Time For An Indonesia Road Fund

BY RAJ KANNAN

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Newly-appointed Finance Minister Chatib Basri has been emphatic both to the parliament and to the market on the importance of higher fuel prices to ease the burden on the country's finances. More notable is his assertion that the costs saved by the subsidy reduction will be used to provide targeted aid to the lowest income groups and to provide the much-needed infrastructure improvements for the country.

Let's look at the numbers involved: The current subsidized fuel price is Rp 4,500 per liter (about $0.45) and one of the lowest in the region. In 2009 this subsidy cost the country Rp 45 trillion ($4.6 billion). However, given that 40% of the fuel used here is imported, the subsidy last year rose to a whopping Rp 212 trillion ($22 billion) or 2.6% of GDP. For 2013, the subsidy under the old price would have risen to Rp 297 trillion ($30 billion). Now under the recently approved Rp 6,000 per liter, it will reduce the subsidy by Rp 30 trillion ($3 billion).

The government has stated that half of these savings would be provided as direct cash assistance to around 16 million households living on less than $2 per day. It is unclear, however, how it plans to use the balance of the savings to improve infrastructure. The government's current track record in infrastructure provision is lacking and most recent reforms to fast track infrastructure delivery remain untested. Therefore, simply stating that the fuel price increase will lead to better infrastructure is not going to cut the mustard.

One possible solution for this lack of visibility on the benefits of the fuel increase is the establishment of the Indonesia Road Fund (IRF) to build both national and regional roads. The IRF will send positive signals that the government is serious about using the subsidy savings to also provide better infrastructure via a properly structured and transparent institutional framework.

Other countries in the region, notably India, have achieved tremendous progress in delivering better roads across their country via its Central Road Fund (CRF). The CRF, launched in 2000, was expected to generate around rupees 2,000 crores ($450 million) in its first year. Instead, the CRF generated close to rupees 5,600 crores in its first year and in 2012 the CRF generated over rupees 18,000 crores.

In Indonesia, the government recently announced plans to build over 2,700 km of the Trans Sumatra Highway and the 1,000 km Trans Sulawesi Highway. These highways would require major funding commitments from the government since these roads connect under-developed areas where income levels are insufficient to afford full-cost-recovery toll fees. Indeed, it's for these types of projects that the IRF can be effectively deployed and more importantly the government can show evidence that these fuel increases are generating greater good for the whole country by enabling nation building projects.

No doubt the skeptics will point to other infrastructure-related development funds that have yet to achieve tangible results. Precisely for these reasons the IRF must be well structured and professionally managed by an institution that has the oversight of the Ministry of Finance but without the inherent problems that comes with being a government agency. In particular, I refer to the unreasonable criminal stigma and legal issues related to causing a loss to the state on management decisions that are purely and transparently commercial in nature.

It is time for Indonesia to launch its own Indonesia Road Fund in tandem with higher fuel prices to positively and strongly demonstrate that these subsidy savings will be put to good use to increase economic development, thus prosperity in the country.