesia eagerly links its economy to China, it uses LNG export as a medium to strengthen Indonesia-China strategic partnership. Tangguh LNG export to China, although it is not Indonesia's largest LNG export contract, reflects a unique case of a developing country's international energy trade. Because it presents evolution of Indonesia's LNG export policy through dynamics of regional and global economic turbulences. This paper analyses the LNG export in the context of Asian economic crisis and its recovery, the peak of crude oil price in 2008 and followed by global financial crisis as the context as well as Indonesia's domestic political dynamics.

Keywords: international energy trade, Indonesia-China energy cooperation, LNG export policy

Introduction

Indonesia was an early producer of oil started in the 1870s. Up to the Second World War, Indonesia produced 148,000 barrels of oil per day (Arndt 1983; Hunter 1966). Indonesian natural gas industry came to life when it found a large natural gas field at Arun in Aceh Province in 1971, and then discovered gas reserves at Badak, near Bontang in East Kalimantan Province in 1972, totaling about 17.5 trillion cubic feet (tcf) of reserves (Wijarso, 1985). Badak exported its first cargo in 1977 while Arun followed the suit the next year. Badak and Arun's export had made East Asia the world's largest regional Liquefied Natural Gas (LNG) market (Nugroho, 2010).

The energy industry boosted Indonesia's economic growth during the 1970s and 1980s by accounting around 80% of the country's annual exports and 70% of the central government's annual revenues (Rosser, 2007:39). LNG is also Indonesia's most significant energy export and has been its largest foreign exchange earner (Stott,

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2008). Indonesia had been the largest LNG exporter for nearly three decades since 1977 to 2005, and its peak export was in 1998 for around 36.1 billion cubic meters (Nugroho, 2010). Indonesia has estimated reserves of around 9 billion barrels of proven and potential crude oil and 182 tcf of gas, according to energy ministry data (Reuters, 22 November 2007).

Profile of Tangguh LNG Project

Tangguh LNG plant project is Indonesia's third LNG centre after Badak LNG plant and Arun LNG plant. Tangguh plant is located in Berau Bay and fed by gas field in Manokwari Regency. Tangguh gas project is developed by a consortium of Beyond Petroleum Plc., (37.16%), MI Berau (16.3%), CNOOC (13.9%), Nippon Oil (12.23%), KG Berau/KG Wiriagar (10%), LNG Japan Corporation (7.35%) and Talisman (3.06%) (the Jakarta Post [JP], 31 December 2009). Tangguh LNG plant is planned to have a production capacity of 7.6 million metric tons (mmt) a year from two production trains (Hudiono, 2005) The LNG project fed natural gas from three production-sharing blocks –the Berau, the Muturi, and the Wiriagar blocks in Manokwari regency, which totally contained 14.4 tcf proven reserves of natural gas (JP, 9 August 2002). These three blocks are controlled through Production Sharing Contract (PSC) by BP Indonesia Plc. which has 37.5% of the reserves, along with by Mitsubishi (16%), Nippon Oil Exploration (12%), British Gas (11%), Kanematsu Corp. (10%), LNG Japan (1%) and China National Offshore Oil Corporation (CNOOC) which has 12.5% stake in the gas fields (JP, 30 September 2002).

Until 2009, The Tangguh LNG plant operator has signed multi-year contracts to supply LNG to several buyers, including to CNOOC, which is serving the Fujian Province's LNG Terminal in China for the amount of 2.6 million ton per annum (mtpa) for 25 years contract. Another one is with Korea's steel company, POSCO and Korea's Electric company, K-Power for a total of 1.15 mtpa for 20 years of tenure (Alfian, 2009). The LNG export contract to Fujian was the first contract made with Tangguh operator. It was expected to generate a total of USD8.5 billion revenue for 25 years contract period while its two trains total production capacity, will generate USD 21 billion in revenue over the same period. Initially, BP and its partners had planned to install four trains at the Tangguh plant, which will generate USD 45 billion in revenue (JP, 30 September 2002). The revenue will be distributed to the Indonesian central government, the Papua province and BP with its consortium partners. Under a PSC, BP and its partners would keep 30% of all revenue and give the remaining 70% to the government. Then according to the Intergovernmental Fiscal Balance Law No. 25/1999, the central government has to hand over 30% of the revenue to the Papua province (JP, 27 December 2002).

Statement of the Problem

Referring to Krasner (1976), there are four major state interests in the international trade: (1) political power; (2) aggregate national income; (3) economic growth; (4) and social stability. Focusing in international energy trade, it related to 'energy security' which has been debated particularly concerning the transnational oil markets. Moreover growing demand of gas in the global market will force consumers to put big concern of a vital gas supply. Emerging cooperation among gas producers and major energy consumer

countries will shape a new geopolitical considerations that strongly influence the highest levels of economic and security policy.

Energy importer country like China that commit to fulfil its large quantity of gas, put its energy security systems partly in the hands of the exporters, which will give both of the two parties a stake in each countries' domestic political stability. Thus, the 'geopolitics of gas' is not simply a struggle for global position, but also "the immensely political actions of governments, investors, and other key actors who decide which gas trade projects will be built, how the gains will be allocated, and how the risks of dependence on international gas trading will be managed" (Barnes et al., 2006: 4-5).

The focus of this study is to investigate Indonesia's LNG export from its Tangguh plant to Fujian Province in China. The export contract was signed in August 2002 to supply 2.5 mtpa of LNG for 25 years in tenure. Under the contract, the crude oil price –as the LNG checking price—was packed in maximum price of USD25/barrel, but the oil price had risen since early 2005 and it reached above USD100/barrel during 2007-2008. It means, the original contract only valued USD2.67 per million British thermal unit (mBtu), although in fact in 2008 Indonesia could even sell its LNG for USD20/mBtu to South Korean companies.

The major emphasis of this study will be on the Indonesia's interests in exporting its LNG to China. This study will particularly investigates Indonesia's interests that drove its LNG export from Tangguh plant to China, and the context that shaped the process of LNG trading tender/negotiation. Some research questions are addressed here. What interests drove Indonesia to export its LNG? Is there a certain political interest behind the deal? How did the domestic context shape Indonesia's attitude and its bargaining position during the negotiation of Fujian LNG contract? How did the global energy market shape Indonesia's assumption in accepting LNG pricing formula?

Since this research aims to reveal the dynamics of the international energy trade in depth and in detail, not shallowly and broadly, the naturalistic approach seems to be more suitable for this research. In addition, the existing data tend to be qualitative in nature as they are derived primarily from news in the mass media and interview with the resource person. This research largely uses a qualitative approach because it focuses on the detailed critical aspects using case study on a particular international energy trade. The data are collected using qualitative method, to be discursive and concerned with a comprehensive account of some event or unit. Although it has a small number of cases, qualitative researchers generally discover abundant information from the research. Sometimes this research is linked with area or case studies that focus on a particular event, decision, institution, location, issue, or piece of legislation (King, Keohane and Verba, 1995:4).

This research is more likely to incorporate an inductive approach and let the data speaks for themselves. This study is multi-method in focus, involving an interpretive approach to its subject matter. Therefore, by deploying a wide range of interconnected methods this approach not only helps in developing a more holistic view, but also facilitates explanation and prediction (Denzin and Lincoln, 1998). The main tool for data collection in this research is the analysis of secondary data, supported by a qualitative interviewing as well as internal documentation (documents of the contracts, etc.). Data analysis is conducted towards the news from several highly credible English newspapers and magazines as well as online websites, such as The Jakarta Post (most read English-language newspaper in Indonesia), Antara News

(Indonesia's biggest news services in terms of subscriptions), Tempo magazine English Edition (most popular magazine in Indonesia), Bloomberg, Reuters, and People Daily English Edition (Chinese government's media). An exploratory interview is also conducted with an energy expert and senior policy maker in energy sector in Indonesia. The interviews explore the context surrounding Indonesia's LNG export to China, interests that shaped Indonesia's policy to export its LNG, and suggestions of Indonesia's policy response to gain its national interests through energy cooperation with China.

Indonesian Government and LNG Marketing to China

Soon after taking over from the authoritarian Suharto's regime, President Habibie's administration (May 1998-October 1999) prioritized Tangguh LNG project over other LNG projects across the country, including the expansion of Badak LNG plant, development of Donggi-Senoro LNG project and East Natuna LNG project (JP, 14 June 1999).

President Abdurrahman Wahid continued implementing the policy and was involved personally in marketing the Tangguh project. He was eager to offer the LNG particularly to key player states in the Asian LNG market (JP, 13 June 2000). Wahid put China's LNG market on top of his list among others due to the country's fast growing demand of energy. China is the second largest energy importer after the US. Wahid visited China and sent his Minister of Energy Yudhoyono to find buyers for the project in China. From the beginning, efforts to sell Tangguh LNG to China were conducted with a government-to-government approach involving a state-owned energy company, Pertamina (JP, 30 May 2000).

President Megawati Soekarnoputri, who took office in July 2001 used any available means to sell Tangguh LNG to China through a tender for Guangdong Province LNG project. As the competition for Guangdong LNG contract between Indonesia and Australia heated up, leaders of both countries took turn to visit China to win over the preference of the Chinese government.

President Megawati visited China and lobbied the Chinese leaders to secure the Guangdong LNG contract. In March 2002 Megawati made a state visit to China accompanied by her husband, Taufik Kiemas, a large number of her ministers and over 100 Indonesian businessmen. Australian Prime Minister John Howard also lobbied the Chinese leaders to win the LNG project during his visit to China (JP, 9 August 2002).

President Megawati and her Chinese counterpart, President Jiang Zemin, performed a dance together for six minutes during a state dinner. The event was widely seen as dance diplomacy by Megawati to sell Tangguh LNG to China (JP, 25 March 2002). She also hosted another summit with Chinese Prime Minister Zu Rongji in Jakarta. On top of that, she sent her husband Taufik Kiemas to lead a government delegation that comprised some Cabinet members to persuade Beijing to reward Indonesia with the Guangdong LNG contract (JP, 21 August 2002).

However, on 8 August 2002, on the same day with the 12th commemoration of the normalization of Sino-Indonesian diplomatic relations, China announced a decision eagerly awaited by Megawati. The USD13.5 billion contract to supply 3 mtpa of LNG for Guangdong terminal was awarded to a consortium of Australia's energy firms (JP, 9 and 21 August 2002).

The date was only coincidence. However, as a largest LNG exporter, this was Indonesia's first failure to win the contract. It was very disappointing because Indonesia was so desperate for foreign exchanges to cover its budget deficit (JP, 12 August 2002). But surprisingly, China also announced a 'consolation prize' for Indonesia without tender process. China offered Indonesia to become a sole bidder for another LNG project in Fujian province, a smaller contract that's expected to value USD10 billion to supply 2.5 mtpa of LNG to Fujian Province (JP, 9 August 2002). However, the signed contract only valued USD8.4 billion for 25 years of long term export (JP, 26 September 2002).

Context of Global LNG Market and the Tender

During Guangdong LNG tender in 2002, the global LNG market was declining. Energy supply was abundant and the energy commodity price was very low. The competition among exporters was very tight. This situation was explained by Indonesian Minister of Energy Yusgiantoro that the arrival of new players from Malaysia, Australia, Brunei Darussalam and Qatar in the late 1980s has changed the regional LNG market's structure from a 'seller's market' to 'buyer's market' (JP, 12August 2002).

The 'buyer's market' happened when the amount of supply in the energy market was higher than demand. The declining market was formed by the scaling down of industrial operation in most Asia's developing countries. It was marked by the ceasing of manufacturing machines that left a big amount of energy supply in the stock pile. Although, just before the crisis, most of LNG producers have increased their LNG production capacity to meet high demand of energy triggered by Asian economic growth.

The decline in demand caused an oversupply condition in the LNG energy market. The oversupply did not only scale down the number of LNG markets, but also forced the contract of LNG trading to be rescheduled due to the fact that most of the LNG contracts were intended for long term deals ranging from 20 to 25 years.

They faced a totally unprecedented condition. All of the importing countries had an oversupply situation and too many contracts. These unstable market situations have also brought about different calculations on the buyers' side. Although they were favored by the 'buyer's market' condition, they prefer to have short term LNG contracts as they took a wait-and-see approach to long term contracts. In their opinion, short term contracts offered better flexibility in dealing with the period of uncertainties. Therefore, the energy market was flooded by 'short term' contracts or buyer's preference to buy small quantities (JP, 11 April 2001). That is because the buyers did not want to be tied with long-term contracts and therefore the buyers became more and more demanding and the competition became tighter (JP, 9 December 2000).

The condition continued until the second half of 2004, when energy market was still dubbed as 'buyer's market'. Demand for Indonesia's LNG from its traditional buyers, like Japan, South Korea and Taiwan, was still running in the lowest curve. In fact, in order to extend the current contracts to supply some 12 mtpa to Japan that will expire by 2010, Indonesia was considering a request from the Japanese to lower the price, as part of a strategy to maintain its customer loyalty (JP, 10 December 2003). This marketing strategy by decreasing the price was also applied to Korea Gas Corp. (Kogas) by discounting up to 40% should the firm agreed to extend its

contract for another 20 years (JP, 23 June 2004).

This 'buyer's market' condition dominated the global energy market from the peak of Asian economic crisis until the second half of 2004. This is the background of China's tender for the Guangdong LNG project, which drew bidders from six countries –Indonesia, Malaysia, Russia, Australia, Yemen and Qatar (JP, 9 August 2002). It is assumed that this energy market context had influenced the China LNG tender process.

Domestic Context and the Tender

It is very important to understand the political economic context in Indonesia during the Fujian LNG bidding process. Prior to the bidding, Indonesia was the last country in Asia to recover from the economic crisis started in 1997. Not only did it hit hard Indonesia's financial sector, but also triggered a broader, systemic political reform. The crisis created a momentum to bring down the authoritarian regime of President Soeharto and provided a period of transition which changed an authoritarian system into democracy. During the transition, political liberalization also opened a tight power competition among elites. Provinces outside Java Island abundant with natural resources demanded full autonomy and even campaigned for independence.

One of the richest provinces but always marginalized, Papua, intended to break away from Indonesia. Responding to this demand, Indonesia should deliver a quick and concrete action to solve the unrest in Papua. The problem would bring the domino effect to other provinces, especially after East Timor was separated from Indonesia. The main concern of the insurgents in Papua was demand for justice and welfare from the central government, particularly for larger shares in the revenues from the exploitation of their natural resources (JP, 13 June 2000).

In this domestic context, development of the Tangguh LNG project was expected to be a strategic step in order to solve the problem. It was expected, by exporting Tangguh LNG, Indonesia would receive sufficient money to finance development in the province with 2.3 million populations. Furthermore, the development was expected to push the economic growth and bring a multiplier effect in the development of various basic infrastructures.

The LNG project itself was expected to provide at least 3,000 job opportunities during the construction and 1,000 would be permanently employed in the plant's operations. The central government had been guaranteeing a fairer share through the Special Autonomy Law of Papua. The law guarantees the province to get 30% of the revenue from the LNG project and 70% will be for the central government (JP, 30 September 2002).

Competition among the Energy Companies

Another issue that also rose during the Indonesia's bidding of Guangdong LNG project was the competition among the multinational companies. They were mostly the investors of Badak LNG plant in East Kalimantan –led by French firm Total Fina Elf and American firms Unocal Indonesia and Vico Indonesia— who asked Pertamina to sell LNG from Badak to China. The investors of Badak plant wanted to sell their LNG to China since their plant was already developed and had been serving international market for decades. They also proposed to build the ninth train in the Badak plant (JP, 25 July 2001).

They argued that exporting LNG from Badak would be cheaper than from Tangguh plant, because Badak LNG was an expansion project while Tangguh was a new one. Investors of Tangguh would need to spend full investment to build infrastructure and other supporting constructions, while Badak project would be more efficient because it would only need to spend money for expansion project.

The efficiency would help Indonesia's position to give more competitive price for the potential customers. Badak investor's reason on the competitive price was relevant with the buyer's market condition at that time. Indonesia's chance to win the Chinese LNG supply contract would be greater if it proposed to supply LNG from Badak plant (JP, 25 January 2001). Pertamina President Baihaki Hakim argued that Tangguh LNG could be less competitive, because construction of the plant had not begun yet, which raised the cost of selling the LNG (JP, 11 April 2001).

Meanwhile, the Indonesia's bidding of Guangdong was also followed by the competition behind the screen between Pertamina and BP. Pertamina was no longer the sole seller for Indonesia's LNG for international market and was replaced by BP, although during the Habibie administration, Pertamina was appointed to market Tangguh LNG to China (JP, 14 June 1999). The change of the market leader from a state owned company to a foreign company was allowed by the new Oil and Gas Law, Number 22/2001 that stipulates foreign contractors are allowed to market their production (The State Secretariat of the Republic of Indonesia, 2001).

The appointment of BP to market Tangguh LNG to China was followed by a controversy. BP failed to compete with the eventual winner, an Australian consortium. Analysts argued that appointing BP to spearhead Indonesia's marketing effort was a mistake. Pertamina should have done the job as it had marketing experience for decades. An analyst, Hutapea, said despite the extensive corruption within Pertamina over the past decades, Pertamina had succeed in putting Indonesia as the world's largest LNG exporter and maintained Indonesia's leadership in the Asian LNG market for decades. He said the government had made a mistake by allowing BP to lead the marketing, "The government made a blunder by distrusting Pertamina" (JP, 12 August 2002).

Hutapea said the problem was the security of supply. He further explained that since the Tangguh plant had not developed yet, China doubted the continuity of supply from the Tangguh project. They might fear other LNG plants could not be responsible to 'help' Tangguh in case of troubles given the fact that China would deal with BP, rather than Pertamina. "Had Pertamina led the marketing effort, China would not have been overly worried about the security of supplies because Pertamina also manages the Arun and Badak plants" Hutapea argued. China prefers to be served by Pertamina as it has been reliable exporter of LNG since 1970s.

Meanwhile, BP perceived as the relatively new player in Asian LNG market, and more importantly it did not has any authority to two other LNG plants that already operated for years (JP, 12 August 2002). Pertamina's position was assumed stronger in the LNG market because it has full authority in two other LNG plants. These authorities were very important to be able to guarantee continuity of the LNG supply to the importer. As an example, when LNG production at Arun plant in Aceh was disrupted, Pertamina could easily secure the continuity of supply by deliver its reserve capacity from Badak plant in Kalimantan. In fact, BP did not have such ability to guarantee security of LNG supply to the importer.

It was the first time a foreign contractor led an Indonesia's LNG marketing team. However, after assessing the failure to win Guangdong contract and considering China's special offer of Fujian LNG project, the government assigned a marketing team led by senior Pertamina official to follow up the offer. The team comprised three Pertamina officials and president of the Tangguh project, Gerald J. Preeboom from BP. Successfully the Fujian contract was signed in August 2002 by Pertamina, not BP (JP, 20 August 2002).

Following its 'success' to secure the Fujian contract, Pertamina intensified a campaign to regain its previous status as the sole seller of Indonesia's LNG. An Indonesian analyst argued that Pertamina's status as marketing leader would improve Indonesia performance to compete in the market because Pertamina had full control of the other two LNG plant. It in turn would assure the security of supply, something that BP did not have. However, other contractors were not enthusiastic about the campaign as they argued that the single seller scheme would be unfair for LNG players in Indonesia, with Pertamina no longer the regulator but rather a market player (JP, 19 September 2002).

In the wake of competition among contractor companies, the Oil and Gas Implementing Body (BP Migas) has appointed Pertamina as the sole marketing agent for Indonesia's LNG to Japan, Indonesia's largest LNG importer. The appointment was for scheduling BP Migas' proposal on the extension of Japan LNG import contract that would due in 2010 (JP, 10 May 2004).

Pertamina was also asked to market the LNG to South Korea and Taiwan. In late May 2004, Pertamina regained its status to lead Indonesia's LNG marketing team. The head of BP Migas announced that they had finished terms and conditions for the appointment of Pertamina as sales agent with other LNG producers such as Total, Unocal, Vico and BP Indonesia for Tangguh." (JP, 28 May 2004).

Learning from the competition among contractor firms, the government has considered to set up an 'Indonesia Inc.', which would position the authority to market Indonesia's LNG. The body, whose goal would be to help Indonesia retain its position as a top LNG producer, would consist of BP Migas, Pertamina, the Indonesian Gas Association and contractors (19 September 2002).

However, the Tangguh LNG export contract for Fujian did have a problem that would explode in the following days. The problem was about pricing formula that caused huge lost to Indonesia, because the contract involved a crude oil check price at USD25/barrel as the ceiling price for the Tangguh LNG for Fujian. Some economic and political issues emerged around the controversial Fujian contract.

Problems over the Fujian LNG contract

Market condition that has been called 'buyer's market' has made the competition very tight. It is very tough when each of the LNG exporting countries had to compete by employing all possible means available to win LNG supplying contracts. However, various measures deployed to win the export contracts must put a national interest on the top priority above all calculation and interests.

Various ways to attract potential buyers, including giving a big discount for LNG price, should be calculated in order to gain long term interest. Pricing of energy commodity in the international market always fluctuates. Sometimes the price drops because of economic, politic or security issues, but at other times the price

can be very expensive because of these contextual variables. As the nature of fossil-based energy is very limited and could not be renewable, the general trend of fossil energy price should be higher in the future. "The negotiator team had acted against the law of nature by assuming the fixing price" said Kurtubi, an energy expert in Jakarta (Iswara, 2008).

Based on this reason, the Fujian LNG contract raised some question on the 'abnormality' of the contract. But since the contract was won during the frustrated situation for Indonesia, the direct appointment as the sole bidder without tender was perceived as the 'consolation prize'. However the 'consolation prize' had raised a public suspicion on the unfair transaction since its early stage.

The suspicion was raised as the Indonesian government was not transparent in announcing the Tangguh LNG export price to Fujian Province although some experts and politicians had questioned the issue. The Indonesian government was seen to keep something behind public eye while in August 2002 Minister Yusgiantoro was still in preparation to send a task force to clarify the contract with the Chinese government. Even until second half of September 2002, the price of LNG export to Fujian was still in question. Having failed to win Guangdong contract, also with unclear details of the Fujian contract, the Indonesian government nevertheless speculatively declared that the result of the bidding was good enough for Indonesia (JP, 7 September 2002).

Responding to that progress, many experts and politicians criticized the marketing team's ability and started questioning whether the largest exporting country was still competitive in the future. "Indonesia's LNG industry is now facing a doubtful future," Ramses Hutapea, an energy analyst said (Simbolon et al., 2002).

Critics also questioned the involvement of the president's husband, Taufik Kiemas who led Indonesian delegation to 'lobby' Chinese policy makers. The rumors in Jakarta speculated that Kiemas himself had been possibly taking profits from the 'marketing activities' (JP, 21 August 2002).

Indonesian government used the 'consolation prize' to forget the frustration for its failure to win the Guangdong LNG tender. The Indonesian government used the Fujian contract to answer various critics following the failure to win the Guangdong contract and later other failure to win respectively Korea and Taiwan contracts. Therefore, the suspicion on the 'unusual' terms and conditions in the Fujian contract could be ignored. Moreover, the price of energy commodity was very cheap, so the formula of the contract could seem normal (Simbolon et al., 2002).

The suspicion was justified three years later when the market shifted to 'seller's market' and energy commodity price hiked in 2005. Again, in answering the suspicion on the Fujian contract detail, the then Minister Yusgiantoro said that it was a 'consolation prize' after Indonesia failed to win Guangdong LNG contract and extend export contract to its traditional LNG importer such as Japan, Korea and Taiwan (Simbolon, et al., 2002).

Minister Yusgiantoro explained that the offer for Indonesia to act as a sole bidder for Fujian LNG project was already tied with the specific terms and conditions. One of the terms was to put the maximum crude oil check price of USD25/barrel as the ceiling price, which meant that the highest LNG price to be exported to Fujian would be only USD2.67/mBtu for a period of 25 years. It meant that the negotiators assumed the crude oil price would always be below USD25 for period of 25 years.

The ceiling price has limited the fluctuation of the LNG price. If the current crude oil price is around USD75 to

USD80/barrel, then the LNG price should be around USD12 to USD15/mBtu. Let us compare this with the price in the Fujian contract. The contract that involves 2.6 mtpa of Tangguh LNG for Fujian puts Indonesia in a huge lost (Kurtubi, 2007).

The use of price ceiling has been perceived as a big problem because it will cause a massive lost for Indonesia, almost USD8 billion in a period of 25 years of export to Fujian. This reality is very hard to swallow. Since Indonesia's current status as a net oil importing country, it has to import crude oil at expensive price, but at the same time sells LNG at very low price. Importing crude oil is quite costly as Indonesia always subsidizes oil price for its domestic market.

The reactivation was followed by the increase of energy demand in the global market. However, the oil price hike in the global market did not affect significantly the Indonesia's exported LNG price for Fujian, China. It caused Indonesia to suffer a huge lost in its foreign currency since its LNG has been exported to Fujian far below the market price.

The lost was caused by the imposed pricing formula that restricted LNG price with maximum equivalent to oil price of USD25/barrel. Indonesia's LNG price for Fujian could not climb in line with the oil price in the market and ultimately Indonesia as an LNG exporter could not benefit from the momentum. This was frustrating since the oil price could not push Indonesia to raise LNG price for Fujian.

The situation raised reaction among Indonesian political elites. Various discourses on the issue surfaced such as 'resource nationalism', demand to cancel the Fujian LNG contract at all cost, and idea to do more rational measure by renegotiating the contract. A visionary idea that gained strong support was the demand to review the energy export policy and to change it into one that prioritizes the natural resources to meet domestic energy demand.

The 'rising oil price' and the irony of pricing formulation in LNG export contract to Fujian have raised a discourse on 'resource nationalism'. However it did not force the Indonesian government to nationalize foreign energy companies as in Venezuela and Bolivia. This is despite the fact that the idea is based on the vision to use the natural resources for the full benefit of the people (Soesastro, 2007).

In the practical terms, the idea is about to prioritize the Indonesia's national energy and mineral companies, to explore, to product, to refine and to distribute or to market the resources as long as the companies can do them by themselves. Then the national companies are allowed to invite other international companies to manage the resources that the national companies are unable to manage. But, the basic rhetoric is about to free Indonesia from the exploitation of the so called 'new colonialism'.

Another disappointment from the Fujian contract was the demand to cancel the contract and find other potential LNG importers who could give more benefit for Indonesia. This is because some analysts have argued that the contract could be cancelled and this scenario was actually accommodated by the agreement. As the maximum penalty for such eventuality is USD300 million, cancellation makes financial sense, rather than suffering lost for around USD75 billion in 25 years (Iswara et al., 2008).

Following the situation, Indonesian government preferred to renegotiate the Fujian contract and to conduct more active effort to pull China's investments and loans to Indonesia. The investments and loans become highly important since Indonesia is in deep concern to build its energy and infrastructure projects. Another measure

that was conducted at the same time is to review the policy of raw material export so that commodities will be for domestic consumption or the process of the material will be inside the country.

The demand for renegotiation was very rational since the LNG pricing formulation normally reflected the progressive price of crude oil in the global energy market (Stott, 2009). There must be no certain limitation to the oil price that serves as the standard or checking price to formulate Tangguh LNG price. The maximum fixed price of the oil price was unusual in the global LNG trading and this price fixing also never happened before.

Ironically, considering the hike of crude oil price in the global market during July 2008, when it reached its top position in USD147/barrel, the price of LNG in the global market should be mirrored around USD20/mBtu. At that time, an energy analyst, Kurtubi, estimated that such pricing difference would cost Indonesia USD3 billion annually (Iswara et al., 2008). Meanwhile, when the crude oil price in the market is moving around USD100/barrel, therefore the normal price of LNG in the global market should be four times higher than the Indonesia's LNG price for Fujian.

While the renegotiations could cause a rift in China-Indonesia relations, it is undeniable that Indonesia has what China needs, large deposits of natural resources (Stott, 2009). Meanwhile, President Yudhoyono changed Indonesia's strategy by pushing for enhanced energy cooperation with China, especially in the construction of power plants and infrastructure under the concessionary loan scheme. Indeed, energy cooperation is an important part of the Sino-Indonesia relations, similar to Beijing's growing ties to other resource-rich developing countries in Africa.

Having suffered a huge lost from the Fujian contract; Indonesia now has learnt to control its tendency to easily export its natural resources. On the other hand, to meet domestic energy demand, the government should change its policy by prioritizing the gas for domestic demand than exporting it. Since Indonesia is a net oil importer, it has been importing oil that is more expensive than the gas price.

Moreover, the government still subsidizes oil retail price that costs more than 10% of Indonesia's national budget. A prominent energy expert and member of National Energy Council, the late Widjajono Partowidagdo, in an interview with the author, said "It is very stupid to export the cheaper one –LNG—and importing the expensive one –oil, that is simple" (Partowidagdo, 2010).

That logical way of thinking influenced some of the top policy makers, and the victory of the duet of Susilo Bambang Yudhoyono and Jusuf Kalla, in the first direct Indonesian presidential election in September 2004, has "altered the political landscape with regard to LNG export" (Stott, 2008). That is right what Stott has mentioned, since Indonesia restores its post-crisis economy and increases its competitiveness in the global market; Indonesia must seriously increase the added value by processing its natural resources inside the country.

That was one of the priority programs of the Yudhoyono-Kalla administration, who prefer to push development of resources-based industry and to minimize export of raw materials commodity. Actually, by tracing Indonesia's energy policy through history, the policy to prioritize domestic energy demand had risen since 1977 when Soeharto administration (1967-1998) handled Indonesia's early industrialization in 1970s that needed a big amount of energy supply.

In the mining sector, new legislation was passed in 2009 which required mining firms to process all mining products into

metal locally instead of just exporting the raw materials abroad. These policies affect China because, besides its energy needs, China's economic growth needs Indonesia's raw materials. To meet its industry demand, China will continue its dependence on Indonesia's material supply from large bauxite field in Kalimantan. However, the Indonesian parliament discussed banning future bauxite exports in favour of refining its own bauxite to alumina domestically (Stott, 2008).

After being widely questioned and renegotiated in 2006, the Fujian contract issue was raised again. In domestic context, politicians was also used this controversial issue as a 'political weapon' to attack their political opponents. Competition among the politicians intensified when the election was around the corner. In order to get popular support they launched a political attack against their rivals. This section will particularly discuss the domestic political context and its dynamics regarding the controversial LNG export contract to Fujian that was signed when Megawati acted as President of the Republic of Indonesia from July 2001 to October 2004.

The political structure in 2008 already changed, compared to the time when the Fujian contract was signed. At that time, Megawati, who failed to stay in power after the 2004 election, brought her party as an opposition power to the government. On the other side, both Yudhoyono and Kalla, who were the cabinet members of Megawati administration, was in power after defeating Megawati in 2004 presidential election.

In 2008, one year before the legislative election in April and presidential election in July 2009, Indonesia's political tension was high. The opposition leader, Megawati, and her party (PDI-P, Indonesian Democratic Party of Struggle) aggressively pushed a parliamentary enquiry to investigate the government decision to cut subsidy for fuel price in the domestic market. To balance the power exercise, the Golkar Party that had a majority of seats in the parliament and was led by the then Vice President Jusuf Kalla, was very eager to criticise Megawati's decision to export Tangguh LNG to Fujian at a very low price. The aim of the Golkar's manoeuvre was to raise public awareness that Megawati had bequeathed a big problem by deciding an export contract.

In countering this political attack, Pramono Anung, Secretary General of PDIP warned Yudhoyono and Kalla that since both of them were members of the Megawati administration from 2001 to 2004, Yudhoyono and Kalla could also be responsible for formulating the policy. Politicians in the parliament also confirmed that the Fujian LNG contract could be politicised and "become an effective bargaining position" said Alvin Lie, a politician outside the two confronting groups who posted in Commission on Energy (Iswara, 2008).

Beside the political issue, Tangguh LNG problem also had a big magnitude and was discussed by various segments of people. This issue could also be an entry point for the businessmen to require sufficient energy supply to operate their industry machines. Meanwhile, it also touched the public sensitivity since they suffer from periodical black-out as the state-owned power company did not receive sufficient energy to produce electricity. Moreover, the government was unable to build infrastructure and other public facilities because a large amount of its budget must be allocated to subsidize fuel price in domestic market. In the 2010-2011 budget, the subsidy is allocated for around 150 trillion of Indonesian Rupiah (USD18 billion), or more than 10% of the total national budget (Partowidagdo, 2010).

In August 2008, Kalla claimed that the Fujian's present formula would totally suffer Indonesia of USD75 billion. He then asked the House of Representatives (DPR) to review the Fujian contract and the Supreme Audit Agency (BPK) would supposedly investigate the country's lost on it. Kalla saw the formula was the worst in the history of Indonesia's energy industry (Iswara et al., 2008). Kalla urged, "So, the House has to investigate the Tangguh LNG contract because this contract is the most dangerous. This contract is the worst so far." (JP, 24 August 2008).

Conclusion

Revisiting the Research Question

As a form of international trade, Indonesia's LNG export to China has a set of interests, as mentioned by Krasner (1976), namely, economic growth, aggregate national income, social stability, and political power. These interests have been reached through a set of measures conducted by the government as discussed above. Discussion and analysis are provided in order to show Indonesia's interests and how the government manages them through answering the research questions.

What interests drove Indonesia to export its LNG? Is there a certain political interest behind the deal? This paper explains that the development of the Tangguh LNG project was expected to be a strategic step in order to solve the social and political stability in Papua Province. It was also expected, by exporting Tangguh LNG, that Indonesia would receive sufficient money to finance development in the province with 2.3 million populations. Furthermore, the development was expected to push the economic growth and bring a multiplier effect in the development of various basic infrastructures. The LNG project itself was expected to provide at least 3,000 job opportunities during the construction and 1,000 would be permanently employed in the plant's operations.

How did the global energy market shape Indonesia's assumption in accepting LNG pricing formula? How did the domestic context shape Indonesia's attitude and its bargaining position during the LNG contract was negotiated? This paper also discusses Indonesian Minister of Energy Yusgiantoro's explanation about the changing LNG market's structure from a 'seller's market' to 'buyer's market' that dominated the global energy market since the peak of Asian economic crisis until the second half of 2004. As the background of China's tender for the Guangdong LNG project, it is assumed that the global energy market had influenced the China LNG tender process.

As mentioned above, Indonesia's interests had shaped its LNG export to China. This paper also discusses that the Fujian LNG contract was received during the frustrated situation for Indonesia following the failure in the Guangdong, Korea, Taiwan, and Japan. Hence, the contract was perceived as the 'consolation prize'. This part later discusses suspicion on the involvement of Indonesian president's husband, Taufik Kiemas who led Indonesian delegation to 'lobby' Chinese policy makers and possibly taking profits from the 'marketing activities'.

Lesson learned

There are several things that can be learned from Indonesia's LNG export to China. First, in pursuing state's interests through international trade, the government should also consider the global market condition in the future. This is because the global market is always dynamics,

particularly energy commodity prices that always fluctuates and is influenced by the economic, politic and security situations, besides speculation in the future market.

The negotiators in international trade, particularly in exporting LNG, should be careful in formulating the export price, since LNG prices are not internationally standardized. There are differences in every single trader and they vary by region of destinations, although the LNG price mostly refers to the crude oil price in the spot market (Girianna, 2009). Learning from the Fujian pricing formula that restricted Indonesia's LNG price to a very cheap price, it would be better to use a progressive pricing formula instead of using ceiling price or putting an upper limit for the LNG price.

Second, before releasing energy export policy, the government should consider its own country's domestic demand first. The government should give priority to generating its own economic development by allocating the energy for domestic need. It is an irony that while Indonesia was exporting most of its LNG, its local industry was suffering because of its lack of energy supply. Moreover, the government has to import oil and subsidize the oil retail price that costs more than 10% of Indonesia's national budget. Concerning this situation, a member of Indonesia's National Energy Council said "It is very stupid to export the cheaper one –LNG—and importing the expensive one –oil" (Partowidagdo, 2010).

The policy to prioritize domestic energy demand will strengthen the country's industrial capability. In turn, this condition will create more job opportunities, give added value to its manufactured products, and offer further value from its export in a better form rather than in raw materials. Third, in managing state's interests, the government should be consistent toward its bigger mission, not being trapped in such temporary circumstances. The compass for government is neither a particular political interest nor a short-term domestic political competition. Instead it should be to pursue a state's political power, aggregate national income, economic growth, and social stability. It is also required to maintain stronger cooperation with its partners in international trade, in this case Indonesia and China. Moreover, the partner is the emerging economic and military power that will strategically influence the regional stability where Indonesia is also situated.

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