

Cancelation of Saudi Aramco Investment in Cooperation to Develop the Oil Refinery in Cilacap

Fitrah Aisyah Adam
{fitrahaisyah80@gmail.com}

Universitas Indonesia, Indonesia

Abstract. Indonesia through PT Pertamina and Saudi Aramco in 2016 officially started the negotiation process to form a joint venture for developing the Cilacap Refinery in Central Java which is Pertamina's Refinery Development Master Plan (RDMP). However, results from the negotiation efforts are not as expected investment from Aramco was canceled. Author's initial identification apart from economic factors, there are non- economic factors that affect the process. Therefore, this paper aims to analyze the cancellation of Saudi Aramco's investment in a joint venture with Pertamina for developing the oil refinery in Cilacap using the Political Bargaining Models. Moreover, this analysis hoped to reveal non-economic factors that affected the cancellation of the cooperation.

Keywords: Joint Venture, PT Pertamina, Saudi Aramco, Political Bargaining Models

1 Introduction

Energy is one key to the economic development of a country. According to data from the International Energy Agency (IEA), global energy demand has exploded in recent decades. Estimated that from 2005 to 2030, global energy demand will increase by 55% (IEA, 2007). Unfortunately, the increasing demand has not been accompanied by an adequate supply of energy. Until now, oil, natural gas, and coal are still the primary sources of fossil energy in almost as many countries. Therefore, several countries have their policies in meeting their energy needs by cooperating, diplomacy, or relying on international oil companies or organizations for their energy needs.

Like other countries, Indonesia also still uses fossil energy sources as its main energy source. The development of the Indonesian oil and gas industry, which experienced peak oil production in 1977 and 1995, reached a total production of 1.68 million bpd and 1.62 million bpd, respectively [1]. This also makes Indonesia one of the oil-producing countries in OPEC (Organization of the Petroleum Exporting Countries). However, entering the year 2000 there was a decrease in average production of around 10-12% while the population of Indonesia was increasing and also increasing the oil demand. Referring to data from the Ministry of Energy and Mineral Resources, in 2014 Indonesia's oil production was only around 789 barrels per day (bpd). From 2010-2014, the average production decreased by around 44%. This could not meet Indonesia's oil demand in the same year as shown in the graph below.

The decrease in Indonesia's oil production was because of the condition of oil refineries that were old and damaged a lot. Thus, the Indonesian government, through Pertamina, established the Refining Development Master Plan Program (RDMP). This program aims to

revitalize old oil refineries in Indonesia by estimating that Indonesia can reach 1.1 million bpd of oil production again [2].

The revitalization of oil refiners is quite expensive. Therefore, the Indonesian government needs foreign investment for implementing the RDMP project. After Indonesia improved regulations for oil and gas investment, several foreign National Oil Companies (NOCs) considered to Indonesia to cooperate through Pertamina, one of which was the NOC of Saudi Arabia (Saudi Aramco). From 2016 until the end of June 2019, they formed Joint Venture Development Agreement (JVDA) as the first step to establish a joint venture company. In 2016, the two agreed to manage the oil refinery in Cilacap with a 55% share of assets (Pertamina) and 45% (Saudi Aramco). Other agreements reached on JVDA included 70% oil supply from Aramco, management control, and oil lifting carried out (Pertamina, 2016).

In the JVDA process, they encountered many problems. One of them is the unfinished asset valuation with Saudi Aramco. Based on its value, Pertamina holds the 2018 enterprise value from the Public Appraisal Service Office (KJPP) of 5.66 billion USD or equivalent to Rp. 79.95 trillion. Meanwhile, Saudi Aramco considers the enterprise value to be 2.8 billion USD [3].

To resolve these differences mentioned above, it negotiated the Indonesian government with The Kingdom of Saudi Arabia as the highest policymaker in Saudi Aramco. At least the President of the Republic of Indonesia, Joko Widodo, has held two special meetings with The Kingdom of Saudi Arabia to negotiate regarding the Saudi Aramco investment. As for the negotiations; (1) In April 2016, President Joko Widodo conducted the first negotiations by visiting Saudi Arabia, accompanied by the Indonesian Minister of Foreign Affairs (Sekertaris Kabinet, 2019). However, the meeting has not agreed. (2) In June 2019 in Japan, the Government of Indonesia took advantage of the G20 meeting to negotiate Saudi Aramco investment. President Joko Widodo and his ministers with the Crown Prince of the Kingdom of Saudi Arabia, Prince Mohammad Bin Salman, and related ministers, held a special meeting to discuss the continuation of the development of the oil refinery in Cilacap. The meeting resulted in a win-win solution for Pertamina and Saudi Aramco. Both agreed to hire a third party to be a valuator who can calculate the validation of the value in question. Based on these conditions, the two agreed to extend the JVDA for three months, which should have ended in June 2019 to determine the end of the agreement between the two countries (ESDM, 2019). But in the end result, the four-year JVDA negotiation process yielded no results at all. The fact in April 2020, Saudi Aramco decided not to invest in the plan to build a joint venture company with Pertamina to revitalize the refinery in Cilacap [4]. This study attempts to understand why did Saudi Aramco cancel its investment?

2 Method

This study focuses on the interactions built on the negotiation process in the JVDA between Saudi Aramco and Pertamina. Involves interactions and relationships between two or more actors so that it requires an analysis that can cover the various interests of these actors. The concept of negotiating power or bargaining power is an option because it can describe what each actor expects interest from the interactions and relationships they form. The Political Bargaining Model by Eden, Lenyaw, and Shculer [5] is the concept the author chose in analyzing the cases discussed above.

The PBM components are; 1) Objectives and relative circumstances. The goals of the MNE and the host country are different and are cooperative. In this relationship, there is positive-sum bargaining, meaning that it must do the bargaining process in order to achieve a positive sum. 2) Resources; MNE transfers of resources that are not site-bound on a property basis are long-term contracts that can be enforced to monopolize scarce factors of production. Host country offers location-bound (property-based) resources. 3) Constraints; Both have in common, economic, political, and institutional constraints. The inseparability of governance constraints international institutions and home country governments can influence the outcome of negotiations. 4) Bargain; MNEs and the government negotiate specific public policies in the industrial sector. 5) Strategy; MNEs use economic and political strategies, lobbying for legitimacy to meet foreign obligations. 6) The relationship between MNE and host country can be strengthened through organizational legitimacy, political accommodation, complementary resources, and personal relationships between the actors. 7). Outcomes; Benchmark results are determined by which party is closest to achieving its goals. Outcomes depend on the parties' goals, resources, and relative constraints. The inseparability of governance, corporate competition, and foreign liability are key variables that affect bargaining outcomes [5].

3 Discussion

The interaction between the Indonesian government and Saudi Aramco is a manifestation of efforts to achieve goals. Each party cannot fulfill its goals without cooperation with external entities. Indonesian government, through PT. Pertamina's desired goal, is to fulfill its oil resources. To fulfill this, the Indonesian government established the RDMP, which requires funding or investment sources from Saudi Aramco. Meanwhile, Saudi Aramco (MNE) has a goal to achieve its vision by 2030.

Saudi Aramco as an MNE offers funding sources and share technology needed by Indonesia as the host country that owns the resources. In the JVDA process, there are many contracts that both parties must evaluate, in this case evaluating the different perceptions of asset valuation, between Saudi Aramco and the Indonesian government. Likewise, the failed negotiation process was largely influenced by the unequal perspective of asset value valuations between Saudi Aramco and the Indonesian government. Other institutions have also been involved in resolving the problem of different perceptions of asset valuation, but the results are still to no avail.

The Indonesian government itself does not create a positive investment environment for foreign companies. The existing political conditions in Indonesia influence these matters. Problems that exist within the Pertamina itself make investors hesitate to invest. Then, the oil and gas mafia issues in Indonesia as stated by the Indonesian President Joko Widodo that the reason that always hinders Indonesia's oil production is because of the oil and gas mafia that surrounds the Indonesian oil and gas industry by utilizing oil imports to get a lot of profit, while this is detrimental to the state

4 Conclusion

Based on the above, it illustrated the complex relationship between Indonesia and Saudi Aramco in the negotiation process between the two parties but did not reach an agreement.

Under the variables studied in the concept of political bargaining models, it shows that the bargaining process affects the cancellation of Saudi Aramco investments. In terms of objectives and resources, can fulfill both parties. However, in terms of obstacles, the Indonesian government is less able to handle the problems. Then, the thing that affects the most is the problem of an unhealthy investment environment in Indonesia, which makes investors less confident to invest. This also happens a lot in foreign investment cases that occur in Indonesia.

Acknowledgement

I would like to thank my supervisors in International Relations, University of Indonesia, Asra Virgianita, Ph.D. so that this article could be submitted in the International Conference on Indonesian Social & Political Enquiries 2021.

References

- [1] ESDM, "Statistik Minyak dan Gas Bumi tahun 2016," 2015. <https://www.esdm.go.id/assets/media/content/content-statistik-minyak-dan-gas-bumi-tahun-2016.pdf> (accessed Nov. 04, 2020).
- [2] FGE, "Asia Pacific Databook 2: Refinery Configuration & Construction, pages 49-51; FGE Asia Pacific Databook 3: Oil Product Balances, page 29," 2020. <https://www.fgenergy.com/latest-reports-and-analysis/FGI+-170+FGE+Gas+Databook-+Asia+Pacific+Natural+Gas+-+LNG--Annual+Update-320.aspx?Page2Id=61&pageSize=5>.
- [3] CNBC, "Maaf Pak Jokowi, Saudi Aramco Pilih Malaysia Ketimbang RI," 2019. .
- [4] CNBC, "Meski Jokowi ke Arab, Negosiasi Kilang Cilacap Masih Alot," 2020. .
- [5] L. Eden, S. Lenway, and D. A. Schuler, "From the obsolescing bargain to the political bargaining model," *Int. business-government relations 21st century*, 2004.