ASIA PACIFIC BULLETIN
Weekly analysis of breaking issues in Asia Pacific

March 15, 2002

A service of APF Canada exclusively for members of
the Asia Pacific Business Network

Indonesian Bank Sale an Important Milestone in Restructuring

On March 15, the Indonesian government announced the sale of a majority stake in the country's largest retail bank, Bank Central Asia (BCA), to a consortium led by a US asset fund, Farallon Capital Management. Despite the surprise choice – British-based Standard Chartered Bank (StanChart) was the favourite to win -- BCA's privatization has become a litmus test of Jakarta's commitment to economic restructuring in the face of opposition by local politicians and vested interests after nearly two years of repeated delays.

In the current political climate, Jakarta's divestment to a foreign investor is a major achievement, especially after plans to sell cement company Semen Gresik, Indonesia's 10th-largest corporation, to a Mexican consortium were postponed in December due to interference by provincial governments in South Sulawesi and West Sumatra, as well as by competing business interests and nationalists in parliament. Even the announcement of the BCA sale was deferred two days after 4,000 bank employees demonstrated against privatization. With US$10 billion in assets, 800 branches, eight million bank accounts, and the country's largest network of ATM's, BCA is undoubtedly Indonesia's banking sector crown jewel. Once owned by Suharto-era crony Liem Sioe Liong, BCA was rescued from collapse in August 1998 and placed in the hands of the Indonesian Bank Restructuring Agency.

Market analysts widely saw the other short listed candidate, StanChart, as favourite to take over BCA because of its track record in developing countries and long association with Indonesia. In their proposals, both suitors promised not to touch BCA's existing management structure nor to fire any of its 21,000 employees. Ultimately, the sale went to Farallon because its offer included easier sales-and-purchase conditions than StanChart's. This suggests Jakarta is primarily concerned with raising hard cash with the least restrictions possible. At 1,775 rupiah per share for a 51% majority stake, BCA's sale will raise about US$540 million for the state's coffers to help plug the budget deficit. With government debt standing at about US$74 billion, Indonesia needs to raise funds wherever it can. Crucially, international lenders and the IMF placed great emphasis on BCA's divestment as a yardstick of economic reform, threatening to withhold financial aid if it was not completed. The Paris Club of creditor nations meets in April, and Jakarta will be asking them to reschedule US$2.6 billion of debt principal and interest falling due in 2002-03.

Farallon's surprise win leaves unanswered questions as to its strategic fit with BCA, as well as its longer-term intentions in Indonesia's troubled financial sector. The secretive San Francisco-based fund does not have a track record in running financial institutions, though in this case it has hired Deutsche Bank as technical adviser. It knows Indonesia well though, with more than US$1 billion invested there since 1997, including stakes in

Indonesian blue chips such as PT Astra, the largest car manufacturer; PT Indofood, the largest noodle producer; and PT Semen Cibinong, the third-largest cement company.

As a fund specializing in the purchase of under-valued assets, Farallon's intentions with BCA may not be as long-term as StanChart's might have been, meaning there are still questions about the future of BCA. The fund leads a consortium of investors in BCA that includes Mauritius-based Farindo Holdings Ltd., and, significantly, shareholders of PT Djarum, Indonesia's third-largest cigarette manufacturer (itself majority-owned by Budi Hartono, an ethnic Chinese Indonesian tycoon). The terms of the agreement give Farallon an immediate 30% stake in BCA, with a right to buy a further 21% within six months. The danger remains that divestment opponents, including such powerful opposing nationalist voices as Parliamentary Speaker Amien Rais, may still try to derail the full sale despite the contractual obligation. As Semen Gresik unfortunately demonstrated, the Megawati government is not exactly proficient at following through with promises to international investors.