

**Credit Opinion: Perusahaan Listrik Negara (P.T.)**

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*Jakarta, Indonesia*

**Ratings**

<b>Category</b>	<b>Moody's Rating</b>
Outlook	Stable
Corporate Family Rating -Dom Curr	Ba3
<b>Majapahit Holding BV</b>	
Outlook	Stable
Bkd Senior Unsecured	Ba3

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**Opinion**

**Company Profile**

PT Perusahaan Listrik Negara (PLN) is the only vertically integrated electricity utility in Indonesia. It is a monopoly operator of transmission and distribution (T&D) networks of over 32,000km and 580,000km respectively. It is the country's largest electricity producer with a generation capacity of over 22,000MW, accounting for 85% of the market. PLN is the sole off-taker for Indonesia's independent power producers (IPPs). In FY2007, revenue was Rp114 trillion. The government - through the Ministry of State-Owned Enterprises (MSOE) - has complete ownership.

**SUMMARY RATING RATIONALE**

The Ba3 combines (1) PLN's underlying credit strength of 13, which maps to Moody's global scale of Ba3; and (2) the high likelihood of support from the Indonesian government in a distress situation, as PLN is 100% owned by the Ministry of State-Owned Enterprises (MSOE).

PLN's standalone credit strength reflects its importance as Indonesia's only vertically integrated electricity utility and expectations of sustainable government support - through subsidies - to ensure its financial viability and operational soundness. Such an expectation is underpinned by its strong links with the government, which is its 100% owner. Furthermore, subsidies to PLN are part of the state budget. As such, Moody's views PLN's rating as closely integrated and strongly linked to the government's credit quality.

While the stand-alone credit quality has incorporated the above factors, it has also taken into account PLN's modest standalone credit metrics, due to the large gap between average sales prices and costs of supply; particularly in light of high fuel expenses as well as major capex requirements - which includes the projected US\$9 billion investments from 2006-2010 under the Fast Track Program to develop 9,000MW coal-fired power generation capacities for the country.

Since PLN is wholly owned by the government, Moody's overlays its underlying credit strength with the joint default analysis for government-related issuers. Moody's assesses the government's willingness to support the company as "high", considering its strategic importance to the economy and status as wholly government owned.

It also takes into account the track record of government support, which includes ongoing subsidies and government loans. The "high" dependence reflects the company's close operating and financial proximity to the government and heavy reliance on government subsidies.

**DETAILED RATING CONSIDERATIONS**

1) PLN's strategic importance as Indonesia's only vertically integrated electric utility and close integration with the government - PLN has a dominant position as Indonesia's only vertically integrated electric utility. The company is strongly positioned as the monopoly operator for T&D and is Indonesia's largest electricity producer with 85% market share. Moody's expects it to maintain its leading competitive position over the medium term, given its long operating track record and high entry barriers. It draws further support from Indonesia's low electrification rate and strong demand growth. PLN is also the holder of the Electricity Authority vested by legislation.

PLN plays an important role in the development of the electricity sector as reflected by government's heavy involvement in its operations and funding, including the provision of subsidies. Under Law No. 19/2003, the subsidy is part of the national budget, accounting for about 5% in 2007.

Its strategic importance is further supported by 100% government ownership through MSOE and there are no plans to divest in the near to medium term. As such, Moody's views PLN's rating as closely integrated and strongly linked to the government's credit quality.

2) Sustainable government support through subsidies to ensure financial viability and operational soundness - Indonesia's electricity market regulatory framework is still undergoing development and considerable change, including its tariffs and subsidy mechanism.

A lack of certainty remains with respect to tariff adjustments. There was a gradual increase from 2000 to 2003 to address the Rupiah's depreciation during the Asian financial crisis. But political concerns over negative social effects have prevented further tariff rises.

Given the limited increase in tariffs, the subsidies, which cover the shortfall between PLN's average electricity sale price and the cost of electricity provision, have become very important. The regulatory environment continues to evolve with respect to the subsidy mechanism, including coverage and disbursement. Subsidy levels have risen sharply in the past few years, mainly as a result of the extension of coverage from low-income households to all customer segments and the removal of the oil-fuel price subsidy for PLN.

Although there is limited track record in the revised subsidy scheme since its implementation in November 2005, Moody's expects sustainable government support through subsidies to ensure PLN's financial viability and operational soundness especially given its strong links with the government, which is its 100% owner. Furthermore, subsidies to PLN are part of the state budget. As such, Moody's views its rating as closely integrated and strongly linked to the government's credit quality.

3) Substantial capex requirements for the Fast Track Program - To reduce the government's subsidy burden and meet rising domestic electricity demand, PLN is mandated by the government through presidential decree No. 71/2006 under the Fast Track Program to develop 9,000MW of coal-fired plants by 2010. The Fast Track Program reduces PLN's reliance on oil by replacing it with coal which is much cheaper and easily available in Indonesia.

Moody's notes the substantial capex requirements for 2006-2010 to develop the Fast Track Program. Total capex is projected at over US\$9 billion, which is expected to be financed 85% by ECA and 15% by bonds. Moody's notes the associated execution risk with regard to the Fast Track Program. But this situation is mitigated by its solid track record and experienced management team.

4) Modest stand-alone credit metrics - Due to continuous financial support in the form of subsidies, the PLN's stand-alone credit quality has incorporated such subsidies, notwithstanding the fact that its pure credit metrics - without any subsidies - are modest due to the huge gap between the average sales prices and cost of supply and its large capex requirements. As such, PLN's stand-alone credit quality of 13 assumes continuous subsidies from the government, and thus reflects the close relationship with the sovereign rating.

## **Other Considerations**

1) Timing gap and fuel cost exposures with regards to the subsidy - There is a timing gap - around 2 months - between monthly submissions of subsidy requests and actual disbursements. But the government is up to date in its disbursements.

PLN is also exposed to fuel cost fluctuations as the monthly subsidy amount is based on the gap between actual revenue and budgeted cost of supply leaving the company exposed to any unexpected spike in fuel cost. However, Moody's notes that Pertamina extended PLN's credit terms for fuel payables when fuel costs were higher than expected thus providing working capital to PLN. In addition, any differences between actual and budgeted cost are compensated quarterly. Furthermore, Parliament reviews the approved subsidies in the middle of each year and makes revisions if those set at the beginning of the year are inadequate.

In August 2007, parliament approved a subsidy of Rp62.4 trillion for 2008. To meet higher-than-anticipated fuel prices, the company expects to receive an increase in subsidy.

2) Inadequate insurance coverage for the T&D network - PLN does not have any insurance coverage for its T&D network. For its generation plants of above 30MW, PLN has adequate insurance coverage against fire, natural

disasters and accidents which cover 100% of the replacement value of such assets insured. However, it does not carry insurance for any business interruptions.

3) Legal subordination - PLN's secured debt as a percentage of total assets will maintain at around 15% level up to 2009 as the proportion of secured ECA loans increases with the implementation of the Fast Track Program. As such, Moody's believes these levels are not material enough to justify a lower bond rating. Moody's will closely monitor PLN's ratio and would reconsider notching if the company fails to meet our expectations within the stated timeframe.

### **Rating Outlook**

The rating outlook is stable, in line with the sovereign outlook.

### **What Could Change the Rating - Up**

Given the close integration of PLN's rating with the sovereign rating, an upgrade in the latter would trigger a rating upgrade of PLN.

### **What Could Change the Rating - Down**

Similarly, a downgrade in the sovereign rating would also trigger a rating downgrade for PLN. Furthermore, a partial privatization of PLN or any government plan to cease subsidy support - a scenario that Moody's considers unlikely in the near to medium term - would impact the support and dependence level and pressure the rating.

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