Political Economy of Net Zero: Indonesia

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Structural issues relating to the partial and separate management of Net Zero Emission (NZE) sectors are the largest bottleneck for Indonesia to achieve net-zero emissions. However, opportunities arise to respond to these challenges from new emerging trends namely blended finance, a Just Transition for all (starting with the energy sector) and multi-level engagement and coordination, especially at the sub-national level.

Accelerating the transition
Political Economy Context

Indonesia aims to achieve net-zero emissions by 2060. Public and private actors have spent $116.2 billion on climate action in the country over the past 30 years. However, six underlying political economy issues have been identified as hindering Indonesia’s achievement of this goal.

First, Indonesia does not have a stable policy environment that can support long-term emission reduction projects. There is limited confidence that the current policy will not be reversed due to political change [1]. Also, most of Indonesia’s climate commitments are not immediately and clearly reflected in the national and subnational regulatory system [2]. For example, Indonesia’s Long-Term Strategy (LTS) for Low Carbon and Climate Resilience 2050, submitted at COP 26, is not legally binding as it has not been enshrined as national law or a government, presidential or ministerial regulation [3,4].

Second, policy signals are not consistent with political commitments. For instance, in the energy sector, there have been abrupt policy changes driven by short-term economic needs and opportunities arising from market and price fluctuations increasing fossil fuel subsidies and distracting from the phasing down of coal. Direct and indirect fossil fuel subsidies are still in place for both the general public and industry, despite the government’s commitment to reduce the use of such energy sources [5]. In addition, the coal trade often diverts the government from its pledges and distracts private sector action, undermining investments in net-zero solutions [6,7]. Since the global price of coal has increased due to the Russia-Ukraine war, the government has introduced a short-term ban on exports to regulate its domestic stock, however overall it is allowing coal exports to benefit from the higher global prices [8].

Third, the majority of public and private financial resources are still allocated to carbon-intensive activities rather than net-zero options. Indonesia needs at least $200 billion per year to realise its climate agenda [9], but the average annual contribution from the domestic public budget in 2015–2020 was just $4.5 billion (2.25% of the required amount) while the government budget is largely allocated to carbon-intensive businesses [10,11].

Fourth, Indonesia lacks a coherent strategy for reaching net-zero emissions and policies in certain sectors interfere with NZE achievements in other sectors. For example, the government has been pursuing a biofuel programme based on palm oil, called B100. This policy will result in emission reduction within the energy sector at the cost of greater emissions from agriculture, forestry and other land use (AFOLU) due to oil-palm expansion, deforestation and large-scale land conversion [12].

Fifth, some independent voices supporting emission reductions, including the academic sector, that are in disagreement with the government receive little attention. The media focuses on popular issues, distracting the public from important matters and paying little attention to policies and essential development issues, such as reducing emissions from deforestation and forest degradation (REDD+) [13]. They also rarely give space to marginal voices many of whom represent people living at the frontiers of climate change [14–16].

Sixth, both government and non-government actors deal with net-zero emissions in silos. For example, the government mangrove management lacks clear regulations and institutional arrangements, and so conservation and development priorities conflict [17]. For non-government actors, climate activity suffers from spatial and temporal fragmentation due to competition amongst civil society organisations (CSOs) for resources and interest of funding organisations in different sectors [18–21].

Call to action

- The transition to net-zero emissions in Indonesia requires a cross-cutting, multi-level, multi-stakeholder approach.
- Broader coordination and engagement are needed to move away from sectoral approaches that hinder the achievement of the NZE target due to inconsistent and counterproductive policies.
- Some cross-cutting opportunities are emerging for philanthropy to respond to these issues, namely blended finance that enhances collaboration across public and private sectors, supporting a just transition for all, starting with the energy sector as a template for all NZE activities, and multi-level and multi-actor coordination mechanisms that engage sub-national governments, from provincial, district, all the way down to the village level.
The growth of NZE finance, trade and investment globally is rapidly increasing. In Indonesia, however, it is growing at a slower pace with the majority of public and private finance still incoherent and inconsistent with NZE. The Climate Policy Initiative (CPI), a US-based non-profit research group, calculates that global financial flows from bilateral, multilateral and privately-leveraged resources was $463 billion in 2015 and 2016, 574 billion in 2017 and 2018, and 632 billion in 2019 and 2020 – below the NZE annual funding target of $4.35 trillion annually by 2030, although the trend is positive [22]. In contrast, Indonesia’s climate spending has always been below target and is currently decreasing. The country requires climate finance equal to the amount of $200 billion per year, increasing to $253 billion by 2030, however allocated amounts were approximately $8.91 billion in 2018, $6.57 billion in 2019 and $5.23 billion in 2020 [23].

Fintech investments have increased consistently from $203 million in 2018 to 329 million in 2020 and although the majority continue to invest largely in brown businesses, fintech start-ups are beginning to invest in green businesses [24,25]. For example, ride hailing company GoTo is investing in electric motorcycles for its services together with electric vehicle (EV) charging stations (Electrum and Pertamina) and EV producers (Gogoro dan Gesits) [26]. These fast-growing fintech companies are potential collaborators for philanthropy in blended NZE finance strategies. For example, philanthropic institutions could provide micro and nano-level grants and technical assistance for pro-NZE businesses followed by commercial lending by fintech companies, once eligible.

Challenge

Current sustainability policies and the short-sightedness of budget and financial plans deter actors from investing in activities that lead to a net-zero economy. First, development partners and some NGOs can be locked into their own values and strict practice guidelines. For example, some organisations do not want to be associated with coal, although financing its phasing out is an important component in achieving net-zero emissions. Indonesia is currently experiencing an energy oversupply and, without coal retirement, new renewable energy development will have to be postponed. Second, budget and financial short-sightedness prevents actors from investing in the net-zero transition. For instance, the State Electricity Company (PLN) has had to postpone plans to build new renewable energy power plants because it is in unhealthy financial conditions. This makes it impossible to meet the high upfront costs of renewables, such as building geothermal steam turbines or purchasing batteries, a future-proof energy system and more advanced skills.

Opportunity

Blended finance is a co-investment opportunity for donor organisations, potentially enhancing coordination across stakeholders and financiers. A strategic use of philanthropic grants for large-scale feasibility studies and medium to long-term financial planning linked to match-making with commercial investors will mobilise more significant investments for NZE from private actors, multilateral banks and public bodies.

Philanthropic funding can be strategically deployed in executing agencies and other financiers for the pilot phase of net zero financial investments, including for scoping and feasibility studies, financial planning, visibility, facilitating research and development, partnerships, engagement strategies, knowledge...
KEY INTERVENTIONS, WHICH IF TRIGGERED, WILL SUPPORT A SYSTEMIC TRANSFORMATION TO NET ZERO.

transfer, or personnel capacity building in the early stages. Philanthropic participation in blended finance for NZE is essential to gather and populate micro efforts, converting them to large enough programmes that can access more substantial investments from multilateral banks, soft loans, private finance, commercial loans and blended finance. Indonesia has the largest geothermal potential in the world, estimated at 29,000 megawatts (MW) [28]. If utilised, geothermal power could increase the renewable energy contribution to Indonesia's energy mix, however, the development of geothermal power plants requires high initial exploration costs, stalling progress in this sector. A blended finance fund, called PT Sarana Multi Infrastruktur (PT SMI), which manages financial support from the World Bank's Geothermal Upstream Development Finance, has been mobilised to support exploration. This initial investment has leveraged more substantial investments in geothermal project development, such as business-to-business soft loans for geothermal companies, and is a good template for future investment. Blended finance can also invest in the setting up of a training and capacity building centre to supplement the lack of geothermal operations supervisors.

Philanthropic funding can also be a safety net to finance rapid responses and to troubleshoot problems that usually cannot be met by stakeholders during project deployment. During project deployment, there can be unplanned and immediate financial needs for consultation to resolve, for instance, rising land and regulatory conflicts, or for quick capacity building in urgently needed areas and competencies. In the case of the Muara Labuh power plant, there was spatial overlap between the geothermal power plant development and the tropical rainforest area; PT SMI and Presidential Staffs Officers\(^2\) were mobilised to facilitate the coordination meeting between the related ministries to negotiate and resolve the issue allowing the renewable energy production projects to continue.

Donor organisations can facilitate the consolidation of different funding sources to finance NZE projects. Philanthropic funds could play a match-making role in a blended finance system to improve the coordination of financiers, promote and increase the credibility of NZE projects, improve market confidence and contribute to de-risking the process together with the guarantee, hedging and insurance instruments. To date, Indonesia has set up three blended finance platforms, PT SMI under the Ministry of Finance (MoF), Global Finance Alliance (GFA) under the Coordinating Ministry of Maritime and Investment (CMMI), and Indonesia Investment Authority (INA) and has invested public funds through these platforms to leverage philanthropic and private investment for NZE. The leading ministries (MoF and CMMI) are also open to discussing with philanthropic organisations the improvement of the platforms, including increasing their credibility and supporting the development of de-risking instruments.

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2  Public officials with coordinating roles
3  The JETP is an effort to support developing countries in achieving early retirement of coal power plants and transitioning their economies towards cleaner energy with the support of the International Partners Group (IPG) and Multilateral Development Banks (MDP), focusing on initiatives to mobilise sovereign and non-sovereign funds under the coordination of JETP International Finance Working Group.
4  The number of pledges and estimated transition cost is subject to change and need further clarification
5  The JETP public and private finance schemes will likely take the form of concessional loans, grants and equity from governments involved in the JETP, and debt and equity from Glasgow Financial Alliance for Net Zero group banks and asset managers, respectively.
Indonesia has committed to integrating the Just Transition (JT) principles into its green transformation, starting with the energy sector and including the coal phase-out. However, guidance and references for their implementation are lacking. Indonesia is one of the signatories to the Silesia Declaration on the just transition, which demonstrates the country’s commitment in this area. The country also provides strategies and a framework for the just transition in its Nationally Determined Contribution (NDC) to the Paris Agreement (2021), Long-Term Strategy for Low Carbon and Climate Resilience (LTS-LCCR) (2021), and Low Carbon Development Indonesia (LCDI) (2021).

There is growing interest in the just transition, as outlined by the inclusion of the topic Just and Affordable Energy Transition Management in the 2022 G20 agenda and in the progressive development of projects like the Social Dimension of Just Transition of Coal in Indonesia by the World Bank. In November 2022, Indonesia, Japan, United States, and other partnering countries announced their participation in the Indonesia Just Energy Transition Partnership (INO-JETP) at the 2022 G20 event in Bali [29]. INO-JETP is co-led by the US and Japan and supported by Germany and other G7 countries. INO-JETP will be processed by PT SMI and MoF especially with regard to implementation, coordination and policy development considering the clean energy transition, the Just Transition and gender-mainstreaming [30]. The INO-JETP contributes $20 billion from the total $600 billion estimated costs for Indonesia to phase out coal-based electricity in favour of a grid powered by renewables [31]. Details of the financial package of public and private finance schemes are to be developed over the next six months [31].

**Challenge**
The just transition is an exciting direction of travel, but its operationalisation and mainstreaming is still unclear for CSOs and the private sector, and even for the government. Given its early stage, all stakeholders may have not yet got familiar with its principles, unlike gender equality, disability and social inclusion (GEDSI), which over the years have become mainstream.

**Opportunity**
There is a growing opportunity for philanthropic institutions to facilitate the mainstreaming of the just transition for civil society, government, the private sector and local communities affected by the changing economic environment associated with net-zero emissions.

The INO-JETP partnership is expecting support to develop an evolving financing package in the form of philanthropic grants, private soft loans or public and private investments. The package can support the technical aspects of the energy transition, including the early retirement and phase-down of coal power plants, re-negotiating coal take-or-pay contracts for plant enclosures, technology and capacity transfers for the development of renewable energy, boosting solar manufacturing, grid connectivity, Carbon, Capture, Utilisation, and Storage (CCS/CCUS), and the mainstreming of electric vehicles (EV) [32–34]. In addition, philanthropy can focus the efforts on the social justice and gender mainstreaming aspect of the transition by supporting the population impacted, especially coal miners and workers, and new workers entering the green energy sector [32].

Beyond the INO-JETP commitment, the just transition for all principles can be applied broadly and encompass other sectors and social causes. In this regard, areas of focus for philanthropic organisations could be: 1) to invest in activities with long-term impacts, such as building knowledge and capacity of stakeholders (CSOs, government and other actors) to implement the just transition; 2) replicating the implementation of the just transition beyond the coal and energy sector and extending it to palm, pulp and paper, social forestry, coastal economic activities and other major commodities; 3) broadening the grantees of just transition projects, including vulnerable and marginalised communities that are often overlooked (women, youth, non-Java regions, grassroots organisations and non-environmental CSOs with widespread membership like Nadathul Ulama, Muhammadiah, Christian, Catholic, Buddhist, Hindu and other religious-based groups).
Indonesia’s commitment to reaching net-zero emissions has been initiated and overseen by the Ministry of Environment and Forestry (MoEF) (referring to Presidential Regulation 16/2015 on KLHK). However, this target has no clear blueprint or common goals across ministries, civil society, government agencies, private actors and the broader public. Moreover, there are contradictory policies, scenarios and responsibilities across ministries. For example, in designing the upcoming carbon pricing regulation (the Presidential Regulation in Carbon Economic Valuation), there is uncertainty between MoEF, MoF, CMMI, the Ministry of Energy and Mineral Resources (MEMR), the Coordinating Ministry of Economics (CME) or the National Planning Agency (Bappenas) on who is leading the process. In addition, NZE has been a top-down target, acknowledged and implemented nationally but has not been rooted in extensive networks of local actors. Therefore, collaboration and data transparency among ministries is highly needed. Broader engagement and more robust coordination in the implementation of the net-zero target are critical to move past partial approaches and sectoral-only perspectives.

Challenge
The implementation of the NZE commitment is slow due to a lack of engagement and coordination, which often leads to inconsistency of actors’ actions and emission measurement mechanisms. First, there is a missing link of key civil society, government and private actors in bringing sub-national and local levels into the regional and national net-zero agenda. Although the net-zero concept has begun to be familiarised on an international and national level, not many people at the local level understand its meaning, nor understand the anthropogenic influence on climate change. Ministerial, provincial and local leaders, as well as the broader public, have different ideas of NZE; hence, the concept needs to be packaged so that everyone, especially at the local level, can understand the target and its urgency. Second, greenhouse gas (GHG) emissions reporting in Indonesia as part of its accountability varies and is not mandatory. This is due to the fact that the country’s regulators have not yet developed a standard, dependable and transparent GHG emissions reporting system. So far, Indonesia has different and uncoordinated GHG emissions reporting systems, created mainly by government ministries and CSOs supported by foreign funding. The existing tools and methods have been developed in sector and project silos. In addition, there is no regulation mandating big emitters from private and state-owned enterprises (SOEs) to report their emissions to government agencies.

Opportunity
Philanthropic organisations can facilitate the engagement and develop a strategy to connect local actors (from the provincial, district and village level) with the regional and national agenda and encourage a bottom-up approach to identify and aggregate local needs for the achievement of net-zero emissions. Pilot projects using a bottom-up approach (in Sintang District, Siak District and Sigi District by Lingkar Temu Kabupaten Lestari or LKTL) have led to positive results [35]. These districts are dedicated to measuring, planning, institutionalising and implementing emission reductions at the local level and these efforts can be replicated in other parts of the country. This has the potential to address at scale the most pressing needs expressed at the local level, notably, food, energy and water.

Philanthropic organisations can support the improvement of capacity and competency for CSOs to better collaborate and mainstream evidence for policy making and community development. Firstly, CSO’s capacity-building programmes are one of the pressing issues related to NZE, as they improve the collection, analysis, communication and delivery of solutions to different audiences (i.e., national government, local government, the public and more specific audiences). More importantly, improved capacity would give CSOs more confidence in their initial role, providing a systematic check and balance mechanism independent of other actors’ influences (government, donor and private actors). CSOs also need to familiarise themselves with the emerging and evolving contexts of climate change,
for example, new discourses on carbon credits and carbon conservation projects. Secondly, CSOs urgently need to collaborate with key partners that have a considerable role in emissions reductions – government, other CSOs, the private sector, universities, law enforcers and the media. These collaborations can encourage actors to take action on climate change and aim to reform institutional arrangements, resolve sectoral fragmentation and build a coalition of willing actors. Collaboration with academic institutions can help communicate complex and critical evidence-based research and solutions in a way that is understandable to audiences from different backgrounds (for example, the government and communities).

Philanthropic organisations can assist the national government in developing agreed, clearer, and more transparent procedures for measuring GHG emissions and removals. The national government needs to support the development of a standard, dependable and transparent GHG accounting and reporting system. This needs to use a scientifically agreed methodology and be able to comprehensively and regularly measure emissions from different sectors. The GHG accounting system needs to be verified by a government agency that is accountable and transparent to the public. The regulation should also mandate big emitters, including private actors, state-owned enterprises (SOEs), jurisdictional governments at the sub-national level and others, to report their emissions.

References

This briefing is based on the findings of the research carried out in the first semester of 2022. The research included literature review and key informant interviews with 29 stakeholders. The stakeholders were classified into a number of categories: nine respondents from national government, eleven respondents from environmental CSOs, six respondents from private-sector actors, and three respondents from funding-organisation actors. The findings are discussed in the paper: “The political economy of Indonesia’s net zero emissions, July 2022”.

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This report presents opportunities for international climate mitigation philanthropy to accelerate the net-zero transition in Indonesia. The priority topics identified are based on analysis undertaken by the authors, their own expert opinion of the national context. While we aim to cover structural and cross-cutting issues drawn on the latest national insights, the report should not be considered an exhaustive list of opportunities. Rather, the report provides an initial overview of potentially impactful interventions. The briefing is the work of the authors and does not necessarily represent the views of Climate Strategies or ClimateWorks Foundation.