



ANALYSIS OF FREEPORT SHARE DIVESTMENT SCANDAL – 14 DECEMBER 2015

Asia Group Advisors (AGA) would like to provide you with an analysis of the ongoing political imbroglio related to the divestment of shares in Freeport Indonesia. The trigger for the scandal was Minister of Energy and Mineral Resources Sudirman Said's releasing a recording of Indonesia's House of Representatives (DPR) Speaker Setya Novanto asking for a 20 percent stake of the mining giant Freeport Indonesia in exchange for securing the company an extension of its mining contract, and then reporting Speaker Novanto to the DPR's Ethics Council.

The Freeport case is likely to have repercussions that stretch well beyond the immediate uproar it has caused. Minister Said is taking on some of Indonesia's most powerful vested interests, and there is now an opportunity for meaningful reform in the country's long troubled energy sector. More importantly, the case highlights the unique position President Joko Widodo finds himself in. An outsider to national politics before taking office last year, President Widodo is not part of the unholy alliance between Indonesia's political and economic elites which in the past has created very narrow parameters for reform. He is from a new generation of political leaders in Indonesia that is not bound by past compromise.

On 2 December, Minister Said played a recording of a June 8 conversation between Speaker Novanto, businessman Riza Chalid, and President Director of Freeport Indonesia, Maroef Sjamsoeddin. Sjamsoeddin had taped the conversation and passed it on to Minister Said. In the recording, Novanto appears to request a 20% stake in Freeport Indonesia, in exchange for helping the company get an extension of its mining contract. Novanto and his associate Chalid also suggested the shares would go to President Joko Widodo and Vice President Jusuf Kalla. Both the president and his deputy have denied any involvement in the matter and publically scolded Novanto for using their names. Meanwhile, Chalid is currently embroiled in a separate scandal involving allegedly manipulated trades with state-owned oil trader Petral.

Freeport's mining contract with the Indonesian government expires in 2021, but the company, which for decades has run the world's largest gold and copper mine in Papua, has been pushing for an early contract extension that would allow it to begin a USD18 billion investment in an underground mine. Indonesian law mandates that the negotiations can't begin until two years before the contract expires.

The deal proposed by Speaker Novanto brings back memories of the New Order era, where blatant rent-seeking was commonplace. Moreover, Novanto's deal looks like a carbon copy of the deal Freeport struck the last time it extended its contract. In 1991, the Indonesian government required Freeport to divest a 10 percent stake to a local partner. At the time the company was also seeking an extension of its contract. Freeport sold 10 percent to influential businessman Aburizal Bakrie's Bakrie Group for US\$213 million, and also guaranteed a US\$173 million loan to finance the purchase. Less than a year later, Bakrie sold half of the shares back to Freeport for US\$212 million, and sold the remainder of the shares some time later for US\$303 million, making close to 1,200 percent profit on its original USD 40 million investment. In the meantime, Freeport obtained its contract extension.

While Indonesia has moved into a new era, politicians like Novanto have not, and this goes a long way in explaining both Novanto's actions and the public uproar the proposed deal has caused. Minister Said has gained strong popular support for exposing Novanto, a close ally of Aburizal Bakrie, now head of the Golkar Party, and a petition calling for Novanto's dismissal from parliament was signed by close to 90,000 people. Both the president and the vice president have publicly condemned Novanto for using their names in the attempted shake-down of Freeport, and called for law enforcement to pursue the case. Novanto has answered by reporting Minister Said to the police for defamation, slander, and violations to the ITE (Electronic Transaction Information) Law by releasing the recording.

At the moment Minister Said has the wind in his back. The President and the Vice President are firmly behind him and he has strong public support. However, by exposing Speaker Novanto and Chalid, Minister Said is taking on powerful economic and political interests that are unlikely to

lay down without first putting up a fight. In the past, Indonesia's political and economic heavyweights have been known to retaliate when implicated in corruption shake-ups. Only earlier this year, the leadership of Indonesia's highly-regarded Corruption Eradication Commission (KPK) was forced to resign over drummed up criminal charges, which came as retaliation for investigating the personal finances of the leading candidate for National Police Chief.

Unlike the KPK case where President Widodo was slow to intervene, he has this time acted early and forcefully. A year into his term, President Widodo appears to have realized the benefits to being a political outsider. As Indonesia's first elected president without a political or military career stretching back to the New Order era, he has more room to operate than his predecessors. With strong popular support, President Widodo is not dependent on his political party to further his political career, and he does not need to return political and economic favors to special interests. Allowing the Freeport case to move forward is a clear sign of President Widodo's independence, and he now has an opportunity to use the momentum created by the case to further push his reform agenda.