Dragoman Digest

Indonesia steps up SOE reform drive with new public listing

The offering could provide a boost to Indonesia's renewable energy goals

Indonesia intends to publicly list a subsidiary of its state-owned oil giant Pertamina; Pertamina Geothermal Energy. The IPO – planned for late 2022 – would be the first of Pertamina's subsidiaries to be listed. Indonesia seeks to raise US$500 million from the IPO.

The listing is part of Minister of State-Owned Enterprises Erick Thohir's reform and consolidation of the US$606 billion SOE sector. Thohir aims to create companies with global scale and greater efficiency. Overall, the government aims to reduce the number of SOEs from 108 in 2019 to 41 by 2024. Jakarta plans to take at least 14 SOEs public. Indonesia's IPO push started last year with the US$1.3 billion listing of telecom tower company PT Dayamitra Telekomunikasi. A consolidation of SOE hospitals is also in the works. IPOs are intended to reduce SOE's chronic indebtedness and coincide with the creation of a foreign investment and structuring channel, INA, which has co-investors including both local and international pension funds.

Capital raised through Pertamina Geothermal Energy IPO will be used to accelerate Indonesia's transition from coal. The subsidiary has total installed geothermal capacity of 672 MW, which it intends to double to 1.3 GW. Indonesia intends to have seven GWs of geothermal generation capacity by 2030. Pertamina Geothermal's IPO, and recently announced plans to restructure and privatise parts of state electricity monopoly PLN, demonstrate that Jakarta will tap global markets to help Indonesia's energy transition. A test of the reforms and processes will be the ability of the Government to present to investors assets and operations free of the pervasive rent-seeking that has handicapped investment in the past. Coal mining is a prominent activity of Indonesia's influencers.

Apple eyes India and Vietnam in shift away from China

Attracting Apple suppliers has provided a high-profile boost to both countries' manufacturing agendas

In September, Apple announced that for the first time it is manufacturing its latest iPhone model (currently the iPhone 14) in **India**. Apple intends to develop India as an alternative production base and has set a target to produce 25 percent of all iPhone 14s in India by 2025. It has also asked suppliers to relocate AirPod production into India. Currently, more than 90 percent of Apple devices are made in China. **Vietnam** is also benefiting from Apple's gradual shift away from China. In August, Apple suppliers Foxconn and Luxshare Precision Industry started the test production of Apple watches and MacBooks in Vietnam.

The relocation of production is expected to be a boon for India and Vietnam's respective aspirations of moving higher up the manufacturing value chain. Launched in 2014, **Prime Minister Modi**'s 'Make in India' initiative for example, aims to transform India into a global design and manufacturing hub. Though the initiative has fallen far short of the headline target to boost manufacturing to 25% of GDP by 2022, India's production of handsets has been a clear success story. India now produces 16 percent of global handsets, up from 9 percent in 2016, having gained market share from China.

Both India and Vietnam will have to resolve broader structure obstacles to continue to graduate towards higher value-added manufacturing. Skills and education quality, electricity supply and infrastructure quality constrain both countries' manufacturing industries. Promotable big-ticket announcements like Apple's relocation may distract from the urgency of deeper reform.

Central Asia's economic outlook defies dire expectations

Multiple factors underly the region's unpredicted resilience

Following **Russia**'s invasion of **Ukraine**, the European Bank for Reconstruction and Development (EBRD) had forecast a bleak outlook for Central Asia. In particular, the region's reliance on Russia for remittances was expected to be a strong downside risk. Seven months on, the EBRD's September report strikes a more sanguine tone. The latest report expects Central Asia's output to grow by 4.3 percent in 2022, and 4.8 percent in 2023. This is up 1.2 and 1.1 percentage points, respectively, from May's forecast.

Several factors underly the improved outlook. Firstly, resource rich economies like **Kazakhstan** and **Turkmenistan,** are reaping the benefits of higher oil and gas prices and appetite for non-Russian energy supply. Secondly, remittance flows from migrant workers in Russia have actually increased – up 96 percent year-on-year to **Uzbekistan** alone in the first half of 2022. This also suggests that elements of the Russian economy are holding up better than expected. Lastly, parts of Central Asia are effectively serving as a conduit for bypassing Western sanctions. **Tajikistan** reported an 85 percent increase in imports from China in the first seven months of 2022. Whether the EBRD's forecast stands the test of time given partial mobilisation in Russia and a souring global economic outlook, remains to be seen.

Another untapped Middle Eastern gas field looks set to be unlocked

Global supply ructions incentives creative Israeli diplomacy

A 28.32 billion cubic metre gas field off the coast of Gaza looks soon to be unlocked after an agreement was reached between **Israel** and **Egypt** on October 6. Under the terms of the deal, Israel will export most of the Gaza Marine field's gas to the **EU**. The remaining volumes will be shipped to Egypt. The revenue, which will be collected by the **Palestinian** Authority (PA), will in turn partially be partially distributed in Gaza – though the exact monetary figures and terms of this arrangement remain unknown. The field's development had been blocked by Israel since its discovery by British Gas in 1999. However, elevated gas prices in the wake of **Russia's** invasion of **Ukraine** encouraged a more pragmatic Israeli Prime Minister in **Yair Lapid** to commence negotiations early this year.

The agreement is the latest example of diplomatic efforts to cash in on Europe's demand for non-Russian gas. On Tuesday, Israel signed a draft agreement with **Lebanon** to unlock the 49.55 billion cubic metre Karish gas field, potentially resolving a 15-year-long maritime dispute.

These agreements could yet be spoiled. The fate of both agreements will depend on the reactions of armed non-state actors in Hamas, and Hezbollah . Hezbollah pointedly threatened to attack Israel's gas operations in the Karish field. This rhetoric has been leveraged by Israeli opposition leader Benjamin Netanyahu, who accused Lapid of "surrendering" to Lebanon and Hezbollah. Depending on how revenue from the Gaza field is distributed, Hamas may also have incentives to disrupt operations.

Japanese companies lead the way on supply chain realignment

Concrete examples emerge of companies relocating manufacturing away from China

Japanese companies have been at the forefront of efforts to mitigate supply chain dependence on **China**. In April 2020, the Japanese government offered US$2.2 billion worth of subsidies to companies onshoring or moving production to Southeast Asia. Whilst, as in other countries, actual relocation efforts have not been commensurate with corporate rhetoric, there have been several recent examples of Japanese companies diversifying operations away from China. Air conditioning manufacturer Daikin, which imports 20 percent of its parts from China, is in the process of relocating its circuit board production to **Malaysia**. Other companies, such as robotics company Yaskawa, have chosen to onshore production. Yaskawa plans to invest up to US$415 million to build a new home appliance component factory as part of a plan to onshore production 50 percent of its inverter component production by 2027.

China offers unparalleled advantages in economies of scale, notably in the production of electronic and machinery. Japan's imports from China in these areas total US$54 billion and US$35 billion respectively. China's domestic market has typically been more profitable than other regional markets for Japanese companies. So, any diversification by Japanese companies will have natural limits so long as China remains attractive.