

6.7 The Restructuring of PT. PANN

PT. PANN submitted their newly prepared Business Plan 2011 – 2015 in May 2011 to MOF at the ministry's request, and held several meetings for discussion and revision. Communications between the two parties appear constructive and honest. In this connection, the restructuring plan proposed by PT. PANN consists of two (2) components: (1) Loan Restructuring as explained in 2 above, and (2) Business Restructuring. The gist of the representative component of (2) is the separation and spin-off of their core business.

It is understood that the component of the spin-off can be approved under the competence of MOF; but the loan restructuring needs final approval by the President and the Parliament. Eventually, a Government Regulation will be issued. According to the officer of PT. PANN in charge of the negotiation with MOF, the proposal is under the process of evaluation by the Committees and waiting to be approved by higher authorities as of the end of September 2011.

1) Confirmation of Debt Amount Payable to MOF

Many pending accounts of state receivables incurred from sub-loans provided by MOF, both principals and associated interests and penalties that are overdue, became the issue between not only PT. PANN but many other SOEs and MOF. Finance Minister Regulation No. 17/PMK/05/2007 entitled SETTLEMENT OF STATE RECEIVABLES SOURCED FROM SUB-LOAN AGREEMENT AND LOAN AGREEMENT ON SOE was issued for the purpose of responding to and settling this issue. State receivables to be settled with reference to the procedures of restructuring of SOEs are defined in Article 3 of the PMK. SOEs that require the settlement of their overdue payables to MOF are defined in the succeeding Article 4. Modes of settlement under this PMK are provided in Article 6. For PT. PANN's case, rescheduling, change of debt conditions and state capital infusion are considered applicable.⁴

MOF (Directorate of Sub-Loan Management, DG of Treasury), PT. PANN and BNI (for the Airplanes only) / BRI (for the Fishing Boats only) held meetings in 2007 to reconcile PT. PANN's liabilities, as of 31 December 2006, arising from the sub-loans mentioned below and agreed to the amounts payable by PT. PANN. They further agreed that these liabilities would be settled with these amounts, and 31 December 2006 is the cut-off date. With these agreements, these liabilities were officially given recognition of stopping the accrual of interests and other charges at the cut-off date. The confirmed and agreed amounts of state receivables are:

US\$ 190,126,691.50 (SLA No. 775 for Aircrafts) equiv. to Rp. 1,708,979,533,276-

US\$ 271,020,278.09 (SLA No. 779 for Fishing Boats) equiv. to Rp. 2,436,743,320,304-

Total: US\$461,146,969.59 equiv. to Rp. 4,145,722,853,580-

(Converted at Rp. 8,991/US\$)⁵

⁴ Elimination of debt is provided as the mode No. 4, but PT. PANN has excluded this mode from the proposal for restructuring.

⁵ According to PT. PANN, the original exchange rates denominated in Rp. against US\$ are much lower than the current rate, so they are claiming for the special rate to minimize their burden.

Amounts in US\$ are fixed, but equivalent amounts in Rp. are tentative and subject to change as to the applied exchange rate to be agreed upon between MOF and PT. PANN.

2) Loan Restructuring

The total amounts in US\$ to be settled have been confirmed as above, for which PT. PANN has proposed the following settlement to MOF:

- Conversion to Equity: Rp. 2,349 Billion (57%) equivalent to US\$ 261 million, covering the principals of the original sub-loans;
- Renewed Sub-loan: Rp. 1,796 Billion (43%) equivalent to US\$ 200 million, under new repayment schedule

(Equal installments over 16 to 20 years) and zero interest rate, covering the interests and penalties accrued due to the pending repayment of original sub-loans

(Total): Rp. 4,145 Billion (100%) equivalent to US\$ 461 million (exchange rate: Rp 8,991/US\$)

3) Business Restructuring

Two Scenarios

It is understood that PT. PANN is considering two scenarios for what they call “Business Restructuring”; they are: (Scenario 1) spin-off of their ship lease business⁶ to a newly established subsidiary company under the existing PT. PANN and (Scenario 2) transfer of the business to a subsidiary of an existing parent company. Both the scenarios are depicted in Figures 6.7.1 and 6.7.2.

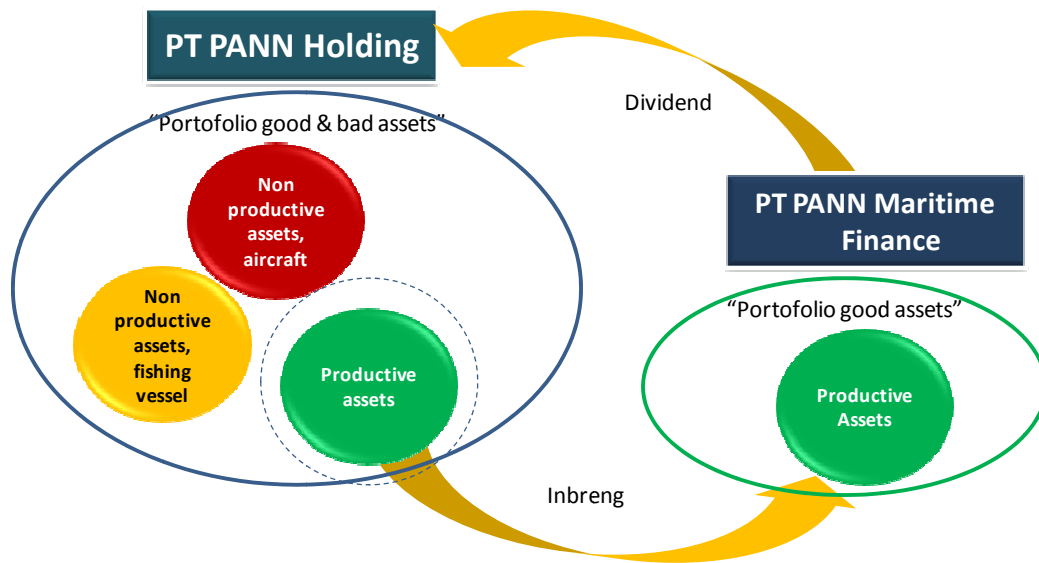
Under Scenario 1, a subsidiary company which receives the core business from the parent company will have to be established by the existing PT. PANN. This subsidiary company needs to obtain the license of leasing business from MOF. Because of the PT. PANN’s negative equity and status as unhealthy SOE, MOF has been requested in the proposal to relax requirements of the related law regarding the establishment of subsidiary company by SOE. This business restructuring should be realized under the competence of MOF.

In case of scenario 2, PT. PPA (*Perusahaan Pengelola Aset*) is assumed to become the parent SOE, subject to the appointment by Ministry of State-owned Enterprises or MSOE, and would purchase the core business of PT. PANN to transfer it to their subsidiary, PT. PPA Finance. Both subsidiary and parent companies would be SOEs. Scenario (2) is generally called business transfer. It may be realized under the competence of MSOE. In this connection, PT. PPA is reported in Annex 6.6.

PT. PANN will have to select either scenario at a certain point in time, leaving out the other. PT. PANN prioritizes Scenario (1) if the approval of the Minister of Finance is obtained soon enough.

⁶ Relevant assets and liabilities and equity as well as officers and employees are included. PT. PANN is not considering any lay-off of their employees subsequent to this business transfer.

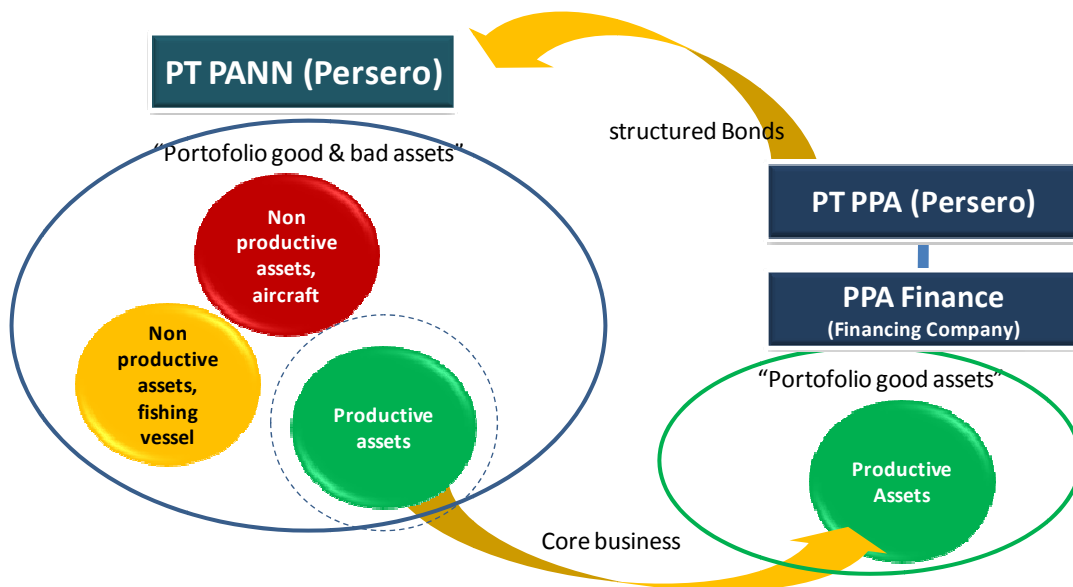
Figure 6.7.1 Business Restructuring – Scenario 1



- ➔ PANN Holding transfer productive assets to PANN Maritime Finance;
- ➔ PANN Maritime Finance will be further developed;
- ➔ PANN Maritime Finance business growth will provide increasing value of the company, so in the future it can be utilized to settle the loan of PANN Holding to the Government.

Source: PT. PANN Presentation in October 2011

Figure 6.7.2 Business Restructuring – Scenario 2



- ➔ Agreement between PT PANN & PT PPA about business restructuring (spin off PANN's core business to Financing Company (a subsidiary of PPA)). This agreement should be approved by Ministry of SOEs;
- ➔ This scenario is intended to speed up the process of spin off the core business to catch the opportunity of TSL JICA loan;
- ➔ If restructuring process in Minister of Finance already completed and the subsidiary company of PT PANN (PT PANN Maritime Finance) has been established, then the core business should be transferred back from PT PPA's Finance company to PT PANN Maritime Finance.

Source: PT. PANN Presentation in October 2011

Business Restructuring to be Realized under MSOE (Scenario 2)

The Business Restructuring Plan to be approved and supported by MSOE has been proposed by PT. PANN and the subsequent preparation is going on among the concerned parties. The concept of the business transfer is shown in Figure 6.7.3.

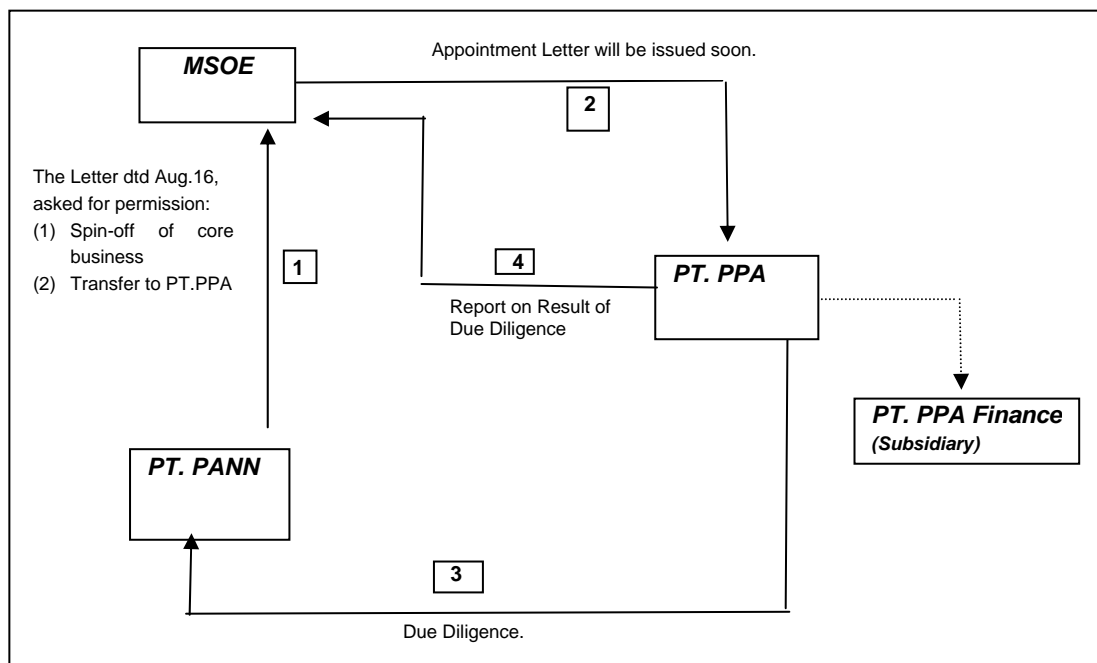


Figure 6.7.3 Concept of Proposed Business Transfer

EA Confirmation in SLA

For the formulation of an ODA loan project, it is critically important to confirm the executing agency. Another critical point is, particularly in this proposed two-step finance project, which is going to make a sub-loan agreement (SLA) with MOF. According to PP No. 10/2011, the executing agency must be the entity which will make an SLA with MOF. As explained in (4), two (2) scenarios might be considered at this time, they are:

- (1) PT. PANN Holding (tentative name) makes an SLA with MOF as E/A, draws down the proceeds and on-lends the fund to PT. PANN Maritime Finance (also tentative name), which delivers lease finance to the end-borrowers. As PT. PANN is just about to submit their project proposal for the PSFP to BAPPENAS, there would be no problems or obstacles to meet the requirement of the said PP.
- (2) If the business transfer to PT. PPA is implemented, it is not yet clear who will be the E/A, either PT. PPA or PT. PPA Finance, even on the assumption that BAPPENAS understands the modification of E/A, that is from PT. PANN to PT. PPA or PT. PPA Finance.

4) Recent Efforts to Appoint PT. PANN as EA

In the course of the JICA Survey until the mid December 2011, PT. PANN and the related government agencies have made concerted efforts to Appoint PT. PANN as EA for the PSFP. They are briefly reviewed as follows:

PT. PANN and MOF

- PT. PANN submitted its business plan 2011-15 to MOF in April 2011. After the consultation with Directorate of Investment Management System, MOF in May, it was amended and approved.
- PT. PANN submitted its loan restructuring plan to MOF in May. There were several discussions and amendments and then it was approved by Finance Minister in November according to Director of IMS.
- In November Directorate of Investment Management System invited PT. PANN to discuss the company's business perspective until 2026 at the technical committee of MOF.

At the inception of the JICA Survey, Director of IMS mentioned that MOF would recommend PT. PANN as EA for the PSFP with two conditions, first, the company's government debt issue would be solved with MOF and, second, the company's business perspective would be promising. Although MOF has stepped slow, the ministry has paid attention to PT. PANN to make it financially healthy and business capable.

PT. PANN and MSOE

- PT. PANN requested Minister of SOE to cooperate with PT. PANN's business restructuring in June 2011.
- MSOE introduced PT. PPA and its subsidiary, PT. PPA Finance to receive PT. PANN's core business (ship leasing) in September. This scheme still remains as an alternative.
- PT. PANN wrote letter to Minister SOE to approve the PSFP to be implemented by PT. PANN on 5 December 2011.
- Minister SOE approved PT. PANN's project proposal on 12 December 2011 and informed the decision to Finance Minister and Chairman of BAPPENAS.

From the beginning of the JICA Survey, MSOE has supported PT. PANN to work as EA for the PSFP. MSOE also prepared an alternative to PT. PANN for its business restructuring.

PT. PANN and BAPPENAS

- Vice Chairman of BAPPENAS (Infrastructure and Facilities) sent a letter to Vice Minister of SOE (infrastructure and Logistics) to help PT. PANN's business restructuring for national connectivity development in August 2011.
- PT. PANN submitted the PSFP project proposal to BAPPENAS on 30 September 2011.
- PT. PANN wrote to Chairman of BAPPENAS to request the inclusion of the PSFP into 'Blue Book 2010-2014' on 5 December 2011.

BAPPENAS has taken a leading role among the JICA Survey relevant government agencies. Director of Transport has worked as the head of the counterpart team and coordinated with relevant agencies such as MOF, MSOE, Coordinating Ministry of Economic Affairs, MOT and MOI. However, as of the mid December 2011, the PSFP has not been included into 'Blue Book 2010-2014'.

7 CONCLUSIONS AND RECOMMENDATIONS

1) Conclusions

The PSFP scheme has been widely practiced in Japan since the mid-1950s and has been applied in three (3) Japanese ODA loans for the development of domestic shipping and its related infrastructure and facilities in the Philippines. The same scheme was initially proposed for Indonesian domestic shipping development in 2005. The PSFP concept, or a similar innovative ship finance, is included in INPRES No.5/2005 concerning the empowerment of the national shipping industry.

Due to the successful implementation of INPRES No. 5/2005, the country's cabotage right has been almost fulfilled until 2010. Beside such quantitative satisfaction, however, qualitative issues still remain in domestic fleet development, represented by its aging fleet profile. In order to improve fleet quality and enable sustainable fleet replacement and procurement, the Study concludes that the implementation of the PSFP is still imperative.

Since commercial financing becomes a main stream aspect in ship finance in Indonesia, the JICA Survey designs the PSFP to take some catalyst roles which are badly needed in the current development stage of Indonesian domestic shipping, which the prevailing commercial ship finance hardly deals with. These roles include providing financing service to small-sized shipping companies, promoting new shipbuilding with technology transfer at domestic shipyards, enhancing ship safety through new shipbuilding and second-hand ship conversion, diffusion of ship management service and urgently expanding ship-repairing capacity. For these things to materialize, the PSFP must handle not only the financial aspect but also ship technology and shipping operation aspects. The main impetus for change from ordinary commercial ship finance is total service delivery rather than just financing.

According to the related government regulation, state-owned commercial banks and other financial institutions can receive a foreign government loan through a subsidiary loan agreement (SLA) with MOF. The Study assessed such state-owned financial institutions with regard to their management capacity as an executing agency of the PSFP.

Nominally, four (4) banking institutions have a right to engage an SLA with MOF. They are Bank Mandiri, BNI, BRI and Eximbank. In fact, Eximbank has no retail service. BRI has a nationwide branch network, but its ship finance is limited to state-owned enterprises. Bank Mandiri and BNI have recently boosted ship finance amounts among private shipping companies. But both of them do not employ any technical staff but just do ship finance business based on borrowers' business scale and past track records. Therefore, the Study has not found any possibility for one of the state-owned commercial banks to work as a PSFP executing agency.

PT. PANN, a dedicated ship finance institution, shares the same mission with the PSFP and has good records in ship finance since its inception. PT. PANN was involved in the previous national shipbuilding project, Caraka Jaya, and is keen on ship safety and ship management. Leasing service is the most suitable financing concept for maritime business, particularly small shipping companies. PT. PANN has the capability and capacity to withdraw the vessel from non-performing operator and the ability to operate the same vessel. Taking such company characteristics into account, the Study confirms

the endorsement of DGST/MOT, Bappenas and MSOE to appoint PT. PANN as a PSFP executing agency prior to the Study.

The JICA Survey has identified three (3) subproject targets for PSFP. They are:

- (i) Second-hand vessel procurement with modification;
- (ii) New shipbuilding with technology transfer; and
- (iii) Urgent shipyard capacity expansion.

The JICA Survey has tentatively prepared a Japanese ODA loan of 30 billion Yen to implement sub-projects and allocated 450 million yen for associated consulting service. The Study has also designed the PSFP implementation scheme and operation guideline where the functions of the EA (PT. PANN), the PMU (the unit for daily supervision and technical assistance) and a higher policy supervision and sub-project authorization mechanism are spelled out.

The applicable SLA has been elaborated with MOF. In the scheme, PT. PANN would be free from the exchange risk from Yen to Rupiah since MOF intends to set interest rate in Rupiah according to the related ministerial decree. PT. PANN, however, must undergo a restructuring process to alleviate excessive debt in order to work as the EA in the project. PT. PANN submitted its business plan (2011-2015) with a loan restructuring plan and a corporate restructuring plan to MOF. With intensive works and discussions between PT. PANN and MOF during the Study period, the business plan (2011-2015) and the loan restructuring plan were approved. However, for PT. PANN to make a spin-off subsidiary for its core business under the competence of MOF, it is waiting to be approved by higher authorities as of the middle of December 2011.

PT. PANN submitted the project proposal to Bappenas on 30 September 2011. However, it has not been included in 'Blue Book 2010-2014' as of the middle of December 2011.

2) Recommendations

The PSFP has been designed to address contemporary sector issues such as financing service to small shipping companies, technology transfer of shipbuilding, alleviating shipyard congestions and diffusion of ship management. The implementation mechanism is doable. It envisages high economic impact. Japanese ODA loan will be tapped into the PSFP implementation. But it is managed by an SLA between MOF and PT. PANN who has enough knowledge and experience to work as an executing agency (EA) and to take business risk. Therefore it is firstly recommended to implement the PSFP without delay.

Although Indonesia experienced some government initiated shipping projects before, this PSFP is different. The PSFP has several distinguishable features such as bottom-up approach from the proponents, focus on small shipping companies, leasing and simple ship collateral arrangement and technical assistance.

The PSFP will give financing services to the three sub-project targets widely. But the fund amount would meet just several percent of the total ship finance needed in the coming years. To maximize the development effect of the PSFP, it is recommended to demonstrate and disseminate PSFP's unique service and technology, including:

- Innovative ship finance: It is desired to give financing service to small shipping companies. To make it happen, it provides total delivery service rather than just

financing, including various technical assistance and advice, ship leasing and simple ship collateral, etc;

- Ship management: Financing and ship management is uniquely combined in the PSFP mechanism. Ship management contributes to protect vessels from unnecessary asset devaluation. It is considered to provide a guarantee, in part, for the ship financing scheme.
- New shipbuilding for middle-class vessels: Taking the country's economic condition, huge domestic fleet need and international second-hand market into account, it is natural to steer ship finance towards new shipbuilding. The PSFP employs a package deal method between domestic shipyard and advanced foreign shipyard which enables to supply qualified middle-class vessels in line with technology transfer.

In the course of the Survey, a crucial factor in project preparation undertaking has been the identification and appointment of EA. At the outset, PT PANN was regarded capable and suitable as EA of the proposed public ship finance program. In order to work as EA satisfactorily, however, PT. PANN is required to enhance its capability particularly at the two points:

- Technical capability – In the PSFP, PT. PANN will handle a variety of lease assets. But some kinds are not found in the existing company asset list, particularly newly built middle-class vessels and shipyard facilities. For instance, RORO vessel has a unique structure to allow vehicle to move around inside and roll-on/roll-off. It is rather difficult to keep it in good condition. The current technical capability must be enhanced to handle various and valuable leasing assets.
- Marketing capability – During the field survey over the country, the team found that many local shipping operators did not know PT. PANN. The company currently operates at HQ in Jakarta without a branch office. To implement the PSFP, however, PT. PANN must reinforce its weak marketing. Otherwise, the PSFP cannot spread its benefit throughout the country. PT. PANN will have to utilize various available channels and connections such as industry associations and chambers of commerce.

In the implementation phase, the performance of the PMU will be critically important. The PMU will do daily supervision, government policy implementation and technical assistance. DGST/MOT is responsible for domestic shipping development policy while MOI is responsible for shipbuilding and repairing industry. Both the agencies are required to identify and give advice on sub-projects for their policy implementation. The PMC will support the PMU and will give various technical assistance services to PMU members, end-users and other project related personnel and organizations. It is thus recommended that the PMU be composed of capable members who are keen on maritime industry development including capacity development.

Indonesia has many islands with vast water territories. There are so many kinds of domestic shipping needs and they are all essential to sustain local economies and societies and maintain inter-island connectivity. The domestic industry consisting of numerous small shipping companies is deemed an inherent and unchangeable industry structure. Many shipping services are provided at sustainable level and far from fat profit margins. Therefore, public ship finance is necessary between government subsidized services and profitable commercial services.

In this sense, the proposed PSFP is the first attempt of public ship finance in Indonesia.

During the PSFP disbursement period, it is strongly recommended to forge a continuous and more effective public ship finance scheme among the related government agencies and PT. PANN.