CORPORATE GOVERNANCE OF STATE-OWNED ENTERPRISES:
INVESTMENT HOLDING STRUCTURE OF
GOVERNMENT-LINKED COMPANIES
IN SINGAPORE AND MALAYSIA AND
APPLICABILITY FOR INDONESIAN STATE-OWNED ENTERPRISES

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ABSTRACT

This dissertation attempts to explain the state of Indonesian state-owned enterprises (SOEs) from the perspective of corporate governance and the government’s master plan to improve that situation by setting up holding companies as a governance structure. The experience of Indonesia’s neighbors in Southeast Asia, mainly Singapore and Malaysia, serves as a comparative model for how the government investment holding company becomes a structure for SOE governance.

Agency Theory (Jensen & Meckling, 1976, Eisenhardt, 1989) is the most dominant theory perspective used to analyze corporate governance problems. In the case of SOEs, the difficulty of defining the ultimate principal at SOEs hinders the development of appropriate mechanisms for aligning the agent’s interest with the principal’s. Other theories related to corporate governance are also briefly touched upon, especially in showing the shortcomings of agency theory. For example, one particularly problematic shortcoming is agency theory’s focus on top executives and shareholders.

Explored in this research are the cases of corporate governance at Singapore’s Temasek Holdings (Temasek) and Malaysia’s Khazanah Nasional (Khazanah). They serve as examples of ‘best practice’ in corporate governance conduct for government-linked-companies/GLCs (structures similar in form to SOEs). The New Corporate Governance approach (Hilb, 2004) is taken as a model to determine how well Temasek fits the corporate governance framework which considers both shareholder- and stakeholder-value orientations.

This dissertation employs a qualitative approach, conducting a case study on corporate governance at Temasek to determine its impact on the formation of a holding company for SOEs under the Indonesian Ministry of SOEs. The Malaysian Khazanah provides a holding structure model that can be employed for comparison purposes. Case study is taken as the proposed method mainly because there is little research exploring the use of a holding structure for the governance of SOEs, and the variables and their relationships are not yet known. Therefore, this research has an exploratory nature.
The dissertation also discusses the contextual differences between Singapore, Malaysia, and Indonesia with regard to the political economy of state involvement in managing enterprises. While there is compelling evidence that successful governance of SOEs can be achieved by a holding structure, Indonesian SOEs can draw valuable lessons from its neighbors’ experience only if it also keeps contextual differences in mind. Especially important is Indonesia’s status as an emerging democracy and its impact on political decision making relating to SOEs.

**Key words:** state-owned enterprises, corporate governance, government-linked companies, Southeast Asia, investment holding company
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1 Introduction

The reputation of Indonesia's corporate sector was badly tarnished by the financial crisis of 1997. One of the factors contributing to that loss of reputation has been the sector’s low governance standard, both in the public and the corporate sides of the economy. Companies have been adversely affected by a general perception of poor ethical standards, ratings have been downgraded, share prices have performed weakly, debt restructuring has become protracted, and financing for new projects has become difficult and expensive to obtain. According to a recent survey by McKinsey & Co. (Barton, Coombes & Wong, 2004), over three-quarters of the investors surveyed believe that the quality of governance is at least as important as, if not more important than, financial issues. The same study also reveals that investors in Asia, the US and Europe are willing to pay a premium of up to 25 percent more for well-governed Indonesian companies, which suggests that such well-governed companies are low in number in Indonesia compared to other Asian countries.
If Indonesian companies expand and therefore need new investment to finance growth, as in Indosat’s case, good corporate governance is a matter that will define the company’s value. Corporate governance is not only a risk mitigation approach, but also a strategic means to boost value. Even when such privatization or other ways of acquiring new funding are not on the agenda, corporate governance is still of considerable importance for companies as a monitoring regime. It serves as a way to align the action of the management with the interests of the shareholders.

Relevance of Research
This research attempts to examine the state of corporate governance in Southeast Asia, especially at State-Owned Enterprises (SOE). The rationale behind this is the specificity that the SOEs have in terms of their ownership structure, especially as viewed by Agency Theory, which is the dominant theory perspective for analyzing corporate governance problems. The problems with and case of corporate governance in Indonesian SOEs will be analyzed using theoretical and empirical perspectives. Indonesia is a country whose economy is
under strong pressure to privatize SOEs and enhance efforts at corporate governance improvement, but progress is still lacking.

The benchmark to be explored in this research is Singapore, which represents an example of ‘best practice’ in corporate governance conduct in Asia (IMD, 2003), including at its government-linked-companies (GLCs), the Singaporean equivalent to an SOE. Corporate governance at Temasek Holdings (Temasek), the Singaporean government’s investment arm for GLCs, is discussed in detail as the best practice example of corporate governance at SOEs in Asia. The fact that Temasek’s model of corporate governance for SOEs has an enormous influence over its ASEAN (Association of Southeast Asian Nations) neighboring countries is another factor which underlies the research intention. Malaysia’s Khazanah Nasional, which is the government’s investment holding company and is similar to Singapore’s Temasek, provides evidence of its influence. Another convincing, as well as controversial, piece of evidence is the expansion of Temasek’s investment activities into its ASEAN neighboring countries, in particular Thailand and Indonesia. Its purchase of PT. Indosat and two Indonesian banks, Bank Danamon and Bank Internasional Indonesia, in 2003, followed by
the recent takeover of Shin Corp from the Shinawatra family in Thailand, emphasizes its superior role in the region. As controversial as Temasek’s venture might be, it is evidence of how SOEs, or, in this case, government-linked investment companies (GLICs), can not only perform economically profitably but can also be a strong investment powerhouse. Good corporate governance, as suggested by Temasek’s ranking and the awards it has received for its corporate governance, is unarguably one of the key factors in its development.

It is therefore logical to consider whether such a model of the investment holding arm is also applicable as a corporate governance structure for other Southeast Asian countries’ state-owned enterprises. Malaysia’s Khazanah Nasional will serve as one example where this has been done, while the case of Indonesia having a master plan to build a national holding company for its SOEs is the main research object.

However, there is no ‘one-size-fits-all’ solution to problems, including those in corporate governance. Differences in each country’s political, legal and cultural systems need to be taken into account when transferring a set of systems from one context to another. Hence, this research will contribute to the understanding of
the differences which one should consider when applying one corporate governance model to another context.

**Research Objectives and Focus**

The objectives of this research are:

1. To examine corporate governance at the investment holding arm of Southeast Asian GLCs (represented by Singapore’s Temasek and Malaysia’s Khazanah) and identify the factors that contribute to the performance of those GLCs;

2. To identify the problems involved in the corporate governance of Indonesian SOEs and the policy measures which have been planned and taken to overcome them;

3. To analyze whether the model of the investment holding arm will be suitable to improve the corporate governance of Indonesian SOEs;

4. To identify contextual differences between Singapore, Malaysia and Indonesia which could make the application of such a holding structure in Indonesia work differently;
5. To summarize the lessons learned from the experience of Singapore and Malaysia in managing their GLCs under the holding structure, which Indonesia needs to take into account in implementing its master plan for building an SOE holding structure.

The current picture of the corporate governance situation in Southeast Asia shows that Singapore, as the region’s business-hub, has better performance in corporate governance (Wu, 2005), despite most of its companies being GLCs. The CLSA Corporate Governance Rating in Southeast Asia (CLSA, 2001), for example, ranks Singapore highest in 5 of the 7 aspects measured, namely, in discipline, transparency, independence, responsibility, and fairness, compared to the other ‘ASEAN –5’ countries (Indonesia, Malaysia, Philippines and Thailand).

At the other extreme, Indonesia is last in the same ranking for 5 of the 7 aspects on corporate governance. The BUMNs (Badan Usaha Milik Negara, the Indonesian term for State-Owned Enterprises) are also notorious for being inefficient, rampant with corruption and being uncompetitive in the market. It is for this reason that the critical issue to be touched upon is SOE corporate governance in
Indonesia. Singapore’s model of corporate governance is presented as the best-practice model, while Malaysia, which is culturally similar to Singapore and Indonesia, is used for comparison purposes. Differences must, however, also be taken into account. Given the fact that it follows a logic similar to Temasek’s, Malaysia’s Khazanah Nasional model serves as the comparative object for Singapore’s model. At the same time, the dissertation at hand will examine how this model has been influential in its ASEAN neighboring country, Indonesia, with respect to its master plan to build holding companies for its SOEs.

**Research Gaps**

It is imperative to highlight two events when the theme of corporate governance is brought up in discussions. In the global context, the first major event was the fall of Enron and other global giants, due to improper, dishonest, non-transparent business practices, and the subsequent loss of global public trust in financial institutions. Specifically in the Asian context, it was the financial crisis in the late 1990s, which prompted most of the affected countries to make improved corporate governance a priority. Various scholars have
pointed to poor corporate governance as a key factor in the Asian financial crisis, especially in the case of Indonesia, where relationship-based business culture is taken for granted as having contributed to the economic woes of 1997-1998 (Van Der Eng, 2004). Countries such as Thailand, Indonesia and, to a lesser extent, South Korea and Malaysia, which have consistently been viewed as having difficulties in implementing good corporate governance concepts, were the ones most adversely affected, while countries such as Singapore, Hong Kong, and Australia, known for their better corporate governance standards, appear to have fared better and were the least affected by the crisis. Unfortunately, there has not been much work published on Indonesian corporate governance. Among the few works are Tabalujan (2002), Simanjuntak (2001 and 2005), Kurniawan & Indriantoro (2000), Sato (2004a and 2004b), none of which focus on Indonesian SOEs. This research gap is to be filled by this dissertation.

Moreover, another perspective on examining the lack of sound corporate governance practice in Indonesia is the absence of a ‘legal culture’ (Friedman, 1969, Tabalujan, 2002) grounding the behavior of Indonesian actors in the corporate world. The major problem with
analyzing the corporate governance situation at SOEs based on agency theory arises from the complex situation of ownership that SOEs have. The difficulty in defining who the principal is at SOEs hinders the development of an appropriate mechanism for aligning the agent’s interest with the principal’s. This is especially so when viewed from the agency theory perspective, where the definition of the State as the ‘principal’ is difficult to determine, and who should act in the interest of this principal to conduct the monitoring regime at an SOE is also unclear. There has not been much research on corporate governance for SOEs, especially with respect to works addressing the problem of ‘state as principal’. Attempting to examine the investment holding arm to enhance shareholder value orientation, this research aims at exploring the way to address this ‘state as principal’ problem.

Structure of Dissertation
This dissertation is structured as follows:

1. Introduction

   This chapter discusses the relevance of the research for practical decision making in business. It outlines the research objectives
and focus of the dissertation and identifies research gaps in the topic. It is concludes with an outline of the structure of the dissertation.

2. Literature Review and Theoretical Foundations

This chapter sets the theoretical foundations of the topic by reviewing literature on corporate governance. It deals with various definitions and important theories on corporate governance. Rounding out the chapter are the approach of New Corporate Governance (Hilb, 2004) and the three pillars of SOEs governance reform (Wong, 2004) as key concepts in this research.

3. Research Questions and Methodology

This chapter outlines the research questions to be answered by this research. It also explains the use of a case study as a qualitative methodology and elaborates further the data collection methods.

4. Situational Corporate Governance of State-Owned Enterprises in Southeast Asia

In relation to Southeast Asia, important aspects to be considered are the institutional context, national culture context and
normative context. In the case of SOEs, ownership structure and behaviour as well as board power-structure and board behaviour are important factors to be examined. This chapter explains the New Corporate Governance approach, especially Situational Corporate Governance, which is based on the reversed KISS principle, in SOEs in Southeast Asia.

5. Temasek Holdings: the Singaporean Government Investment Holding Company

This chapter discusses Temasek Holdings as the Singaporean government’s investment holding company and examines how it fits the New Corporate Governance framework. All four aspects of the reversed KISS principle, situational, strategic, integrated and controlled, are used as tools to analyze Temasek’s corporate governance practices. The impact of Temasek Holdings on how other countries manage their SOEs ‘under one roof’ is also discussed in this chapter. It is important to examine the specific context of Singapore, with its transformation from a ‘developmental state’ to ‘developing the external wing of the economy’. Finally, a discussion of board structure as the measure of corporate governance practice highlights the issues
of diversity and transparency as a consequence of Temasek’s global venture.

6. Khazanah Nasional Berhad: Revamping GLCs as Malaysia’s Nation-Building Project

The section on Khazanah as the Malaysian government’s investment holding company begins with an explanation of the basic principle of separation between the government’s various roles in economic management. Later follows the story of the GLC Transformation Program and how it fits the New Economic Policy and Ninth Malaysia Plan as the country’s fundamental economic policy. Finally, an analysis of the board structure as a measure of corporate governance practice discusses the strong presence of the government in the GLC Transformation Program.

7. Corporate Governance of Indonesian SOEs: Building an SOE Holding Company in the Direction of Indonesia Inc.

This chapter starts with the existing problems of corporate governance at Indonesian SOEs. Furthermore, contemporary issues on the corporate governance of Indonesian SOEs are elaborated. The chronological development at the Indonesian
Ministry of SOEs related to leadership changes amid political democratization in Indonesia is an important factor. The three-step strategy of restructuring, ‘profitization’ and privatization of Indonesian SOEs is also a historically important milestone which one needs to examine closely from time to time. Finally, the heart of the chapter focuses on specific benchmarks in key sectors of Indonesian SOEs leading to the master plan of Indonesian SOEs to build a Temasek-style holding company.

8. Corporate Governance and Holding Structure for SOEs as a Global Trend

In order to demonstrate the significance of this model, the chapter portrays the ongoing trend in SOE governance toward building a holding structure elsewhere in the world.


This chapter centers on the phenomena of globalization and democratization pressuring contemporary Indonesia. They have given rise to the greater corporate governance challenge of juggling shareholder value and stakeholder interest, two values which do not always go hand in hand. The issue of a state’s
sovereign wealth funds as strategic investors and reactions to their expansionist behavior based on economic nationalist sentiment showcases the political economy dimension of this problem. It has led to the massive task of managing the impact of economic nationalism on Indonesia’s quest to build holding companies for its SOEs. The fact that Indonesia is now experiencing democracy under the presidency of Susilo Bambang Yudhoyono, Indonesia’s first directly elected president, provides both a challenge and an opportunity in managing Indonesian SOEs.

10. Conclusion

This chapter concludes the dissertation with a discussion of the way forward with respect to the governance of Indonesian SOEs and key issues which need to be taken into account.
2 Literature Review and Theoretical Foundations

2.1 Corporate Governance Definitions

Numerous definitions of what corporate governance is have been developed by both academicians and practitioners. One of the definitions is: Corporate governance is the system by which business corporations are directed and controlled. The corporate governance structure specifies the distribution of rights and responsibilities among different participants in the corporation, such as the board, managers, shareholders and other stakeholders, and spells out the rules and procedures for making decisions on corporate affairs. By doing so, it also provides the structure through which the company objectives and the means of attaining those objectives and monitoring performance are set (OECD, April 1999).1

Another definition by the ICC (International Chamber of Commerce)2 states that: Corporate governance is the relationship

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between corporate managers, directors and the providers of equity, people and institutions who save and invest their capital to earn a return. It ensures that the Board of Directors is accountable for the pursuit of corporate objectives and that the corporation itself conforms to the law and regulations.

The OECD's definition is in line with the simplest yet most frequently quoted definition of Corporate Governance by Sir Adrian Cadbury, the father of the core of the UK Combined Code on corporate governance, which regulates corporate governance in UK companies. Cadbury defines corporate governance as the system by which business corporations are directed and controlled (Cadbury, 1992).

It is important to note that the numerous definitions of corporate governance have a tendency toward either one of the two orientations in businesses: shareholder value and stakeholder value. A definition such as: Corporate governance deals with the ways in which suppliers of finance to corporations assure themselves of getting a return on their investment (Vishny/Shleifer, 1997) is strongly influenced by the shareholder-value perspective, while, on the other hand, the definition of corporate governance as “… the
systems of laws, rules, and factors that control operations at a company. …. Set of structures, which include participants, such as managers, workers, suppliers of capital...“(Gillian & Starks, 2003) is clearly a stakeholder-value-oriented construct.

If one considers the dominance of the US economy and financial markets, a dominance compounded by weaknesses in other governance systems, the Asian financial crisis, and Japan’s continuing poor economic performance over the last 15 years, then we can expect that the Anglo-American model of corporate governance, with its strong orientation toward shareholder-value, should or will be the final destination in the evolution of national corporate governance systems. If so, then the ‘end of history’ for corporate governance may already be in sight (Tabalujan, 2002).

On the other hand, the classic Anglo-American model has focused almost exclusively on shareholder value, where profit is the only target in corporate governance as quality of governance. Transparency and accountability are of no meaning or counterproductive to the profit of the largest shareholders in power. Thus, the choice of corporate governance includes openness to other stakeholders. The model of ‘enlightened shareholder’ value or the
pluralistic, stakeholder model can embrace this concept (Gupta, Pike, Roos & Burgman, 2003).

**Corporate Governance: Important Theories**

**Agency Theory**

Agency theory explains how best to organize relationships in which one party (principal) determines the work which another party (agent) undertakes (Eisenhardt, 1985). The theory argues that under conditions of incomplete information and uncertainty, a situation characterizing most business settings, two agency problems arise: adverse selection and moral hazard. Adverse selection is the condition under which the principal cannot ascertain whether the agent has accurately represented his ability to do the work for which he is being paid. Moral hazard is the condition under which the principal cannot be sure whether the agent has put forth maximal effort (Eisenhardt, 1989).

In its narrow sense, corporate governance is, in fact, centered on the agency problems that arise from the separation of management and ownership (Simanjuntak, 2001). It is the reason why agency theory is important for corporate governance studies. Agency theory argues that in the modern corporation, in which share ownership is widely
held, managerial actions depart from those required to maximize shareholder returns (Berle and Means, 1932). Although the ideas of agency theory (Jensen & Meckling, 1976) can be attributed to Ronald Coase, the American economist from the 1930s, it has only been applied to directors and boards since the 1980s. Inherently, this theoretical view is based on the belief that people are more self interested than altruistic and cannot be trusted to act in the best interest of others, but rather, maximize their own utility (Coase, 1937). Agency theory presents the relationship between directors and stakeholders (including shareholders) as a contract. Thus, the directors, acting as agents of the stakeholders, will make decisions in their own interest and hence be subject to transaction costs for the checks and balances necessary to reduce non-compliance over enforcement costs.

Agency theory deals with the structure of ownership of a firm, how the owner’s interests in the firm are managed by executives at the firm and how the mechanisms of aligning the interest of the owner with those of executives are developed. It also deals with controlling the mechanisms so that they do actually work and prevent acts which are clearly not in line with the principal’s interests, such as fraud or
shirking on the part of the agent. This is translated into the forms of the organization of the board structure, rules on strategy-setting and strategic decision-making processes, reporting and controlling mechanisms, and the management of risk as an inseparable element of business. In addition, it includes the issues of selection and remuneration, which also serve as a means to control the behavior of the agent to be in line with the principal’s interests, thus lowering the likelihood of adverse selection and moral hazard.

![Figure 2.1 Principal-Agent Relationship According to Agency Theory (own depiction, based on the literature)](image)

**Figure 2.1 Principal-Agent Relationship According to Agency Theory (own depiction, based on the literature)**

Agency Theory is often criticized as being one-sided in its view of corporate governance. It only considers the perspectives of the top executives and neglects the entitlement of employees, customers and the environment. Therefore, other theories such as Stewardship Theory, Stakeholder Theory, Resource Dependence Theory and
Institutional Theory also need to be taken into account in analyzing corporate governance situations.

**Stewardship Theory**
Scholars have recently been critical of the agency perspective in CG studies (Hoskission et al. 2000; Blair 1995; Perrow 1986), largely because of its limited ability to explain the sociological and psychological mechanisms inherent in the principal-agent relationship. An alternative managerial motivation view to agency theory may be termed stewardship theory (Donaldson 1990; Barney 1990). The underlying assumption of stewardship theory is that managers are good stewards of firms. Under this theory, the classical idea of corporate governance is that the managers, on behalf of the shareholders, essentially want to do a good job, i.e., to be good stewards of the corporate assets, not to have conflicts of interest or make secret profit at the expense of the shareholders. The power of the firm is exercised by the directors, who are appointed by, and are accountable to, the members at a general meeting. An independent auditor produces a report to members to show that the firm’s accounts and financial statements are true and fair. This theory
remains the theoretical foundation for much regulation and legislation (Adams, 2002).

Stewardship theory thus focuses on developing mutual trust and cooperation between principal and steward. Indeed, stewardship theory proposes that trustworthy and cooperative relationships between principals and stewards are positively correlated with firm performance (Tian and Lau, 2001). This has several important implications for management control systems, especially with regard to effective information-sharing mechanisms to address the information asymmetry problems highlighted in agency theory as one of the agency problems.

The main differences between agency theory and stewardship theory are in the following aspects. First, the underlying assumption of agency theory is that managers will behave rationally, opportunistically and self-servingly, while stewardship theory assumes or, rather, believes that these managers are trustworthy and cooperative. Second, it leads to different implications from those of agency theory, which emphasizes monitoring and control, instead of relying on trust and relationship-building between principal and steward. Third, the focus of agency theory is on the independence of
different groups (for example, board members, monitoring committee and management), which might lead to ‘goal conflict’, while stewardship theory focuses on understanding and identification between them to achieve ‘goal alignment’. Table 2.1 summarizes the contrast of the two theories’ views on corporate governance.

Some scholars would go so far as to argue that stewardship theory fits better than agency theory in certain contexts, for example, in transitional economies (Van Thang, 2005). In Southeast Asia, Vietnam, with a very different economic, institutional and social environment from those of developed countries, is an evident case of this context, where assumptions of agency theory need to be carefully reviewed (Phan 2001). However, to what extent this also applies to Indonesia is still arguable given the country’s state of rampant corruption, which suggests that, indeed, agency theory’s assumption of human opportunistic and self-interested behavior fits better.
Table 2-1 Contrasting Perspectives on Corporate Governance
(Van Thang, 2005 based on existing literature)

<table>
<thead>
<tr>
<th>Assumption of human behavior</th>
<th>Agency Theory</th>
<th>Stewardship Theory</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agents are opportunistic and self-serving</td>
<td>Trustworthy and work for the benefit of the corporation</td>
<td></td>
</tr>
</tbody>
</table>

| Primary role of Supervisory Board | Board members are to control and monitor managers | Board members provide managers with resources, expertise, network and power |

**Stakeholder Theory**

Stakeholder theory emerged during the 1970s to reflect the fear at a societal level that large multinational corporations had become too powerful to be held accountable solely to shareholders (Freeman, 1997). The theory argues that there are business interdependencies with other elements of society. The corporation is an institution engaged in mobilizing resources for productive uses in order to create wealth for the benefit of its multiple stakeholders. Stakeholders are all residual risk holders; they have something at risk. Thus, the unit of analysis in a stakeholder view is the firm embedded in a stakeholder network. High performance implies the adequate creation of benefits and minimum adverse effects for all stakeholder interests involved. This theory had been, however, left to
gather dust until the more recent environmental issues of the 1990s
started to produce greater social awareness and trends toward ‘triple
county line’ reporting.

Nevertheless, recent heated arguments over corporate governance
show a trend toward moving away from the traditional concept of
shareholder value towards the broader concept of the stakeholder
society (Sato, 2004). Managerial decisions do affect investors, but
also exert externalities on various other stakeholders of the firm,
such as employees, customers, suppliers, communities where the
firm is located, potential pollution, and so forth. From the
stakeholder-society perspective, corporate governance is the design
of institutions that induce or force management to internalize the
welfare of stakeholders, and a governance system is “the complex set
of conditions that shape the outcome of the ex post bargaining over
the quasi-rents that are generated in the course of a relationship”
(Tirole 2001).

As will be shown later, the importance of stakeholder theory for the
corporate governance of SOEs is emphasized by the fact that SOE s
have a more complex set of stakeholders since they are usually also
subject to social goals along with their profit-making objectives as a
firm. The importance of stakeholder theory in the context of corporate governance is also undisputed; the institutionalist approach, described in the following section, could only have arisen after recognition that corporate governance deals with the structure of rights and responsibilities among the parties with a stake in the firm.

**Institutional Theory**
Having mentioned institutional differences as a factor that can differentiate how an assumption in one context can lead to a different implication in another, it is also important to mention another theoretical perspective, institutional theory. Aoki (2001) attempts to approach corporate governance by employing more diverse social and cultural institutional factors. For institutionalists, corporate governance concerns “the structure of rights and responsibilities among the parties with a stake in the firm” (Aoki, 2000: 11). From the viewpoint of comparative institutional analysis employing game theory, corporate governance is seen as “self-enforcing mechanisms that govern (such) strategic interactions among the players” and is defined as “a set of self-enforceable rules (formal or informal) that regulates the contingent action choices of the stakeholders (investors,
workers, and managers) in the corporate organization domain” (Aoki 2001, p. 281).

Rather than using the framework of neoclassical economics, this new institutional economics (NIE) approach uses perspective and methodology from the newly developed framework of comparative institutional analysis. Comparative institutional analysis strives to discover the source of economic gains from diversity and the circumstances under which they are realized, using the universal analytical tools commonly employed in the field of economics and shared by economists worldwide. In this sense, comparative institutional analysis leans toward an economics of pluralism. Based on this approach, the existence of different types of corporate governance structures is necessary to provide important theoretical frameworks to examine the evolution of different corporate governance structures (Aoki, 2003). It can explain why some organizational architecture can become a convention in one economy but not in others. This could serve as an important basis for the comparison of the governance structure model of Indonesian SOEs and Singapore’s Temasek Holdings.
An approach which emerged from institutional theory is “actor-centered institutionalism” (Aguilera & Jackson, 2003), which explains firm-level corporate governance practices in terms of institutional factors that shape how actors’ interests are defined (socially constructed) and represented. This view also criticizes or, rather, complements agency theory, especially in the latter’s failure to account for key differences across countries. Agency theory is considered to have ‘an undersocialized view’ of corporate governance, while institutional theory itself tends to be ‘oversocialized’. Actor-centered institutionalism bridges the gap between them (Aguilera & Jackson, 2003).

Aguilera and Jackson describe corporate governance and the institutional domains shaping it as having three dimensions – management, capital and labor – depicted in the diagrams below.
Figure 2.2 Dimensions of Corporate Governance (Aguilera & Jackson, 2003)

Figure 2.3 Institutional Domains Shaping Corporate Governance (Aguilera & Jackson, 2003)
Aguilera and Jackson’s approach enriches and complements the view on corporate governance provided by agency theory. While agency theory suggests that the impact of internationalization is the convergence of corporate governance best practice into the “Anglo-American model”, institutional theory suggests that countries will continue to diverge along stable, path-dependent trajectories. It is true that, due to institutional factors in the development of property rights within common law and civil law traditions (La Porta et al., 1999) and financial systems which differ across counties, the Anglo-American model has been more widespread among countries than, for example, the ‘Rhineland’ model of Germany and Japan. However, a hybridization of the corporate governance model where practices developed in one national setting are transferred to another and undergo adaptation through recombination with other governance practices eventually prevailed (Pieterse, 1994). This is certainly a very useful contribution to the context of this research on examining whether the investment holding arm model of Singapore and Malaysia can be applied in the context of Indonesia and whether it should possibly undergo modification.
The institutionalist framework goes beyond the confrontation of shareholder-value and stakeholder-society perspectives and provides a broader scope of comparative (not normative) analysis on governance mechanisms, connecting the domain of corporate organizations with other domains of financial transactions, labor transactions, political regimes, and so forth (Sato, 2004) This makes the framework very useful in analyzing the state of governance at SOEs.

Organizational, Resource-dependence and Resource-based Theory
Many organizational theorists have demonstrated that the peak of the organization is the CEO and few went further to show the role of the Board of Directors as the peak structure. Recently, corporate governance has benefited from contributions from the psychology of behavioral science and the sociology of organizational management work (Cyert, March and Simon, 1963).

Resource-dependence theory is a predecessor of resource-based theory, and this perspective states that when there are elements in the environment that exert power over an organization, it will strive to secure a friendlier environment or more independence (Pfeffer,
1972). Resource-based theory (RBT) examines the link between a firm’s internal characteristics and performance (Penrose, 1959; Barney et al. (2001); Wernerfelt, 1984). Barney et al. (2001) investigate the linkages between RBT and corporate governance and find that several contributors to this issue identify such links. For example, Castanias and Helfat (2001) emphasize the importance of human capital arguments vis-à-vis more traditional agency theory arguments concerning corporate governance. Mahoney (2001) argues that the recognition of the problem of opportunism has important corporate governance implications. Lockett and Thompson (2001) discuss the links between RBT and agency theory. Wright et al. (2001) suggest that mismanagement may mean that human capital is not deployed effectively.

The Public as Principal and New Public Management
The analysis of corporate governance problems at state-owned enterprises will use the perspective of agency theory in perceiving SOEs in the context of principal-agent relationships. There has been analysis of the role of the `public` as principal, where looking at government as a principal requires clarification of the objectives that the government is pursuing (Lane, 2003). A principal has certain
interests that he/she wishes to pursue. We must carefully examine what the objectives of a public principal are. A principal is a person who instructs an agent to act on his behalf against remuneration. Government becomes a principal when it hires people to do the job for it. The people hired by the government to get the job done function as agents of the government. The government may rely upon different kinds of agents working under various institutional arrangements with differing consequences.

A public principal targets social objectives that need to be provided to a group or community of people. The basic insight is that government as a public principal has incentives linked with social objectives. The state as an owner can aim at different interests than the same state in its role as performance contractor. The real challenge is to find the right balance between political influence and management’s capacity to act (Schedler in Noetzli, 2004). This is just to illustrate the complexity of the state as principal, which already has to fulfill two differing objectives.

The situation becomes more complicated when social objectives such as affluence, human development, education, and social care are mixed with private incentives such as money, prestige, and power,
since government officials are individuals too with natural needs for those incentives. This is where the greatest dilemma in public-as-principal starts, that is, the mixing of social and private incentives in the public sector (Lane, 2003).

Selfish motives such as private incentives surely play a major role with agents in the public sector (politicians, bureaucrats, professionals), although these agents actually should provide that their outputs accomplish social objectives. Social objectives refer to the incentives of the public principal and are mostly intangible, such as the well being of the nation, economic growth, prosperity, peace, community development. The government as public principal sets priorities among these different social objectives as output. Although the public principal may be driven by mainly selfish motives such as economic gain and power or prestige, the public principal should choose between alternative social objectives as output to be achieved.

However, in reality, it is difficult to ensure that the achievement of these social objectives will be placed ahead of the fulfillment of private incentives. While the public principal should be an institution aiming to achieve these social objectives, the elements of the public
principal are individuals with a strong tendency to act on private motives. There has also been little explanation of the incentives for the public agent to ensure that these social objectives be fulfilled.

New Public Management has recently become common in discussions of Best Practice in management of the public sector, also referred to as ‘public governance’, though not all SOEs are in an area that can be categorized as the public sector. The terms ‘new public management’ (NPM) and ‘managerialism’ are commonplace in the public management literature (Hood, 1991; Osborne and Gaebler 1992; Hughes, 1998) describing the adoption of a private sector management model which emphasizes the accountability of managers and is results-oriented.

This is again another counter-analysis to agency theory, which focuses mainly on extrinsic motivation and neglects intrinsic motivation. It is an area where corporate governance can actually learn from public governance. The discussion on public governance considers intrinsic motivation as having a primary role, such as employee involvement and participation at the board of director’s level, orientation of management activities to various stakeholders,
clear separation of executive and normative functions, as well as the appointment of titles as a form of recognition (Frey, 2003). It is therefore important to differentiate corporate governance approaches from the various contextual factors it might have. A new approach to corporate governance which greatly emphasizes the situational elements of the firm as one of its main dimensions is elaborated in the following section.

**New Corporate Governance**
The analysis in this research work is based on the approach of New Corporate Governance, where principles of good corporate governance applied in a firm should be kept situational, strategic, integrated and controlled (Hilb, 2004). A new approach to corporate governance which believes in a balance in both value-orientations is emerging and in fact becoming more common. According to the definition of New Corporate Governance (Hilb, 2004), it is a system "by which companies are strategically directed, integrative managed and holistically controlled in an entrepreneurial and ethical way in accordance with a particular context". This definition attempts to cover both the value-orientation of the shareholder and stakeholder
perspective. This integrated approach of corporate governance will be paramount in examining the empirical case of Singapore’s Temasek Holdings corporate governance practice. Integrated corporate governance sets itself apart from other corporate governance approaches through the four dimensions related to keeping corporate governance situational, strategic, integrated and controlled and has been dubbed the reversed-KISS principle. The New Corporate Governance framework is presented in Figure 1 as a holistic framework for the direction and control of enterprises that seeks to integrate the formerly isolated elements of corporate governance in research, teaching and practice.

Figure 2.4 The New Corporate Governance framework (Hilb, 2004)
It is especially important that the framework incorporates both the orientation of Shareholder-Value, mostly used in Anglo-American firms, and Stakeholder–Value, which has a strong presence in German and Japanese firms. The integrated ‘glocal’ model (Hilb, 2004) is depicted in Figure 2.5.

**Board Performance**

![Figure 2.5 Corporate Governance Approaches (Hilb, 2004)](image)

Highlighting the New Corporate Governance framework for the purpose of this research is especially important for the analysis of Temasek Holdings' corporate governance model. This model applies the principles of keeping corporate governance situational, i.e., with
regard to Temasek’s status as the holding of government-linked companies, and strategic, where both shareholders and stakeholders are given a place in its determination of success and accountability.

**Three Pillars of SOE Governance Reform**

From the agency theory perspective, the key difference in the corporate governance of SOEs is its characteristic of having the state as the owner. The poor performance of many SOEs can be attributed to the three main challenges facing SOE governance in comparison to private sector enterprises (Wong, 2004). The following diagram describes the differences between public sector governance and governance of private sector enterprises and the challenges for reform.

![Diagram showing the three pillars of SOE governance reform](image)

**Figure 2.6 Three Pillars of SOE Reform (Wong, 2004)**
This unique governance situation poses challenges that make the path to SOE governance reform more difficult; however, reform is necessary in order to improve the poor performance of SOEs in comparison to their counterparts in the same industry. No government yet has been able to fully tackle the problems. Privatization has been employed as a means to solve this problem, however, only in some cases can privatization bring about the expected results, especially when political resistance is high or the SOE to be privatized is not attractive to investors because of the company’s extreme mismanagement. Thus, corporate governance reform is a viable option if SOEs are to be profitable and efficient or at least in the same standard as their private firm counterparts in the same industry.

Corporate governance reform must tackle all three issues in an integrated manner; otherwise, the results would be disappointing. This reform should only address SOEs operating in a purely commercial manner (with singular focus on value maximization) or SOEs that are commercially viable and operate in a way that is largely commercial and social in nature. In other words, when the costs of any non-commercial objectives are removed, SOEs should
be able to recover their own cost of capital. Otherwise, it would not be viable to improve them; rather, closing them down or selling them off would be a better option.

The problems facing Indonesian SOEs will be elaborated in this thesis. The integrated reform packages suggested by Wong (2004) in handling these problems comprise clear directions, insulation from political interference, and transparency improvement. Mainly, the work at hand will examine whether the investment holding structure as practiced by Temasek and Khazanah help in supporting the above SOE reform package in the three aspects discussed.

The main objective of the research is to provide greater insight into the different contexts that Singapore and Malaysia face in their efforts to build a holding company to manage their state assets, so as to provide the Indonesian government with a comparative study of its own master plan and the challenges it will face.
Research Questions and Methodology

Research Questions
Agency theory perception of state-owned enterprises has been very pessimistic, especially with regard to conflicting interests that will arise in monitoring and controlling by government institutions. This is especially true in the case of Indonesia, which has led to a situation where privatization might be the best way to ensure that the governance of these enterprises is properly conducted (Duncan and McLeod, 2007). Privatization measures taken in the past few years have, however, drawn criticism from the public, especially in cases where the SOEs are sold to foreign investors. Both nationalistic sentiments and the view that the performance of these SOEs can actually be improved without having to be sold are behind these criticisms (Prasetiantono, 2004). Temasek Holdings is one of the foreign investors caught in the crossfire.

Ironically, the analysis of Temasek Holdings' corporate governance shows that being the holding of Singapore government-linked companies does not necessarily prevent it from practicing good

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3 Interview with Prof. Dr. Djisman Simanjuntak (Indonesian corporate governance expert) on 13 December 2006 also confirmed that for the context of Indonesian SOEs.
corporate governance. In fact, as evidence of their good practices, the TLCs have won several awards as well as recognition in Singapore for their corporate governance. The value created by Temasek for its shareholders is also a result of its focus on sound corporate governance as one of its most important pillars.

It poses several questions for research on Indonesian SOEs and its comparison with Singapore’s Temasek Holdings with regard to corporate governance as a key pillar for performance improvement. Based on Wong’s (2004) approach to SOE governance reform, which addresses the issues of conflicting objectives, political intervention and lack of transparency, the thesis examines how the holding structure can help in addressing those three issues in the context of Indonesian SOEs governance.

The key questions are:

1. What are the advantages of the holding structure in terms of measures toward key SOE governance reform?

2. Does the holding structure really serve as a means to avoid conflicting objectives, minimize political interference and improve transparency in the governance of GLCs and SOEs?
3. Can Indonesian SOEs also be managed under the structure of a private investment holding with the government as its major shareholder, instead of under the Ministry of SOEs as a bureaucratic government body?

4. What are the similarities of the Indonesian context of state-owned enterprises in comparison to Singapore and Malaysia which might serve as compelling factors to apply such structures in Indonesia?

5. What are the major contextual differences between these Southeast Asian countries which might hinder the application of such an investment holding?

6. What are the lessons to be learned for Indonesian SOEs from the case of holding structures in Singapore and Malaysia?

It is expected that this research will contribute to a better understanding of the key success factors in managing SOEs within the ASEAN region, which will then provide guidelines for Indonesian SOEs, the government as well as the management community regarding a better way to improve corporate governance practices at SOEs.
It might be ironic for Indonesia that Temasek Holdings, due to its aggressive acquisitions and share-buying tactics with respect to certain Indonesian companies, is the company whose name has generated so much controversy in discussions of the privatization of SOEs in the wake of liberalization. Nevertheless, we have to put aside pro and contra on privatization in Indonesia. An objective view will put Temasek Holdings as example of corporate governance best practice based on the recognition it has gained and the value it has created. This is a result of having corporate governance as one of its pillars.

**Case Study as Methodology for Qualitative Research**

Based on the type of research questions, there are about six directions that scientific research can take: descriptive, explorative, evaluative, predictive, explanatory and control. The above-mentioned research questions belong to the explorative type. Especially given that research examining the use of the holding company structure for state-owned enterprises has not been found, it is logical that this research is exploratory in nature. Many variables are not known in regard to the success of Temasek Holdings in
corporate governance practice, especially in relationship to the structure of holding company that it has.

A literature review reveals that management research has been using case study as one of the most frequently applied methodologies, especially when the number of variables of interest far outstrips the number of data points (Yin, 1994). Case study is also considered to be an appropriate tool in the early development of a management theory when key variables and their relationships have yet to be established (Yin, 1994, Eisenhardt, 1989b).

This situation also exists in the case of a comparison between Temasek Holdings, Khazanah Nasional, and Indonesian SOEs, where the number of variables which might lead to better governance practices in the case of the holding structure is not yet known and might be quite high. The author therefore applied the case study method for this research by conducting a field study in Singapore, Malaysia and Indonesia, although this might not be the ideal multiple-case study. Yin (1994) suggested that a multiple-case study should be best designed around the same replication logic that underlies the design of same multiple specific experiments. Eisenhardt (1989b) also suggested that cross-case analysis involving
four to ten case studies may provide a good basis for analytical
generalization.

However, when the goal is to find the success factors of the holding
company model and see the applicability for the context of
Indonesia, it might be an adequate approach. Additional or further
comparisons can also be drawn when there are other countries in the
Asian context, such as Vietnam and China, whose governments have
established or about to establish an investment arm. Such
comparisons will strengthen the results of this case study when it is
conducted by following the same logic.

The case study method consists of a mixture of the following various
qualitative techniques (Ruigrok, Gibbert, Kaes, 2004; Yin, 1998):

- Documentation and archival study
- Interview
- Questionnaires
- Direct observations and participant observation

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4 The situation in China and Vietnam as transition economies with lower
degrees of political openness in managing their SOEs under holding
structure is indeed briefly discussed later, to gain comparison with the
situation in Indonesia having experienced rapid democratization in the last
decade.
- Physical artefacts (ethnographical or anthropological features)

The case studies on GLICs in Singapore and Malaysian and the Indonesian Ministry of SOEs, together with several companies under the ministry, relied on open semi-structured interviews, document-based study and, in most cases, press article analysis.

A longer encounter and more in-depth relationship with the object are required to apply observation techniques, while interviews and document study require shorter periods of time, as long as the right information and right person to be interviewed can be accessed.

Several critical points that the author must consider while doing case study research in this area are the construct validity, internal validity, external validity and reliability of the case study method (Ruigrok, Gibbert, Kaes, 2004). The construct validity or concept validity of a procedure refers to the quality of the conceptualization or operationalization of the relevant concept, to the extent to which a study investigates what it claims to investigate. It is important to consider construct validity during the data collection phase. Internal validity or logical validity (Cook & Campbell, 1979; Yin, 1994) refers to the causal relationships between variables and results and
whether there is a compelling argument that will support the research conclusions. Internal validity will be very important in the data analysis phase.

External validity has received the most attention from academia, especially since case study researchers are exposed to institutional pressure to generalize the research results (Ruigrok, Gibbert, Kaes, 2004). External validity refers to the possibility of determining generalizable findings for a wider context or situation. Especially for management research with close links to practice, the chances of a study being read is surely higher when there are practical conclusions that can be applied not only within the specific context of the study.

Last but not least, the reliability of the case study method must be maintained, so that those researchers who follow will arrive at the same insights if they conduct the study along the same steps again (Denzin and Lincoln, 1994). Transparency and replication by providing complete documentation and a database of the research procedure and all of its results represent the best way to maintain reliability (Yin, 1994).

One major point that the author also needed to be aware of in doing case study research in this area is the possibility of having selection
bias (Ruigrok, Gibbert, Kaes, 2004), that is, only highlighting positive outcomes from the case study that support the expected conclusion and add value, while downplaying negative points which contribute less to the goal of the research. On the other hand, a dilemma also arises when one conducts a case study based on a certain company’s success or failure. The result of the study will strongly affect the image and standing of the company in the public, which could later also affect the value of the company. It would be unlikely for the company to be willing to allow both the strengths and weaknesses of its model to be revealed. However, it is only through transparent research covering both sides that lessons can be learned from the case.

The author views case study as the best method for the research, given that it is actually the success of Temasek Holdings that makes the study of its corporate governance model interesting. By demonstrating that Temasek’s success indeed comes from a set of corporate governance practices that exceeds those of Indonesian SOEs, the Indonesian public (business community, media and the society at large) might learn that there is homework to be done by Indonesian SOEs in the area of corporate governance. It might be
better to understand what enables the growth of such a holding of
GLCs to lead to such expansion, rather than merely being critical of
Temasek’s expansion into Indonesia.

**Methodology for Data Collection**
It is understood that in case study research procedure, data collection
and analysis will overlap (Eisenhardt, 1989b). It can sometimes be in
the form of joint collection, coding, and analysis of data. Field notes
are helpful in overlapping data collection and analysis. Field notes
are an ongoing stream-of-consciousness commentary about what is
happening in the research, involving both observation and analysis
(Van Maanen, 1988). Field notes help the author to keep track of the
lessons learned during the ongoing process of data collection while
also promoting analysis of the situation.

The interviews in Indonesia were conducted with:

1. Prof. Dr. Djisman Simanjuntak: Corporate Governance Expert
   and Executive Director of Prasetya Mulya Business School

2. Mr. Martiono Hadianto: former CEO and President
   Commissioner of PT. Pertamina (now President Director of PT.
   Newmont Pacific)

3. Dr. Ichjar Musa: PT. Pertamina
4. Mr. Umar Juoro: Commissioner of Bank International Indonesia (BII) and Senior Fellow at The Habibie Center

5. Mr. Setyanto P. Santosa: Commissioner of PT. Indosat

6. Mr. Sumaryanto Widayatin: Commissioner of PT. Jasamarga

7. Mr. Pahala N. Mansury: Executive Vice President (EVP) Coordinator Finance & Strategy and Chief Financial Officer (CFO) PT. Bank Mandiri

8. Dr. Jos Luhukay, National Committee of Good Corporate Governance and former CEO of LippoBank (a Khazanah-linked company)

9. Dr. Tony Prasetiantono, Chief Economist of Bank Negara Indonesia (BNI)

10. Ms. Felia Salim, Commissioner of Bank Negara Indonesia (BNI)

11. Mr. Pandu Djajanto, Expert Staff on Corporate Governance for the Minister of State-Owned Enterprises


The interviews in Singapore were conducted with:

1. Ms. Myrna Thomas, Managing Director for Corporate Affairs, Temasek Holdings Pte. Ltd, together with Ms. Serena Khoo and Ms. Daliea Mohamad, both of whom are Directors for Corporate Affairs.

2. Mr. Yeoh Lam Keong, Director of Economics & Investments at Government of Singapore Investment Corporation (GIC). The information gathered was not in his capacity as a GIC officer, as GIC is not the focus of this research, but instead is meant to provide background information on Singapore’s GLC.

3. Singapore Technologies Telemedia (STT) as a Temasek-linked company also supplied information through a written interview which provides information as to how corporate governance is conducted at one of Temasek’s investee companies.

The data collection regarding Temasek Holdings was also conducted by press review and document analysis, including the Temasek Review, its annual report.
Interviews in Malaysia were carried out with Khazanah’s Senior Vice President at the Managing Director’s Office in charge of External Communication, Mr. Ahmad Shahizam Shariff, and the information on the context in Malaysia was also supported in an interview with Dato’ Dr. Michael Yeoh, the CEO of ASLI (Asian Strategy and Leadership Institute), a government think-tank.

The interviews with those top decision makers and experts were the most useful sources for gaining insight. The interviews, archival study, and press review served as sources of qualitative data as well as some quantitative data on the companies’ performance.

Triangulation is the application and combination of several research methodologies in the study of the same phenomenon. One of the principal aims of triangulation in the social sciences is to corroborate one set of findings with another; the hope is that two or more sets of findings will 'converge' on a single proposition. In order to apply the triangulation approach, it is necessary that one use a variety of methods in research. Triangulation can be applied to many elements of research methods, including strategies, settings for data collection.

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affecting external validity – and sources of data – single versus multiple (Scandura & Williams, 2000).

In this research, triangulation was achieved through:

- a combination of research methods: qualitative information through archival study/press reviews and interviews, and quantitative, through data obtained from company’s document (annual report);
- a comparison of the same phenomenon in three different countries: Singapore, Malaysia and Indonesia.
- sources of data: On the Singapore side, triangulation was achieved by having sources from Temasek Holdings and ST Telemedia as its investing companies. It was enriched with discussions with academics and experts on the topic of government-linked companies. The Malaysian triangulation was achieved by having two different interviews: one with a Khazanah Nasional official as the internal source of information, and another at an academic think-tank which provided an external party’s assessment of the model. In Indonesia, interviews with past and current officials of the Indonesian Ministry of SOEs (former Minister for SOEs and the current
expert staff for corporate governance at the ministry) were corroborated with information and opinions from the management board of Indonesian SOEs. All were triangulated with external sources of information from corporate governance experts (academicians, practitioners, consultants).

The archival study, interviews, and observations in Singapore served as a means to determine the key aspects of the model, ingredients for success of implementation, and its prerequisite. The archival study, interviews, observations and survey in Indonesia were used to compare the Indonesian situation and existing prerequisites for applying the Singaporean and Malaysian model, and interviews with decision makers are employed to confirm the possibility of applying the model.
Situational Corporate Governance of State-Owned Enterprises in Southeast Asia

It is important to note in situational corporate governance that for different types of firms, different approaches to corporate governance should be recommended. Despite the fact that the Anglo-American approach has been gaining great influence and has become the global Best Practice standard, one must take into account that the context in which a firm is embedded differentiates the situation. There are firm-specific factors that define this context. This requires that corporate governance for each firm must be kept situational as well. In principle, the factors defining the context can be divided into company-internal and company-external dimensions (Hilb, 2004, based on McGrath, 1976).

In seeking to understanding why corporate governance at SOEs in Southeast Asia should apply a situational approach, it is important to grasp how the company-external contexts differ with regard to their institutional, national culture, and norm contexts. In particular for the
case of SOEs, the company-internal context will also differ especially with regard to the type and behavior of the SOE’s shareholders. The following section will elaborate what the peculiarities of the company-external context for SOEs in Southeast Asia are and offer a subsequent analysis of the company-internal context for SOEs.

**Situational Corporate Governance in Southeast Asian Countries**

Company external contexts can be differentiated into the institutional, national culture, and normative contexts.

**Institutional Context**

Aguilera and Jackson (2003) employ the actor-centered institutionalism approach to explain the institutional context of firms (Scharpf, 1997) with regard to their interaction among their multiple stakeholders. Those stakeholders are:

- **a) Capital-/Shareholder**

  With regard to the firm’s shareholders, it is important to note whether the firm is primarily financially or strategically driven, i.e., other aspects such as image, growth, and market share, in its decision making. The constellation of capital providers in the
firm strongly defines this orientation, and countries differ from one another with regard to the importance of these capital providers and their influence over firms.

Anglo-American countries, in which shareholders play a strong role, put a great deal of emphasis on their particular interests in comparison to other stakeholders such as creditor banks. The case of Japan is the opposite, as a high percentage of firms capital comes as debt (Hilb, 2004). These national differences are shaped by the following institutional conditions in each country:

- property rights
- financial system
- existence of inter-firms network

The following table explains the impact of those differences on firm orientation, time-frame of investment, and percentage of equity:
Table 0-1 Interdependence of institutional context on capital factors (Hilb, 2004 based on Aguilera & Jackson, 2003)

<table>
<thead>
<tr>
<th>No</th>
<th>Institutional Factors (Capital)</th>
<th>Motivation for Investment</th>
<th>Time-frame of Investment</th>
<th>Percentage of Equity</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Strategic</td>
<td>Financial</td>
<td>Flexible</td>
</tr>
<tr>
<td>1</td>
<td>Property Rights</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Preference for large sharehol-</td>
<td>X</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>ders</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Protection of minority shareho-</td>
<td>X</td>
<td>X</td>
<td></td>
</tr>
<tr>
<td></td>
<td>lders</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2</td>
<td>Financial Systems</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Bank-based financial system</td>
<td></td>
<td></td>
<td>X</td>
</tr>
<tr>
<td></td>
<td>Capital market-based financial</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>system</td>
<td></td>
<td></td>
<td>X</td>
</tr>
<tr>
<td>3</td>
<td>Existence of Inter-firm Network</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Multiple inter-firm network</td>
<td>X</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Low inter-firm networks</td>
<td>X</td>
<td>X</td>
<td></td>
</tr>
</tbody>
</table>

The situation regarding the above issues in Southeast Asian countries is varied. For example, Indonesia is a bank-based financial system where the capital market is relatively dormant.
(Simanjuntak, 2005) and thus manifests a low percentage of equity in its firms. The inter-firm network is also strong, as shareholder ownership is very concentrated in Indonesia, where the capital market is not especially active. This then leads to a more strategic than financial motivation for investment with a long-term horizon. However, the biggest drawback in the system involves the issue of property rights. As a country formerly under Dutch rule, Indonesia has a legal system based on civil law tradition, as in the Netherlands itself or France, the most prominent example. La Porta et al. (1998) presented evidence that countries with civil law tradition provide weaker protection for outside investor interests than common law countries based on the British system. Both the content of their respective laws and regulations and the enforcement of implementation under common law provide better protection of shareholder rights than in civil law countries. By way of explanation, La Porta et al. (2000) suggest that this may stem from the fact that civil law countries have a history of more state intervention in private matters, including ownership, which may manifest also itself in corporate governance regulation.
Another issue requiring further analysis on the capital holders for the Indonesian institutional context is its dependence on bank financing (Simanjuntak, 2005). The financial crisis in 1998 provided clear evidence of how overdependence on bank financing, especially on foreign banks denominated in foreign currency, can be disastrous when a currency crisis strikes. Many firms had to default on their foreign-debt repayment, forcing the government to bail them out or act as guarantor of those debts. Furthermore, many firms had to be taken over by the government, creating a further burden for the state. This dependence on bank-financing also led to an agency problem in corporate governance: The major suppliers of capital to a firm had little or no control over management.

In comparison with other Southeast Asian countries, however, Indonesia’s fate was not much different. The case of Thailand and, to a lesser extent, Malaysia, which also suffered from the crisis, demonstrates how Southeast Asian developing countries have a bank-based structure of owners of capital. This structure has intermingling cross-ownership, which makes it more
strategically oriented but also more prone to the domino effect, with little protection of property rights.\(^6\)

\(b\) Labor (Employees)

Employee interests are relatively under-researched in corporate governance, except in Germany, where the role of the workers’ representative is very strong. National culture is influenced very much by the following constellation:

- Representation of employees in the board
- Importance of the labor union
- Skill formation

Germany and Japan are prominent cases where the above first two constellations, particularly Germany for the former and Japan for the latter, are obviously strong. The constellation in the Southeast Asian countries is more diverse, depending on the respective political system. Countries like Indonesia, the Philippines, and Thailand, which underwent drastic political changes in late ‘80s (the Philippines) and at the end of the ‘90s

\(^6\) However, the case of Malaysia and Singapore would differ. As former British-ruled countries, their legal systems are based on Common Law, which provides better protection of property rights.
(Indonesia and Thailand), have started experiencing stronger pressure from labor unions, which form constellations of relationships that tend to be more confrontational than cooperative. In the past, labor unions have been mostly under cooptation of a bureaucratic regime and the owners of capital, which provided stability and avoided class-conflict. However, the unions have suddenly emerged as one of the interests groups demanding more involvement, especially in decisions which affects the welfare of workers. Nevertheless, union involvement in the board as part of corporate governance is still minor, if not non-existent. Defining whether this change will lead to better circumstances for Indonesia with regard to corporate governance is problematic. On the one hand, if companies in the country are subject to an increasing importance of stakeholder orientation, they will have to respond in a manner which will build a model of corporate governance that involves employee representatives in decision making. On the other hand, a country in need of a business-friendly environment for investors in order to return to its growth level prior to the crisis would certainly face difficulties with an
increasing role of unions, as experiences in other countries suggest.

In Singapore, how labor unions are integrated into the decision-making process is clearly different from the process in other countries. Represented by NTUC (National Trade Union Congress) as the sole legal labor organization in Singapore, labor unions have enjoyed a relatively cosy relationship with the government and capital-holders, which ensures stability for firms’ as well as for the country’s economic growth.

The situation reflects how ‘class-based’ and ‘enterprise-based’ unions (Aguilera & Jackson, 2003) pursue different strategies in taking control over companies’ decision making. While the enterprise-based unions prefer to take internal participation as their controlling strategy, the class-based unions take an external control as strategy. The third factor, skill formation of labor, also defines this strategy. Workers with a firm-based skill formation will also pursue an internal participation strategy, while workers with a skill formation coming from the market or state (firm-ext) will also pursue an external participation strategy.
The following table summarizes the impact of different institutional situations that labor has in a country on its pursued strategy of participation in a company’s decision making.

Table 0-2 Interdependence of institutional context on labor factor (own depiction based on Aguilera & Jackson, 2003)

<table>
<thead>
<tr>
<th>No.</th>
<th>Institutional Factors (Labor)</th>
<th>Participation Strategy</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Internal</td>
</tr>
<tr>
<td>1.</td>
<td>Labor Representation</td>
<td></td>
</tr>
<tr>
<td></td>
<td>a. Strong representation</td>
<td>X</td>
</tr>
<tr>
<td></td>
<td>b. Weak representation</td>
<td></td>
</tr>
<tr>
<td>2.</td>
<td>Union Organization</td>
<td></td>
</tr>
<tr>
<td></td>
<td>a. Class-based or craft-based</td>
<td></td>
</tr>
<tr>
<td></td>
<td>b. Enterprise-based</td>
<td>X</td>
</tr>
<tr>
<td>3.</td>
<td>Skill Formation</td>
<td></td>
</tr>
<tr>
<td></td>
<td>a. State-based or market-based</td>
<td></td>
</tr>
<tr>
<td></td>
<td>b. Firm-based</td>
<td>X</td>
</tr>
</tbody>
</table>

In summary, it is not possible to uniformly classify the role of employees in corporate governance in Southeast Asia, as the situation differs starkly from one to another. This is clearly a factor requiring in-depth analysis when conducting comparative governance research within the Southeast Asian context.

c. **Top Management**

The role of top management in corporate governance has also not been thoroughly explored, despite its most dominant role.
Ironically, it is quite obvious that recent past corporate governance scandals are a reflection of how decision-making which is led by individual top managers who concentrate too much on their own interests can be disastrous. The so-called “Top Executive Value Thinking” has been the dominant factor in these scandals.

Top executive value thinking in each country is defined for the most part by two important factors:

- Career perspective (Sørensen, 1977): especially when the managerial labor market is predominantly closed, as in Japan (Dore, 2000 and Wakabayashi, 1980), or open, as in the US (Baker, Jensen, & Murphy, 1988 and Stroh, Brett, Baumann & Reilly, 1996), providing career opportunities elsewhere.

- Managerial ideology, described as “the major beliefs and values expressed by top managers that provide organizational members with a frame of reference for action” (Goll & Zeitz, 1991: 191). This ideology is shaped by many factors such as education (generalist or specialist), diffusion of cognitive models of control.
(O’Sullivan, 2000) and the informal routines and norms that shape the autonomy or commitment of management. The country’s political system also affects the ideology-shaping of managers. Countries with a presidential system tend to shape a top-down business approach among managers, while a non-presidential system is likely to drive more consensus-seeking behaviors (Hilb, 2004). A clear example is how the USA and Swiss systems differ in this matter. The Swiss consensual political system, in which, for example, leaders of political parties sitting together on the federal council, the highest government body, alternately serve as the country’s federal president, has led to a greater commitment to the concept of the firm with a functional orientation, as well as less autonomy and financial orientation than their American counterparts.

In this respect, no clear evidence or trend has been found regarding Top-Executive-Value thinking in Southeast Asian countries, in particular, in Indonesia and Singapore. Indonesia
has a presidential system with the President as both Head of State and the Government, while Singapore has a parliamentary system in which the Prime Minster, as the Head of Government, is the power holder, and the President, as Head of State, has a symbolic role. These two different political systems influence the shaping of top management thinking and corporate governance style as well: Indonesian managers tend to have a more top-down approach than Singaporean managers. However, the political situation has changed. While Singapore has enjoyed a relatively stable political and cultural climate over the last ten years, Indonesia has, over the same time period, undergone radical change in politics and culture. That process has forced Indonesian managers to develop a more open attitude toward the demands of a larger group of stakeholders, e.g., labor unions and environmental groups, who have been able to raise their voices in the new, more open political environment.

While career opportunities have not been scientifically measured and compared, the fact that Singapore has a stronger presence of multinational firms and is more strongly embedded
in the international business network suggests that the career horizon is more open in Singapore than Indonesia, thus shaping a greater autonomy for the country’s managers than in a relatively more closed labor market with fewer external career opportunities. The following table summarizes the impact of the different institutional situations that the managerial labor force may encounter in in a country on its degree of autonomy versus commitment, and financial versus functional orientation.
Table 0-3 Interdependence of institutional context on management factor (own depiction based on Aguilera & Jackson, 2003)

<table>
<thead>
<tr>
<th>No</th>
<th>Institutional Factors (Management)</th>
<th>Relation to Firm</th>
<th>Financial vs. Functional Orientation</th>
<th>Type of Skills</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Autonomy</td>
<td>Commitment</td>
<td>Financial</td>
</tr>
<tr>
<td>1</td>
<td>Ideologies</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Generalist knowledge and/or hierarchical decision-making</td>
<td>X</td>
<td></td>
<td>X</td>
</tr>
<tr>
<td></td>
<td>Specialist knowledge and/or consensual decision-making</td>
<td></td>
<td>X</td>
<td></td>
</tr>
<tr>
<td>2</td>
<td>Career perspective (managerial labor market)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Open</td>
<td>X</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Closed</td>
<td>X</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Having summarized the three dominant stakeholders shaping the institutional domain, the key question is “…how the combination of institutional domains, in a particular country shape corporate governance at the firm level?” (Aguilera & Jackson, 2003: 454)
In the context of Indonesia, the primary concern about corporate governance reform is precisely the gap between the spirit and the letter of governance-related laws and the regulation and implementation thereof (Simanjuntak, 2005). It is however by no means the only difficult obstacle to corporate governance reform. Recognition that the gap exists is another significant problem. It might be because the benefits of corporate governance reform are unconvincing for policy-makers, of little relevance to economy-wide policy making, or not in favor of the policy-makers.

In this regard, Rosser (2005) provides another view, the political economy perspective, in his explanation of why corporate governance reform in Indonesia has been slow in its progress. He argues that the weak implementation of regulatory changes in the area of corporate governance is caused by the political dominance of the politico-bureaucrats and their corporate clients over the technocrats in the Indonesian government. The bureaucrats and their corporate clients are the controllers and owners of Indonesia’s major conglomerates, while the technocrats represent the international financial institutions, Western governments, and controllers of mobile capital. Thus, the conflicting interests of these two coalitions
– the politico bureaucrats and the owners of major conglomerates on the one hand, and the technocrats who brought the agenda of corporate governance changes in line with the Anglo-American model on the other hand – have been the major cause of slow corporate governance improvement and implementation in Indonesia.

**National Culture Context**
Figure 2.5 provided an illustration of how corporate governance is differentiated by a board’s value orientation (Hilb, 2004). That figure also serves as a basis for understanding how a corporate governance model is generally formed within the context of national culture. Several factors influence national culture:

- composition of capital provided by shareholders and other stakeholders (e.g., creditors), like the clear contrast between the USA, with about 80% of capital coming from shareholders, and Japan, where only about 20% comes from shareholders
- attitude toward competition and cooperation, as the two dimensions of how the corporate governance approach is
measured, as depicted, for example, in Figure 3.1 (Hilb, 2004 based on MODE Model)

**Figure 4.1 Differences among National Cultures**

- Classification of various national cultures, such as Hofstede’s (1997) or Laurent’s (1997). Laurent’s classification of ‘soft’ and ‘hard’ national cultures, or as he termed them, ‘blue’ and ‘green’ cultures, along with the dimensions and drawbacks of both cultures are described in Table 3.4 and Table 3.5.
Table 0-4 Dimensions of Hard Culture and Soft Culture  
(Laurent, 1997)

<table>
<thead>
<tr>
<th>No.</th>
<th>Dimensions</th>
<th>Type of National Culture</th>
<th>‘Hard Culture’</th>
<th>‘Soft Culture’</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Timeframe</td>
<td>Short-term results</td>
<td>Long-term orientation</td>
<td></td>
</tr>
<tr>
<td>2.</td>
<td>Point of interests</td>
<td>Task-orientation</td>
<td>Relationship-orientation</td>
<td></td>
</tr>
<tr>
<td>3.</td>
<td>Driving factor</td>
<td>Goal</td>
<td>People</td>
<td></td>
</tr>
<tr>
<td>4.</td>
<td>Promoted attributes</td>
<td>Performance and Mobility</td>
<td>Engagement and Loyalty</td>
<td></td>
</tr>
<tr>
<td>5.</td>
<td>Motto</td>
<td>Changeability of each part</td>
<td>Encouragement of cooperation and networking</td>
<td></td>
</tr>
<tr>
<td>6.</td>
<td>Decision-finding</td>
<td>Fast (Top-down) decision</td>
<td>Slow (Bottom-Up) decision</td>
<td></td>
</tr>
<tr>
<td>7.</td>
<td>Goal</td>
<td>Transparency</td>
<td>Innovation</td>
<td></td>
</tr>
<tr>
<td>8.</td>
<td>Strategy</td>
<td>Clarity</td>
<td>Flexibility</td>
<td></td>
</tr>
<tr>
<td>9.</td>
<td>Characteristic</td>
<td>Predictability</td>
<td>Adaptability</td>
<td></td>
</tr>
<tr>
<td>10.</td>
<td>Feedback</td>
<td>Controllability</td>
<td>Responsiveness</td>
<td></td>
</tr>
</tbody>
</table>

Table 0-5 Drawbacks of Hard Culture and Soft Culture  
(Laurent, 1997)

<table>
<thead>
<tr>
<th>No.</th>
<th>Hard Culture</th>
<th>Soft Culture</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Over-structured</td>
<td>Confusion</td>
</tr>
<tr>
<td>2.</td>
<td>Too short-term orientation</td>
<td>Little attention to short-term</td>
</tr>
<tr>
<td>3.</td>
<td>De-motivation of individuals</td>
<td>Restrictions for individuals</td>
</tr>
<tr>
<td>4.</td>
<td>Numbers-obsession</td>
<td>Group-obsession</td>
</tr>
<tr>
<td>5.</td>
<td>Ruthlessness</td>
<td>Difficulty to change</td>
</tr>
<tr>
<td>6.</td>
<td>Too focused on planning</td>
<td>Too focused on vision</td>
</tr>
<tr>
<td>7.</td>
<td>Over-management</td>
<td>Redundancy</td>
</tr>
<tr>
<td>8.</td>
<td>Disproportionate trust on system</td>
<td>Disproportionate power game</td>
</tr>
<tr>
<td>9.</td>
<td>Rigidity</td>
<td>Chaos</td>
</tr>
<tr>
<td>10.</td>
<td>Overemphasis on market</td>
<td>Overemphasis on hierarchy</td>
</tr>
</tbody>
</table>
For a comparative governance study of corporate governance models in the region, it is important to identify how Southeast Asian countries, particularly, Indonesia, Singapore, Malaysia and Thailand, score on these dimensions. If Laurent’s hard and soft cultures are unavailable for those countries in detail, Hofstede’s or Trompenaars & Hampden-Turner’s dimensions of national culture, which have several similarities to Laurent’s, can be used to explain the national culture differences.

**Normative Context**
The above-mentioned national cultures also define the normative regulation in each country. The normative context of corporate governance has two dimensions which both have to be fulfilled, as shown in Figure 4.2:
Figure 4.2 Corporate Governance Compliance (Hilb, 2004)

a. Legality of the Management Board

The legality of corporate governance is differentiated according to legal regulation (hard law) and non-binding recommendation (soft law), which vary strongly in each country. Usually, countries with a high number of publicly-listed companies in the stock market put emphasis on hard-law with some soft-law recommendations on smaller and non-listed firms, while countries with a small number of listed companies seek numerous regulations in the form of non-binding soft law.
When the theme of corporate governance arises in discussion, it is imperative to highlight two events. The first is, in the global context, the fall of Enron and other global giants due to improper, dishonest, and non-transparent business practices, which led to a grave loss of global public trust in financial institution. The second event, specific to the Asian context, was the financial crisis in the late 1990s, which prompted most of the affected countries to make improved corporate governance a priority. Agreement is growing, at least in principle, on what good governance entails, and most countries in the region have adopted explicit governance codes. Corporate governance is a major agenda item in Asia right now, even though progress does not occur at the same speed or with the same quality of implementation in individual countries due to the influence of each country’s political, economic, and cultural contexts. A series of new corporate-governance laws and codes have been launched as a reaction to those phenomena. Due to its overarching and restricting global effects, especially for companies listed at the New York Stock Exchange,
Sarbanes-Oxley (2002) is the most prominent and highly-debated one. However, the global point of reference for international policy dialogue in corporate governance involves the OECD Principles of Corporate Governance, developed in 1999. The OECD code has been the standard Best Practice recommendation for corporate governance codes all over the world. The situation in different countries has, however, manifested a disparity in levels of achievement. The highest level of worldwide Best Practice recommendations for corporate governance is surprisingly the South-African King II Report, whose content includes terms on risk management and integrated sustainability reporting.

In Asia, it is important to note that Singapore (2002) is regarded as having the most commendable Best Practice code. There is a positive effect for Southeast Asian countries when they see that one of the countries in the region is regarded as the best in terms corporate governance codes for the entire Asian region. Moreover, Singapore is also highly regarded in terms of efficient practices of board

The legal aspect of the normative context in corporate governance suggests that Singapore can be considered as exemplifying the best practice standard in Southeast Asia and Asia as a whole, not only in terms of codes and regulations but also practice. It is now important to see the legitimacy aspect as the other part of the normative context in Southeast Asian countries.

b. Legitimacy of the Management Board

One obvious lesson from all of the corporate governance scandals is that a lack of integrity is a major cause of mismanagement. A company can have an idealistic vision and mission statement, a best-practice-oriented corporate governance code of conduct, and the strictest laws and regulations, but without the integrity of its top management, all is to no avail. Again, the case of Enron emphasizes precisely this lesson: Just one-year before its downfall,
Enron had been regarded as having one of the finest sets of best-practice guidelines in the US.

The issue of integrity is also important in Southeast Asia, as the financial crisis is believed to have also resulted from a lack of integrity, not only among its corporate leaders, but also political leaders. The political changes which occurred following the Asian crisis are the result of a demand for a better and cleaner government free from corruption. While this issue has not yet been fully resolved, with political instability still plaguing some countries in the region (Indonesia from 1999 until 2004, Thailand and Philippines, as recently as the beginning of 2006), the importance of integrity has been clearly recognized by the public, making it now an important criterion for choosing leadership.

Singapore has again set itself apart from its neighboring countries with regard to this issue. Apart from the long-lasting, stable political system, resulting from the relatively clean governance it has been enjoying for almost 40 years, Singapore has also witnessed positive trends in the behavior of its companies. In terms of business ethics-related
behavior within Singaporean companies, the role of executive boards has scored reasonably well in IMD World Competitiveness. The 2003 ranking places Singapore 5th globally, 3rd in Asia-Oceania (behind Australia and New Zealand) and tops the ranking among all Asian countries.

The institutional, national culture and normative context of corporate governance in Southeast Asia has shown that Singapore is well-positioned to be a benchmark for its neighboring nations. However, it is precisely due to these differences that it is of paramount importance to take these gaps into account when attempting to follow best-practice corporate governance guideline and governance structure.

**Situational Corporate Governance of State-Owned Enterprises**

Apart from the company-external context, situational corporate governance should also consider components of the company-internal context which influence corporate governance. The most important components with regard to corporate governance in state-owned enterprises are the ownership structure and behavior (given the role of state as principal, is situation is unique) and the board’s power structure and behavior, which is influenced very much by
what corporate governance system a country has, i.e., a dual or monistic system.

Ownership Structure and Behavior at State-Owned Enterprises
As discussed before, the key difference in the corporate governance of SOEs is the unique condition of having the state as the owner. The poor performance of many SOEs can be attributed to the three main challenges facing SOE governance in comparison to private sector enterprises (Wong, 2004). The following table describes the differences between governance in state-owned enterprises and private sector enterprises.

Table 0-6 Differences in Governance between Private and Public Sector Enterprises (Wong, 2004)

<table>
<thead>
<tr>
<th></th>
<th>Private sector firms</th>
<th>SOEs</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>A. Objectives</strong></td>
<td>Clear focus on value maximization</td>
<td>Pursue commercial and non-commercial objectives</td>
</tr>
<tr>
<td><strong>B. Agency Issues</strong></td>
<td>Single agency – concerned about self-interested behaviour by managers</td>
<td>Double agency – concerned about self-interested behaviour by managers AND politicians / bureaucrats</td>
</tr>
<tr>
<td><strong>C. Transparency</strong></td>
<td>High level of disclosure (for publicly listed private firms)</td>
<td>Low level of disclosure</td>
</tr>
</tbody>
</table>
Corporate governance reform must tackle all three issues in an integrated manner; otherwise, the results will be disappointing. This reform should only address SOEs operating in a purely commercial manner (with a singular focus on value maximization) or those operating in a manner that reflects both a largely commercial and social orientation, but are commercially viable. In other words, when the costs of any non-commercial objectives are removed, the SOE should be able to recover its own cost of capital. Otherwise, it would also be not viable to improve the company and instead, closing it down or selling it off would be a better option.

The integrated reform packages suggested by Wong (2004) in handling these problems include clear objectives, insulation from political interference, and transparency improvement, as depicted in the following diagram.

It is important to note, especially with regard to the second measure, that Temasek Holdings has been mentioned as an example of how political insulation is conducted. By putting the ownership and monitoring of all SOEs, or, in Singapore’s case, the GLCs, under just one structure, the political interference of various government agencies or officials is minimized. These GLCs should only ‘serve
one master’, that is, Temasek Holdings, which also helps in setting up clear objectives and monitoring their achievement. The role of Temasek as the “one master” is highlighted in this research as it might serve as a model not only for enhancing shareholder-value orientation for SOEs but also for insulating companies against political interference. However, while evidence from Temasek Holdings also suggests that this model was successful in upholding the first and second pillars of SOE reforms, it is clear that it was much less successful in the case of the third pillar, i.e., improving transparency (Ho, 2005)

**Board Power-Structure and –Behavior at State-Owned Enterprises**

Two other company-important factors which differentiate the corporate governance of one firm from that of another are power structure and behavior within the board. They are differentiated by the internationally-varied board systems of corporate governance. The two most frequently used systems are the following:

1. The monistic board system

   It is the system most commonly used in countries where there are overlaps between the Supervisory Board and
Managing Board. This is often also found in family companies in which most of the family members are at the same time members of both the Managing Board and Supervisory Board, i.e., the so-called executive managing board. In the US, only the CEO who is at the same also the Chairman of Supervisory Board sits on both boards. The risk inherent in this model, however, is the possible concentration of power in the hands of the chairman and CEO, as there is a lack of critical feedback from necessary parties. It is even more dangerous when the role of chairman and CEO is held by the same person. The role of the Supervisory Board might be reduced to a mere administrative role in order to simply fulfill legal requirements.

2. The dual-board system

The dual-board system is the most frequently occurring system in Germany as well as a number of other countries, including Indonesia, which was heavily influenced by the Dutch, who have the same system. In this model, the Managing Board and Supervisory Board, or in Indonesian
terms, the Board of Directors and Board of Commissioners must be separated from each other, ensuring better checks and balances. However, the risk is that it might lead to a power struggle between the two boards, which would hinder the firm’s sustainable competitiveness.

Figure 4.3 Two Models of Board Systems (Hilb, 2004)

In the context of Indonesia, suggestion for reform of the dual-board is quite evident (Simanjuntak, 2005: 177): “At issue is the working relationship between the Board of Commissioners and Board of Directors. This relationship must be defined precisely as possible as regards nomination of commissioners and directors and remuneration. Indonesia
can consider strengthening the Board of Commissioners along the German system or moving to a single board system where the CEO is the only representative of management in the board and the CEO is not allowed to also to serve as chairman of the board.”

While the latter suggestion might be a viable solution, and is one which others have also suggested to be such, as will be elaborated in the next paragraph, the former consideration of strengthening the dual system seems to be not helpful, in particular for the case of Indonesian SOEs. The current dual system requires that representatives of the Ministry of SOEs sit at the Board of Comissioners. Strengthening the role of Board of Comissioners could be good, assuming that the representatives of the ministry can really play a monitoring and controlling role in protecting the interests of taxpayers as shareholders. However, if we assume the current condition - that politicians and bureaucrats are poor overseers of enterprises - then strengthening the role of Board of Comissioners will only provide inviduals with doubtful capacity and capability with the opportunity to exercise
power. In such a case, the potential power struggle which one fears as the drawback of the dual system might become reality.

More plausible seems to be the latter suggestion to proceed with the single board system with a separated role of Chairman and CEO, but also adding the requirement that the majority of Supervisory Board members should be independent directors who have no vested interests in the firm (Vermeulen, 2002). However, that would require fundamental legal changes. In that way, the independence of non-executive directors, assuming that they are also independent of political interest, can be better guaranteed to insulate SOEs from political interference.
It is important to highlight the situation of SOEs in Southeast Asia in this section, as well as the situation of GLCs as their other form. However, I limit the countries to be discussed in the research to Indonesia, as the main object upon which results and conclusions should be drawn upon, Singapore, as an example of best practice of corporate governance and the country from which the GLC investment holding model stems, and Malaysia as another country managing GLCs in investment holding along the Singaporean model. Examples from several other Asian countries, Thailand, Vietnam, and China planning to employ the investment holding model are also mentioned.
New Corporate Governance at Singapore’s Temasek Holdings: Holding Structure to Govern GLCs

Temasek Holdings is the investment arm of the Singaporean government which serves as the holding company of Singapore’s government-linked companies (GLCs). Temasek defines GLCs as those companies in which the government has a 20% or greater ownership and/or controls the majority of voting rights.

Typical Singaporean companies generally grow out of a majority family-owned environment or government-controlled entity. Temasek’s GLCs belong to the latter group. Up to 80% of some GLCs are directly and indirectly controlled by the government, while a smaller percentage of major non-government-linked companies in the banking, shipping and technology sectors are controlled indirectly through inter-corporate equity shares between GLCs and non-GLCs (Anandarajah, 2005).

Situational Corporate Governance at Temasek Holdings

Temasek Holdings is a private investment arm, with the Singaporean government as its major shareholder, and it is responsible to the President of the Republic of Singapore as the highest government

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7 Analysis is based on information from Temasek Review 2007: Creating Value.
office, reflecting a government-owned characteristic. However, Temasek was incorporated in 1974 as an exempt private company\(^8\), also known as a Fifth Schedule company, with limited liability to hold investments in companies previously held directly by the Singapore Ministry of Finance. Therefore, Temasek is a private company by definition. This is where the unique situation of Temasek must be taken into account. As an investment holding of the government, with ownership of companies in strategic industries which surely influences public life, Temasek is by ownership structure and economic purpose a private investment institution. This was a consequence of a strategic commitment to managing these investments on a sound commercial basis as a private investment, separated from the government’s economic function of policy-making and market regulation. With this system, the government is then able to act in the larger interest of the overall economy, whereas a private investment’s interest is to achieve financially profitable and value-creating results. However, Temasek

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\(^8\) An exempt private company, as defined under the Republic of Singapore's Companies Act, includes a private company in whose shares no beneficial interest is held directly or indirectly by any corporation and which has no more than 20 members. As an exempt private company, Temasek is not required to publish or publicly disclose its financial accounts.
noted that the government needed to own and control companies for various reasons. These include critical resources, i.e., where ownership of a resource is critical to Singapore's security or economic well-being\(^9\). It is one of the reasons why the model for Temasek Holdings was formed.

The value created by Temasek for its shareholders, which amounts to SG$ 164 billion\(^{10}\) (about US$ 108 billion) portfolio value, is also related to its focus on sound corporate governance as one of its important pillars. The company’s value has grown more than 400 times from a mere SG$ 354 million in 1974 when Temasek was established.

Temasek considers both shareholder and stakeholder orientation in its business decisions. As an investment company, the measure of success for Temasek’s board is clearly defined as shareholder-oriented by its commitment to maximizing long-term shareholder returns. The company’s shareholders require the company is to earn a proper return on Temasek’s investments as a commercial entity. Its stakeholder-orientation is reflected in its accountability to the

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\(^{10}\) Based on market value for listed assets and book value for unlisted assets as of 31 March 2007.
President of the Singapore, an independent and directly elected representative of the people of Singapore, as Temasek’s stakeholder. As it is accountable to the representative of the people, Temasek must also make certain that its business decisions benefit the people of Singapore as its stakeholder through the creation of value for the Singaporean government as its shareholder.

The government-owned characteristic of Temasek is emphasized by the presidential approval required in the following cases:

1. Appointment, re-appointment and/or removal of key personnel

   Appointment, reappointment and/or removal of Board members or the CEO is subject to the approval of the elected President of the Republic of Singapore acting at his own discretion

2. Any use of past reserves\(^{11}\) by each newly elected government

   The Board is required to ensure that the annual operating budget or any proposed transaction does not draw on past

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\(^{11}\) Article 1424(4) of the Singapore Constitution defines “past reserves of the Government” as those reserves not accumulated by the Government during its current term of office, including accretions which are deemed to be part of such reserves.
reserves, except with the approval of the elected President.

The Chairman and CEO are required to certify a Statement of Reserves and Statement of Past Reserves to the elected President on a semi-annual basis.

3. Certain financial governance matters in designated government institutions and companies to ensure proper governance and management of key assets.

Apart from its normal fiduciary duty, the Board is accountable to the elected President to ensure that disposal of investments is transacted at fair market value.

Except for all of the above-mentioned matters, the Board and Management have full authority and responsibility for investment and other business decisions, reflecting the characteristic of a private investment seeking profitable results.

As an investment company, the Temasek Board’s measure of success is clearly defined as shareholder-oriented in its commitment to maximizing long-term shareholder returns. The company’s shareholders require it to earn a proper return on Temasek’s investments as a commercial entity.
Its stakeholder-orientation is reflected in its accountability to the President of the Singapore, an independent and directly elected representative of the people of Singapore as Temasek’s stakeholder. In being accountable to the President, Temasek must also make certain that its business decisions benefit the people of Singapore as its stakeholder, by creating value for the Singaporean government as its shareholder.

Having both orientations as a measure of success and a controlling function, Temasek companies aim to fulfill the 'glocal' type of coopetition model (Hilb, 2004) as an integrated corporate governance approach. Moreover, by maximizing investment value for the Singaporean government as its shareholder, Temasek generates more state income for the government as a source of funding for development. The greater investment value generated also means more state funds for development, which should benefit the people of Singapore as one of the key stakeholders, providing that they are used properly. There seems to be no conflict between shareholder and stakeholder value in this situation, where satisfying one party will also mean generating capabilities to satisfy other parties.
However, this can work properly only in a system where good and clean governance exist, not only at the level of enterprise management, but also at the level of government and public sector management. Therefore, a thorough analysis of this success model should be followed by a careful consideration of whether the socio-politic-cultural situation in Indonesia is supportive or contradictive to this model. It is now apparent that the clean and good governance culture that Singapore has been applying is in contrast with the acute corruption problem that Indonesia has. Transparency International Corruption Perception Index 2005 ranks Singapore as the 5th best, while Indonesia ranks 137th out of the 159 countries surveyed. This is one of the already obvious obstacles hindering the possible transfer of Temasek’s corporate governance model from Singapore to Indonesia, since corporate governance clearly requires transparency.

Strategic Corporate Governance at Temasek Holdings

Successful corporate governance practice should also drive the company to successfully develop, implement and monitor its corporate strategy. The four main conditions for developing this are:


(retrieved on April 13th, 2005).
• a strategically targeted composition of the board team,
• a constructive and open-minded board culture,
• an efficient board structure, and
• shareholder- and stakeholder-oriented board measures of success

Temasek fulfills those conditions and incorporates them into its corporate governance guidelines in the following points:

1. **Board Composition**

   Temasek has a number of distinguished business leaders serving both on its board as well as the boards of its various companies. That allows the holding to have a wide range of access and influence to fulfill its goal as an investment holding by opening opportunities in and providing sufficient information on certain industries or companies that potentially add value to Temasek. A detailed profile and analysis of Temasek’s board 2007 is found in section 5.4.

2. **Board Culture**

   Temasek’s directorship profile for its companies’ boards reflects a mixture that would support a constructive and open-minded culture. The direct and deemed shareholdings
in 34 major GLCs (ranging from 29% to 100% ownership) consist of the following elements on its boards:

- Independent member : 71%
- Non-Singaporean : 15%
- Female : 8%
- Temasek management : 7%

Providing a non-Singaporean perspective, those members help to develop an open-minded culture and to ensure that international perspectives in decision making are taken into account (despite Temasek’s being owned by a national government). The high proportion of independent members can also prevent biased and narrow-minded decisions serving merely the interests of internal board members. In the specific case of Temasek’s board itself, the important role of having a non-Singaporean on the board is elaborated in section 5.4.

However, the number of females is still low with respect to international standards. It is nevertheless a relatively significant figure in the context of Asian culture, where few female business leaders are in top positions.
3. *Board Structure*

Temasek supports a robust board governance process that institutionalizes professional and objective management of a company and its leadership renewal. The business of Temasek is guided and directed by a nine-member Board, assisted by three Board committees:

- Executive Committee (ExCo)
- Audit Committee (AC)
- Leadership Development and Compensation Committee (LDCC)

The New Corporate Governance approach (Hilb, 2004) suggests that an optimal number of board member is a seven, assisted by only two board committees:

- An integrated Audit and Risk Management Committee
- An integrated board management committee which is responsible for nomination, feedback, remuneration and development of the board and top management
Although it does not exactly follow the model in terms of the number of members and boards, Temasek’s structure is in line with the recommended composition in that it has the AC in charge of audit and risk management functions, and the LDCC fulfills the function of the second board. Temasek’s ExCo, a board committee not in the model, is authorized to act on behalf of the Board. It reviews, considers, and approves matters, including those relating to supervision and control, financing and funding, merger and acquisitions, changes in shareholding structure, dividend policy and major business decisions, within financial limits delegated by the Board. It is also responsible for formulating policies and guidelines to manage Temasek’s capital resources effectively and efficiently.\footnote{Previously until 2006, this last function was carried out by another board committee called the Capital Resources Committee (CRC).}

4. Board Measures of Success

As Temasek is an investment company, its board’s measure of success is clearly defined as shareholder-oriented by its commitment to maximizing long-term shareholder returns.
Its shareholders require that the company earn a proper return on Temasek’s investments as a commercial entity. Its stakeholder-orientation is reflected by its accountability to the President of the Singapore, an independent and directly elected representative of the people of Singapore, as Temasek’s stakeholder. In being accountable to the representative of the people, Temasek must also make certain that its business decisions benefit the people of Singapore as its stakeholder by creating value for the Singaporean government as its shareholder.

**Integrated Corporate Governance at Temasek Holdings**
The New Corporate Governance approach recommends that four targeted processes exist in order to have integrated corporate governance: targeted selection of board members, targeted feedback on their performance, targeted performance-related remuneration, and targeted development.

Temasek’s practice of the above-mentioned points is stipulated by the Leadership Development and Compensation Committee (LDCC), whose objectives are to establish policies and provide guidelines for Temasek and relevant TLCs in the following areas:
• Leadership and succession plans for key positions
• Board appointments, renewals and compensations
• Reviews and approval of performance-based compensation plans

The LDCC applies a 360° performance evaluation to Board members as a means to gain integrated feedback on Board performance. Remuneration and the development program to improve performance are based on this evaluation.

**Controlled Corporate Governance at Temasek Holdings**

The controlling or monitoring board dimension should cover the following four functions: auditing, risk management, communication and evaluation.

1. **Auditing Function**

   The auditing function of the Temasek board is carried out under the approval of annual audited accounts. The Audit Committee (AC) assists the Board in this function by reviewing the following systems and processes to ensure the proper conduct of company business:

   - Financial reporting
   - Internal and external audit
Management of financial risks

Internal controls

Compliance with applicable laws and regulations

The AC has full access to information and cooperation from all employees. It has the authority to engage external legal and professional advisors where appropriate.

2. Risk Management Function

Risk management and oversight are the responsibility of the Board. Supported by the CEO together with senior management and the Risk Management Unit (RMU), the Board determines the objectives and policies that govern the business and investment risks, review the risk management framework and promote a culture of risk awareness within the company.

In April 2005, oversight and risk management of the public market fund management unit was delegated to the Board of the newly incorporated Fullerton Fund Management Company (Fullerton) supported by the Risk Management Unit. Apart from Fullerton, the Temasek Board is also
assisted by two Board committees in the following risk areas:

- **Executive Committee**
  - Business & political risks (management & oversight)
  - Structural foreign exchange risks
  - Investment and country risks (for strategic investments)
  - Operational risks (of Temasek as a whole)

- **Audit Committee**
  - Operational risks and assessment of compliance with internal controls
  - Interaction with external and internal auditor to review auditing process
  - Evaluation of the effectiveness of risk management within Temasek

3. *The Communication Function*

The Board communication function is fulfilled by the Board and Committee Meetings. The Board meets at least on a
quarterly basis, and more often if required. The ExCo meets
between Board meetings, as and when required, to provide
timely decision making and clearance on major operational
matters. The Audit Committee meets quarterly to review the
audited financial results before submission for Board
approval. The LDCC meets at least twice a year to provide
an update on developments and significant changes at the
boards and management of TLCs, as well as to review
compensation benchmarks and guidelines. It also meets at
least once a year for Board feedback, evaluation and to
approve compensation.

4. The Evaluation Function

The Board evaluation function at Temasek is not elaborated
in detailed. However, it has a 360° system of performance
evaluation, meaning that every member of the board is
evaluated by all other members. It is also evaluated by
subordinates in order to ensure that all decisions made are
fair.
Temasek Holdings: Inspiring Other Countries to Manage SOEs ‘Under One Roof’

The case of corporate governance of government-linked companies (GLCs) under Singapore’s Temasek Holdings (Temasek) and Malaysia’s Khazanah Nasional Berhad (Khazanah) has drawn interest with respect to its being a possible model for Indonesia to govern its state-owned enterprises (SOEs). The holding company structure as a way to manage state assets “under one roof” is now a global trend, especially in countries that are considered to be in a developmental state.

In Southeast Asia, Vietnam has also recently set up such holding companies for its SOEs under the name of State Capital Investment Corporation (SCIC). Under Thaksin’s administration, Thailand also had plans to build such a super-holding structure, but with the fall of his administration after a military coup, the plan now seems to have been shelved. Outside ASEAN, China is also on the way to galvanizing its SOEs under one holding structure, and Kazakhstan as well. In countries like the UK and Australia, the government’s one-
roof structure performs monitoring and management functions, but it does not hold equity in the companies\textsuperscript{14}.

As a theoretical framework, the holding company structure seems to fit the three pillars required for SOE reform (Wong, 2004): clear direction, insulation from political interference, and transparency improvement. The holding structure as practiced by Temasek and Khazanah helps in supporting the above three aspects of SOE reform as described in the following figure.

The corporate governance practice of Temasek is also perceived as the best practice for GLCs and SOEs in Southeast Asia, both in terms of conformance and performance. In terms of conformance, the GLCs, also dubbed Temasek-linked companies (TLCs), have received the following awards for corporate governance practices:

- In the CLSA corporate governance ranking of Singaporean companies published in 2002, 11 of the top 15 listed companies are TLCs
- At the 27\textsuperscript{th} Annual Reports Award competition (2001), Keppel Land, Singapore Airlines, and ST Engineering won the top three prizes for main board listed companies

\textsuperscript{14} Details can be found at Putrajaya Committee on GLC High Performance, Progress Review, December 2006.
Standard & Poor’s inaugural Transparency and Disclosure Survey published in November 2001 rated ST Engineering as one of the companies with the highest level of corporate transparency and disclosure in Asia Pacific.

Those awards present a compelling argument for taking Temasek’s corporate governance as a best practice example for state-/government-owned (or linked) enterprises in Asia from a conformance perspective.

With regard to performance, it is obvious that the value created by Temasek for its shareholders, amounting to SG$ 164 billion (about US$ 120 billion) portfolio value as 31 March 2007, is definitely also a contribution of its focus on sound corporate governance as one of its important pillars. Temasek’s shareholder returns achieved 27% in March 2007, which is even better than those of the best-performing long-term investors such as Warren Buffet whose Berkshire Hathaway had a return of 20.7%. This is a commendable achievement for a state-owned entity. Due to the lack of an appropriate benchmark\textsuperscript{15}, analysts questioned whether the figure of 24% as Temasek’s shareholder value return is indeed satisfactory.

\textsuperscript{15}“Just how good are Temasek’s returns?“, The Straits Times, 8 September 2006.
enough. However, there is still no doubt that the holding is currently one of the biggest sovereign wealth funds. It is therefore logical that Southeast Asian countries aim to emulate the Singaporean model to manage their SOEs. The next chapters will review the state of development in the area of governing state enterprises in Singapore, Malaysia and Indonesia. It will also touch briefly upon Vietnam, as Temasek admits that Vietnam is influenced by the Singaporean model\textsuperscript{16}. China, with its state investment agency modeled after Temasek, is poised to be the largest in Asia and will also be dealt with briefly in the dissertation.

\textit{Singapore’s Temasek Holdings: From Developmental State to Developing ‘The External Wings of the Economy’}

Singapore developed Temasek Holdings in 1974 as a limited liability exempt private company\textsuperscript{17} to incorporate investments previously held by the Ministry of Finance Inc. It has now evolved into an Asian investment house, headquartered in Singapore. This is the unique

\textsuperscript{16} Author’s interview with Myrna Thomas, Managing Director for Corporate Affairs for Temasek Holdings, 14 September 2007. In the case of Malaysia’s Khazanah and the Indonesian SOE master plan, Temasek stated that it could not claim that the two have followed in its footsteps.

\textsuperscript{17} Under the Singapore Companies Act (Chapter 50), an exempt private company has no more than 20 shareholders and no corporate shareholder and is exempted from filing its audited financials with the public registry.
context of Temasek. The company started out as a holding company for Singapore’s GLCs after independence, when there was a need for the government to play the role of catalyst for development of areas that lacked attractiveness for private sector investment (Hamilton-Hart, 2000 and Low, 2001). Its role has since been transformed into developing ‘the external wings of Singapore’s economy’ (Rodan, 1993).

The cases of Singapore’s Temasek and Malaysia’s Khazanah are interesting to analyze, as they have shown similar approaches to dealing with globalization in regard to governance of their GLCs: embracing an open economy as envisaged by the Washington Consensus, but with strong government intervention. However, it should be noted that despite majority government ownership, GLCs have fared considerably well thus far and account for about a quarter of total stock-market capitalization.

This recipe for government’s strong role is reflected in Temasek’s Charter (2002), which states: “Temasek will retain control of companies it is deemed critical to the economy – such as airport,

\[\text{For example, Tian and Oh (2004) discussed how, in the case of Malaysia, government intervention was even stronger at the onset of capital controls (i.e., it accepted neither unrestricted capital mobility nor the lifting of all barriers to entry for foreign companies, particularly banks).}\]
seaport and utilities— but will divest in companies which have no potential to grow beyond Singapore”. It also underlines that: “The government needs to own and control companies for various reasons. These include critical resources – where ownership or a resource is critical to Singapore’s security or economic well-being. The government also needs to have a controlling stake in companies that enable the government to achieve specific policy objectives by providing services for the public good”.

Critics sometimes conflate the continued dominance of the GLCs in the economy. However, it seems that the government has committed to divesting GLCs “which lack a strategic rationale or the potential to grow into regional or international players” and to ensuring “ministries and statutory boards . . . avoid spawning companies to provide services which private firms can provide, and crowding out the private sector” (Singapore Ministry of Trade and Industry 2003).

Thus, Temasek has recently started to divest some of its shareholdings. Therefore, while there is value in carefully allowing foreign competition and gradual privatization, the government realized that it is now vital for Singapore to privatize swiftly and become globally competitive.
In line with this understanding, the strategy taken is to phase out of the sectors deemed no longer strategic within the domestic realm, but expanding through cross border investments into prospective industries with higher returns. There are four major themes surrounding the investments: transforming economies, the thriving middle class, deepening comparative advantages, and emerging champions. These themes signify Temasek’s goal that its presence should not only be in the Singaporean economy, but across the globe, especially in Asia, where it is deemed to fit the theme and yield returns.

This is also reflected by the declining trend in the percentage of its domestic investments over the years. While there is a clear rise in its investment in North Asia (excluding Japan) and South Asia, Temasek’s exposure to OECD economies (not including Korea) is also declining. Interestingly, although also increasing, Temasek’s investments in ASEAN remained constant for two years within the period 2004 to 2007. With the challenges related to rising protectionism faced in Indonesia and Thailand\textsuperscript{19}, its focus on

\textsuperscript{19} Clear examples are the Shin Corp case in Thailand, arguably part of the series of events leading to the military coup ousting PM Thaksin Shinawatra, and investment in Indosat in Indonesia, which is subject to constant
ASEAN is now clearly centered on Vietnam, with the company having set up its representative office there. This is Temasek’s third representative office after the offices built in China and India, where Temasek is also dominant.

Figure 5.1 Trends in Temasek’s Regional Investments (Temasek Review 2004-2007)

*Board Structure as Measure of Corporate Governance Practice: Diversity and Transparency as a Consequence of Global Ventures*

With this global diversification strategy, it is obvious that the government should also encourage greater diversity within the resistance and pressure from the Indonesian interest groups based on nationalistic sentiments.
management of GLCs, which are currently still largely overseen by people with bureaucratic backgrounds. This has resulted in the recruitment of a number of foreigners to the boards of various Singapore GLCs, as well as to Temasek’s Board of Directors. Simon Israel, a New Zealander, was recruited to the board of Temasek’s directors, understandably to add to Temasek’s clout when venturing into international businesses.

Table 0-1 Temasek’s Board of Directors (Temasek Review, 2007)

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<th>No</th>
<th>Name</th>
<th>Current position outside the Board</th>
<th>Background</th>
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<tbody>
<tr>
<td>1</td>
<td>S. Dhana-balan</td>
<td>-</td>
<td>Government (former minister) and GLCs</td>
</tr>
<tr>
<td>2</td>
<td>Kwa Chong Seng</td>
<td>• Chairman &amp; Managing Director ExxonMobil Asia Pacific&lt;br&gt;• Board Member, DBS Group&lt;br&gt;• Public Service &amp; Legal Service Commission</td>
<td>Private sector</td>
</tr>
<tr>
<td>3</td>
<td>Sim Kee Boon</td>
<td>• Member, Temasek Advisory Panel and Temasek Trust&lt;br&gt;• Board, Fullerton Financial Holdings&lt;br&gt;• Advisor, Civil Aviation Authority Singapore/CAAS and Lum Chang Group</td>
<td>Government (civil servant), GLC (Keppel)</td>
</tr>
<tr>
<td>4</td>
<td>Koh Boon Hwee</td>
<td>• Chairman of DBS Group Holdings&lt;br&gt;• Chairman &amp; CEO, Sunningdale Tech</td>
<td>Private sector</td>
</tr>
<tr>
<td>No</td>
<td>Name</td>
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| 5  | Kua Hong Pak          | • Managing Director and Group CEO, ComfortDelGro Corporation  
• Deputy Chairman, SBS Transit and VICOM  
• Board member: PSA International, PSA Corporation, StarHub, Ringier Print (HK) Ltd and Cabcharge Australia                                                                 | Private sector                    |
| 6  | Goh Yew Lin           | • Executive Director, GK Goh Holdings, and independent Director of CIMB-GK Pte Ltd, Boyer Allan Management Ltd  
• Chairman, Yong Siew Toh Conservatory of Music and Deputy Chairman, Singapore Symphonia Company Limited (public service)  | Private sector (with public service appointment)                                                                                   |
| 7  | Teo Ming Kian         | • Permanent Secretary, Ministry of Finance and National Research and Development in the Prime Minister’s Office  
• Chairman, MND Holdings, Accounting Corporate Regulatory Authority, and Inland Revenue Authority of Singapore  
• Board Member, National Research Foundation and Monetary Authority of Singapore                                                                                         | Government                        |
| 8  | Simon Claud Israel    | • Chair, Singapore Tourism Board  
• Advisory Board, Lee Kong Chian School of Business Singapore Management                                                                                                                      | Private sector (multinational corporations in consumer goods industry)                                                            |
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<th>No</th>
<th>Name</th>
<th>Current position outside the Board</th>
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<tr>
<td></td>
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<td>University • Board of SingTel, Neptune Orient Lines, Fraser &amp; Neave, Fullerton Financial Holding</td>
<td>Civil service &amp; GLC (Singapore Technologies)</td>
</tr>
<tr>
<td>9</td>
<td>Ho Ching</td>
<td>Executive Director and CEO, Temasek Holdings</td>
<td></td>
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One should note that with Temasek being a government-owned investment holding company, the members of its boards with their formerly political backgrounds play a considerable role. As Worthington’s (2003) comprehensive analysis of governance in Singapore indicates, an embedded bureaucracy is the paradigm used by Singapore in governing each of its sectors. The concept of clear separation between state and society does not apply in Singapore, which also accounts for the relationship between the state and the private sector.

However, despite the hegemony of the state in the governance of Temasek and the GLCs, there is a growing perception that Temasek is increasingly commercially driven and relatively independent of
political interference\textsuperscript{20}. In the area of transparency, it is believed that economic democratization will always take place, regardless of the speed of political democratization\textsuperscript{21}. Hence, the Temasek Review, issued annually since 2004, has published the company’s accounts, established rules and governance procedures, even though this is not required under its status of exempt private company. Its web presence has also undergone a clear transformation, reflecting more openness to communication with the media by providing the names of contact persons for media relations. In terms of organizational structure, the transformation is even more obvious with the creation of the position of Managing Director for Corporate Affairs, to which Myrna Thomas, a former media personality, was appointed. Her primary task in that capacity is to effectively manage Temasek’s communications with its stakeholders\textsuperscript{22}.

Interestingly, the position was created just after its venture with Thailand’s Shin Corp was confronted with a political problem, which can arguably be considered one of the series of events, if not the

\textsuperscript{21} Author’s interview with Yeoh Lam Keong, Director of Economics and Strategy, Government of Singapore Investments Corporation (GIC), 12 January 2007.
\textsuperscript{22} “Temasek to polish image”. The Nation, 10 April 2006.
main trigger, that led to the political crisis in Thailand culminating in the military coup ousting PM Thaksin Shinawatra\textsuperscript{23}. Not only in Thailand has Temasek faced such political issues; there are also long-standing problems in Indonesia with regard to Temasek’s investment in Indonesia’s telecommunication operators Indosat and Telkomsel, even though it has frequently emphasized that the investments were made by ST Telemedia and SingTel, Temasek’s subsidiary companies. Allegations of monopolistic practice\textsuperscript{24} by price-fixing was just one of a series of attacks clearly aimed at Temasek by various interest groups in Indonesia, e.g., parliamentarians playing the nationalist card, labor unions worrying about their position and about employment, and local businessmen eyeing to take over ownership of the lucrative telecommunication operators. These groups were seeking either to reverse the 2002 takeover of Indosat by Temasek or to pressure Temasek into relinquishing ownership. Temasek’s argument was that it did not involve itself in any operational decisions of STT and SingTel as its


\textsuperscript{24} “Indonesia: Temasek accused of unfair business practices”, The Jakarta Post, 20 October 2006.
investee companies. This is also the case for Indosat and Telkomsel, the companies in which STT and SingTel hold shares.\(^{25}\) In both cases Temasek denied any wrongdoing, and in the case of Shin Corp, even Minister Mentor Lee Kuan Yew addressed the issue.\(^{26}\) While Temasek stated that it always operates commercially without its own government’s intervention, it has been extremely difficult for Temasek to shake off the stigma of Singapore, Inc., which is attached to all venture activities undertaken by Temasek and its companies.\(^{27}\) There is no doubt that Singapore-based transnational corporations, a majority of which are Temasek-linked companies, are strongly encouraged by the state to regionalize their operations (Yeung, 2000). Therefore, investments by Temasek in other countries, especially in neighboring ASEAN countries, are frequently perceived as serving the agenda and interests of the Singaporean government. Even on a global scale, protectionism


\(^{27}\) In an interview with the author on 14 September 2007, Myrna Thomas even argued that if Temasek’s international investment had indeed been coordinated by the Singapore government, the Shin Corp case would not have happened since they would have understood better the political context and the potential risks inherent in the context of Thailand.
against foreign investment by sovereign wealth funds is on the rise, something that Singapore’s PM Lee Hsien Loong acknowledged\textsuperscript{28}. Hamilton-Hart (2005) expresses it as a lesson on the need for incentives to adjust to doing business regionally in Asia. Citing the example of Suzhou Industrial Park in China which did not yield the expected level of success, Hamilton-Hart indicate that the international ventures undertaken by the Singaporean government have not always proceeded smoothly. Although Temasek has the best-trained and most experienced people, and has focused on human resource management as the key for capability development in a dynamic environment (Roberts and Dick, 2005), there are still lessons to be learned by the company in managing its international ventures. Communication with its stakeholders and managing its public image are starting to take a front row seat in Temasek’s strategy. The creation of Temasek Trust and Temasek Foundation\textsuperscript{29}, which will disburse funds and develop programs to improve the lives of people in the region, is seen as part of this strategy.

\textsuperscript{28} “PM Lee warns against protectionism”, ChannelNewsAsia, 10 September 2007.

\textsuperscript{29} “Temasek launches S$500m trust to aid Asia's development”, Channel NewsAsia, 16 May 2007.
A regionalization strategy is a necessity for Singapore and thus Temasek, especially given the issue of limited natural resources and the possibility of its market being saturated. Therefore, developing the external wings of the economy is imperative for Singapore. However, learning from its Indonesian and Thai ventures, an understanding of how to do business in the different contexts of other economies is critical and clearly still needs to be developed more fully. A sign of this better understanding has been shown in the company’s increased cautiousness regarding market corrections and growing protectionism.\(^{30}\)

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\(^{30}\)“No single deal will sink this ship”, Today, 3 August 2007.
Khazanah Nasional: Revamping GLCs as Malaysia’s Nation-Building Project

The success of Singapore’s Temasek Holdings in managing its GLCs has driven its closest neighbor to emulate its approach. Khazanah Nasional Berhad (Khazanah) was incorporated as an investment holding arm of its GLCs and is the investment holding arm of the government of Malaysia to manage its commercial assets. It is the trustee to the nation’s financial assets. Its objectives are to promote economic growth and, on behalf of the government, make strategic
investments which would contribute to nation-building. It was incorporated in September 1993 and began operations in 1994. It is structured into a holding company that is a wholly-owned entity of the Ministry of Finance (MOF), which is part of the Malaysian Government. Khazanah invested mostly in the fields of finance, telecommunications, utilities, communication services, information technology, and transportation. As of March 2005, it managed US$ 15.8 billion in assets, with a combined market capitalization of over US$ 50 billion\(^{31}\).

The fact that Malaysia also has a similar approach to Singapore in managing GLCs via a government-owned investment holding company provides Indonesia with even greater reason to admire the model and attempt to emulate it. Optimistic as the new Indonesian SOE minister may be with regard to emulating the success of a Temasek-style holding structure\(^{32}\), caveats must be mentioned with regard to the application of his master plan in Indonesia, especially considering the different contexts that Singapore and Malaysia have


\(^{32}\text{“Indonesia plans Temasek-style holding company”. Reuters, 31 May 2007.}
in comparison with Indonesia. Even between Singapore and Malaysia (at one time Singapore was part of Malaysia) differences exist, especially with regard to the political economy dimensions of the investment holding company as a state apparatus. The Singaporean government used Temasek Holdings first as a catalyst for economic development, especially in those sectors where private companies were reluctant to invest, and later as an investment vehicle in strategic sectors and regions to ensure Singapore’s survival in the face of limited domestic natural resources and a saturated market. Malaysia’s case is different from that of Singapore.

Khazanah Nasional Berhad (Khazanah) was formed in 1994 as the investment holding arm of the Malaysian Government. It was entrusted to manage the assets held by the government and to undertake strategic investments. It has stakes in more than 40 companies, with a combined market capitalization of more than RM150 billion (approximately USD40 billion), the net worth of Khazanah Investment Portfolio Performance as of 31 May 2006. Khazanah’s investments are in various sectors including finance,
telecommunications, electric utilities, communication services, information technology and manufacturing.

**Separation of Government’s Roles in Economic Management**

What has drawn interest to Khazanah’s role is the belief that the Malaysian government should be in business, just as the Singaporean government is with Temasek. The failure of the market, the necessity to deliver public goods, and the low level of equilibrium make state interventions imperative. Thus, in this context, it is important to differentiate the various roles government should have in business as regulator, developer, public goods provider, and investor. These roles are depicted in following diagram.
According to the Malaysian government, GLCs are defined as those companies which the government – federal or state – controls directly or through government-linked agencies. Under this definition, GLCs would fall under three categories:

1. where the government of Malaysia (GOM) exercises direct control through Khazanah, the Ministry of Finance (MOF) Inc., Kumpulan Wang Amanah Pencen (KWAP – the national pension funds) and Bank Negara Malaysia (BNM – the central bank)

2. where other federal government-linked agencies – Permodalan Nasional Berhad (PNB), Employee Provident Fund (EPF), Tabong Haji (the Moslem pilgrimage funds – exercise control (technically owned by depositors, but capital, and some income, portion guaranteed by GOM)

3. where state agencies exercise control – especially active are the states of Selangor, Johor, Pahang, Perak, Sarawak, Terengganu
GLCs under the Khazanah definition are limited to the first and second case.

On the spectrum between the market and state (diagram below), the GLC’s role should be in the middle. The common challenge should be how to drive performance in the absence of profit motive, which is clearly the case for SOEs. It is therefore important and interesting to consider how Khazanah manages its GLCs.

Figure 6.2 The Role of GLCs between Market and State According to Khazanah

Key principles of Khazanah's mandate as a strategic investment house include:
1. Creating sustainable value
2. Increasing national competitiveness
3. Cultivating a culture of high performance

These are to be achieved via four strategic initiatives:

1. Legacy investments: to streamline and restructure
2. GLC transformation: to increase shareholder and strategic value
3. New investments: to develop new markets and cross border investments
4. Human Capital Management: new management practices and reward systems

The Key Performance Indicators (KPI) measured for success are based on the three pillars of financial metrics, strategic value creation, and institution building

<table>
<thead>
<tr>
<th>... via four Strategic Pillars ...</th>
<th>and success measured by KPIs</th>
</tr>
</thead>
<tbody>
<tr>
<td>Legacy investments</td>
<td>Financial metrics as primary</td>
</tr>
<tr>
<td>Streamline, restructure</td>
<td>KPI: TSR and economic profit,</td>
</tr>
<tr>
<td>GLC transformation</td>
<td>ROE</td>
</tr>
<tr>
<td>Increase value: shareholder + strategic</td>
<td>Strategic value creation:</td>
</tr>
<tr>
<td>New investments</td>
<td>capability building in customer</td>
</tr>
<tr>
<td>New sectors, cross border</td>
<td>acceptance, sectoral and</td>
</tr>
<tr>
<td>Human Capital Mgmt</td>
<td>geographic exposure, market</td>
</tr>
<tr>
<td>Active leadership development</td>
<td>penetration, human and</td>
</tr>
<tr>
<td></td>
<td>knowledge capital, technology</td>
</tr>
<tr>
<td></td>
<td>Institution building: processes,</td>
</tr>
<tr>
<td></td>
<td>charter, systems and controls,</td>
</tr>
<tr>
<td></td>
<td>work culture, brand equity</td>
</tr>
</tbody>
</table>
Figure 6.3 Khazanah’s Strategic Initiatives and Key Performance Indicators (KPI)

It is important to also note why the Malaysian government has undertaken this path for the management of its GLCs. It is precisely because GLCs as a group have basically underperformed their peers in all measures except for their size. GLCs make poorer use of capital, with 11.3% of ROE in comparison to non-GLCs’ 13.7%. They are less productive, with 109,000 Malaysian Ringgit profit/employee ratios, in comparison to non-GLCs’ 127,000 Malaysian Ringgit. At 60%, GLCs also have a higher debt of equity ratio in comparison to non-GLCs’ 35%. An undertaking by Khazanah has helped improve the situation significantly, as demonstrated, for example, by the fact that its listed portfolio has increased by 18% in comparison to a rise of 8% of in the KLCI (Kuala Lumpur Capital Index).

Its role in the region has increased considerably in the past year. For example, Khazanah, just like Temasek, has also shown its influence in the Indonesian economy with its ownership of two major Indonesian banks: Bank Niaga and Lippo Bank. Unlike Temasek’s ownership of Indosat and Telkomsel, the acquisitions of these banks
have drawn little controversy. This might be due to the fact that a telecommunications company such as Indosat has been deemed more strategic and critical not only to the well-being of a country’s economy, but also to its national security. In analyzing the applicability of Temasek Holding’s model for the case of Indonesian SOEs, Malaysia’s Khazanah can serve as a case for comparison.

The GLC Transformation Program
Despite its incorporation in 1993, it was only in 2004 that Khazanah, together with other Malaysian GLICs and GLCs, really started to undertake serious measures to transform itself. A key reason for that was clearly the strong role of the then Prime Minister of Malaysia, Dr. Mahathir Mohammad, as the Chairman of the Board of Khazanah. It was only when there was a change of political leadership, with the election of the current Prime Minister Abdullah Badawi, that the transformation program took place.

On 14 May 2004, PM Abdullah Badawi identified the transformation of GLCs as a national priority and announced a set of initiatives to transform GLCs into high performance entities. These initiatives included establishing guidelines on performance-linked
compensation (PLC) and key performance indicators (KPIs), Board composition reform, the appointment of new CEOs for several GLCs, and the revamping of Khazanah. To sustain the momentum created by these early initiatives, the Putrajaya Committee on GLC High Performance (PCG) was established in January 2005. Given the critical position and role that GLCs have in the nation’s economy and the potential benefit of their enhanced performance, the PCG launched a structured GLC Transformation Program (GLCT) on 29 July 2005 and designated Khazanah as Secretariat to the PCG. This program was built upon the three underlying principles of national development, performance focus, and good governance. Based on five key policy thrusts (Figure 4.4.) and ten strategic initiatives (Figure 4.5), the objective of the program was to design and implement comprehensive national policies and guidelines to catalyze the transformation of GLCs into high performing entities.

<table>
<thead>
<tr>
<th>Underlying principles</th>
<th>Policy thrusts</th>
<th>Initiative design &amp; implementation</th>
</tr>
</thead>
<tbody>
<tr>
<td>National Development Foundation</td>
<td>Policy Thrusts set the framework to the principal agents for change at the GLC level, GLC Board, and GLC level</td>
<td>• Ten Initiatives were identified to be developed, and launched by PCG and implemented by GLCs (based on their corporate strategies)</td>
</tr>
<tr>
<td>Performance Focus – create economic and shareholder value through improved performance at GLCs. Driven by principles of developmental meritocracy</td>
<td>1. Clarify the GLC mandate in the context of national development</td>
<td>• The Initiatives were identified and developed on the basis of their importance as levers of change and their potentially large impact on value</td>
</tr>
<tr>
<td>Governance, Shareholder Value and Stakeholder Management</td>
<td>2. Upgrade the effectiveness of Boards and reinforce the corporate governance of GLCs</td>
<td>• Some Initiatives aim to create an enabling environment, while others are provided as tools for internal improvement of GLCs</td>
</tr>
<tr>
<td></td>
<td>3. Enhance GLC capabilities as professional shareholders</td>
<td></td>
</tr>
<tr>
<td></td>
<td>4. Adopt corporate best practice</td>
<td></td>
</tr>
</tbody>
</table>
**Figure 6.4 Overview of the GLC Transformation Programme: Five Key Policy Thrusts (PCG Progress Review, 2006)**

<table>
<thead>
<tr>
<th>No</th>
<th>Initiatives</th>
<th>Description</th>
<th>Output</th>
<th>Launch Date</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Enhancing Board Effectiveness</td>
<td>To enhance board effectiveness through revamping board practices and processes</td>
<td>Green Book</td>
<td></td>
</tr>
<tr>
<td>2</td>
<td>Strengthening Directors’ Capabilities</td>
<td>To develop a strategy to match directors to the right boards and to establish a Directors Academy</td>
<td>Directors Academy</td>
<td>Dec '06</td>
</tr>
<tr>
<td>3</td>
<td>Enhancing GLC Monitoring &amp; Managing Functions</td>
<td>To reinforce the ability of GLC’s to monitor and manage individual GLC’s</td>
<td>Blueprint for GLC’s</td>
<td>Dec '06</td>
</tr>
<tr>
<td>4</td>
<td>Improving Regulatory Environment</td>
<td>To enhance regulatory capabilities at GLC's and create a Regulatory Knowledge Network</td>
<td>Programme for Managing Regulatory Environment</td>
<td></td>
</tr>
<tr>
<td>5</td>
<td>Achieving Value Through Social Responsibility</td>
<td>To guide GLC’s to become responsible corporate citizens while creating value for their shareholders and stakeholders</td>
<td>Silver Book</td>
<td></td>
</tr>
<tr>
<td>6</td>
<td>Reviewing and Revamping Procurement Practices</td>
<td>To enhance the effectiveness and efficiency of the procurement processes in GLC’s</td>
<td>Red Book</td>
<td></td>
</tr>
<tr>
<td>7</td>
<td>Optimising Capital Management Practices</td>
<td>To establish guidelines for GLC’s to optimise their capital structure</td>
<td>Purple Book</td>
<td></td>
</tr>
<tr>
<td>8</td>
<td>Strengthening Talent Management Practices</td>
<td>To improve GLC’s capabilities in attracting, developing and retaining talent</td>
<td>Orange Book</td>
<td>Dec '06</td>
</tr>
<tr>
<td>9</td>
<td>Intensifying Performance Management Practices</td>
<td>To encourage adoption of performance management best practices at GLC’s</td>
<td>Blue Book version 2</td>
<td></td>
</tr>
<tr>
<td>10</td>
<td>Enhancing Operational Efficiency and Effectiveness</td>
<td>To enhance operational efficiency and effectiveness through the adoption of a framework for continuous improvement</td>
<td>Programme on the Framework for Continuous Improvement</td>
<td></td>
</tr>
</tbody>
</table>

**Figure 6.5 Overview of the GLC Transformation Programme: Ten Strategic Initiatives (PCG Progress Review, 2006)**
These guidelines were codified in a transformation manual launched in July 2005 and through specific guidelines on individual initiatives. Upon establishing an institutional framework, PCG, via Transformation Management Office (TMO), was responsible for program management and overseeing the design and execution of these policies and guidelines.

At the time the interview was conducted at Khazanah, it had been nearly two years since PCG’s formation. A progress review was undertaken to assess progress, evaluate its impact, and identify challenges. In doing so, the program was able to be and can later be improved to ensure a more rapid realization of objectives.

Board Structure as a Measure of Corporate Governance Practice: Government Control in the GLC Transformation Program

GLC transformation is critical to Malaysia, since its GLCs generally underperform in comparison to their private sector counterparts, despite their roles as:

- a significant part of the economy, constituting 54% of market capitalization in KL Composite Index and 5% of the workforce;

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33 Interview with Ahmad Shahizam Mohd Shariff, Senior VP at Managing Director’s Office in Charge of Communication, Khazanah Nasional Berhad.
• a provider of strategic utilities (e.g., public transport, water) and services (e.g., telecoms, airlines, banking);

• an executor of industrial policy and development (e.g., automotive and semiconductors);

• builders of international linkages by conducting foreign ventures and investing in new growth sectors, and;

• a developer of the Bumiputera community by developing human capital and suppliers.

The Putrajaya Committee on GLC High Performance (PCG) was formed in January 2005 to follow up on and catalyze the GLC Transformation Program. PCG is chaired by the Second Finance Minister, with participation from the heads of the GLICs: Khazanah, PNB, EPF, LTAT, LTH and representatives from the Ministry of Finance Inc. (MOF) and the Prime Minister’s Office, to work together to monitor developments and recommend further measures for improvement. The Transformation Management Office (TMO) was established at Khazanah, the Secretariat to the PCG. This TMO is responsible for managing the roll-out and implementation of the 10 initiatives proposed in the GLC Transformation Program.
The GLC transformation is being undertaken with the underlying principles of national development foundation, performance focus, and corporate governance with regard to shareholder value and stakeholder management. A critical element with respect to the issue of corporate governance is the board. Upgrading board effectiveness and reinforcing corporate governance at GLCs are elements of one of the policy thrusts in GLC transformation.

Before we talk about policy thrusts for improving board effectiveness at the GLCs, it is important to look at Khazanah’s Board of Directors, composed of government representatives, with the Prime Minister himself serving as the Chairman of the Board. Of the eight members of the current board, three are from the government. Apart from the Prime Minister, who is also the Minister of Finance, the Second Minister of Finance and the Governor of Bank Negara Malaysia also sit on the board. The remaining five members of the board come from the private sector.
### Table 0-1 Khazanah’s Board of Directors (Khazanah, 2007)

<table>
<thead>
<tr>
<th>No</th>
<th>Name</th>
<th>Position outside the Board</th>
<th>Background</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Dato’ Seri Abdullah Bin Haji Ahmad Badawi (Chairman of The Board)</td>
<td>Prime Minister</td>
<td>Government (politician)</td>
</tr>
<tr>
<td>2.</td>
<td>Tan Sri Dato’ Nor Mohamed Yakcop</td>
<td>Second Minister of Finance</td>
<td>Government (bureaucrat)</td>
</tr>
<tr>
<td>3.</td>
<td>Tan Sri Dato’ Sri Dr. Zeti Akhtar Aziz</td>
<td>Governor of Bank Negara Malaysia</td>
<td>Government (technocrat)</td>
</tr>
<tr>
<td>4.</td>
<td>Tan Sri Md Nor Yusof</td>
<td>Chairman of Khazanah Executive Committee</td>
<td>Private sector</td>
</tr>
<tr>
<td>5.</td>
<td>Dato’ Mohammed Azlan bin Hashim</td>
<td>Chairman of Proton Holdings Berhad</td>
<td>Private sector</td>
</tr>
<tr>
<td>6.</td>
<td>Dato’ Mohammed Azman bin Yahya</td>
<td>Advisory panel of Bursa Malaysia</td>
<td>Private sector</td>
</tr>
<tr>
<td>7.</td>
<td>Raja Datuk Arshad Raja Tun Uda</td>
<td>Member of the Capital Market Advisory Council</td>
<td>Private sector</td>
</tr>
<tr>
<td>8.</td>
<td>Dato’ Azman bin Haji Mokhtar (Managing Director)</td>
<td>Managing Director of Khazanah Nasional Berhad</td>
<td>Private sector</td>
</tr>
</tbody>
</table>

The composition delineated above signals that the government indeed plays a role in managing the GLCs. However, in the context
of corporate governance through a holding structure, the government should not micro-manage GLCs. In fact, this has been described as one of the key success factors for managing GLCs under the holding structure. In a nutshell, the Malaysian experience shows that the key success factors in governing GLCs are:

- Clear and specified role of the government (policymaker and regulator, but not investor), Khazanah (macro-manage as strategic investor) and GLCs (micro-manage in each respective company based on)
- Clear key performance indicators (KPIs) to target, measure, and evaluate the performance of GLC managers, who at the end of the day have to make commercial sensible decisions and deliver shareholder value
- Corporate Social Responsibility (CSR) as the key initiative in meeting stakeholder expectations; however, that needs to be put in the context of the profitable management of corporations. The

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34 Summarized from author’s interviews with Dato’ Dr. Michael Yeoh (ASLI) and Ahmad Shahizam Shariff (Khazanah) on 8 and 9 February 2007 respectively.
importance put on CSR is evident in Khazanah’s sitting on the advisory panel of CSR Malaysia.\(^{35}\)

However, all of the above must be put in the specific context of Malaysia, where the development of Bumiputera’s entrepreneurs as human capital is the basis for the creation, development, and transformation of GLCs.

**The New Economic Policy and 9th Malaysia Plan**

A unique political economy background with the New Economic Policy (NEP) as the basis of policy-making has provided the foundation for the GLICs and GLCs in Malaysia.\(^{36}\) With the race riots of 1969 in mind, the ruling elite came to a consensus that an affirmative action policy was necessary to provide a distribution of wealth among the ethnic groups in Malaysia.\(^{37}\) Together with four

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\(^{35}\) Author’s interview with Paul Chan, Secretary General of Malaysian Institute of Corporate Governance (MICG), 17 January 2007.

\(^{36}\) Lim Teck Ghee discussed this in his seminar on Malaysian Economy and Society: One Step Forward, Two Backwards? at the Institute of Southeast Asian Studies on 27 February 2007. He argued however that Malaysian GLCs are part of the so-called “Four Distributional Coalitions” of the political, bureaucratic, military, and religious elites, which have overlapping membership and are in fact multi-racial.

\(^{37}\) Author’s interview with Dato’ Dr. Michael Yeoh, CEO/Director of Asian Strategy & Leadership Institute (ASLI), 8 February 2007.
other government-linked investment companies (GLICs)\textsuperscript{38} in Malaysia, Khazanah serves as the principal vehicle to enhance Bumiputera’s participation in the corporate sector, particularly through equity participation\textsuperscript{39}. Indeed, there has been a shift of equity participation so that domestic capital is no longer overwhelmingly the domiciled ‘Chinese capital’ of pre-NEP days, but a conglomerate-dominated national capital whose ranks have been filled, however imperfectly, by capitalist segments from the Malay community (Khoo, 2007).

Under the leadership of PM Mahathir Mohammad, a ‘strong man’ with centralized decision-making authority and initiatives, there was however little need\textsuperscript{40} to institutionalize the framework for decision-making at Khazanah. In fact, strategic decisions related to Khazanah were never taken at Khazanah itself, but rather were driven by the ‘proactive’ leadership of Mahathir, because the Prime Minister is also the Chairman of Khazanah’s Board of Directors.

\textsuperscript{38} Employees Provident Fund (EPF), Permodalan Nasional Berhad (PNB), Lembaga Tabung Amanah Angkatan Tentera (LTAT) and Lembaga Tabung Haji (LTH).
\textsuperscript{39} As mentioned in The 9\textsuperscript{th} Malaysia Plan: 227, 10.13.
\textsuperscript{40} Author’s interview with Ahmad Shahizam Mohd Shariff, Senior Vice President in Managing Director’s Office in charge of Communication, Khazanah Nasional Bhd., 9 February 2007.
Over the years, the GLCs have grown to a size that has vastly surpassed their immediate post-colonial scope. Through Danamodal and Danaharta, EPF, PNB (tasked with acquiring equities on behalf of indigenous groups), Petronas (the national petroleum company), Ministry of Finance Inc., and Khazanah, the state came to be the largest holder of listed firms in the region after the governments of China and Singapore (EAU, 2002: 136). It should be noted, however, that such vast state ownership is often looked upon critically.

However, the Asian crisis of 1997-1998 fundamentally affected the state’s ability to govern the market in the East Asian developmental state model, with challenges posed by globalization. After the financial crisis, with new doctrines in place, reforms began with the GLCs, most notably the telecommunications and energy utilities, Telekom and Tenaga (Case, 2003). By introducing what was now regarded as corporate best practice, the positions of board chairman and chief executive officer were separated (EAU, 2002: 142).

Similarly, state agencies that held listed assets, whether to

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41 In 2005, the GLCs accounted for 36% of the Malaysian Exchange’s total market capitalization and 5% of the national labor force (Anna Taing, 2005. ‘Acid test for GLC transformation’, The Edge, 8 August 2005).
rehabilitate the interests of those Malay business elites who had been ousted, to undertake cross-ethnic redistribution, or to fulfill developmental visions, began in some instances to increase their holdings and then reform their management structures. The GLC Transformation Program, led by the PCG (Putrajaya Committee on GLCs High Performance), is currently the main issue on the government’s agenda with respect to revamping the GLCs.

GLCs are major players in the Ninth Malaysia Plan (9MP). The recently announced 9MP has laid down an ambitious plan, distinguished by its goal of accelerating growth through efficiency gains and emphasis on enhancing human capital and service delivery, while also addressing redistributive issues. A major aim is to enhance competitiveness for sustainable, broad-based growth. To achieve this, five major thrust were enshrined in the 9MP, and it is expected that GLCs, by virtue of their being vital engines of national economic growth, will be instrumental in ensuring the implementation and success of the 9MPs. Some of the immediate beneficiaries encompass sectors such as agriculture, property and infrastructure, e.g.: Iskandar Development Region, and
biotechnology. A brief summary of present and potential GLC involvement in the context of the five thrusts is illustrated below.

Figure 6.6 Relationship of GLC Transformation Programme and the 9th Malaysia Plan (PCG Progress Review, 2006)
Figure 6.7 Khazanah’s Investment Holding Structure
(Khazanah Website, 31 August 2007)
Corporate Governance of Indonesian SOEs: Building an SOE Holding Company in the Direction of Indonesia Inc.

The Indonesian government has been struggling to find ways to manage its over 100 state-owned enterprises (SOEs). Only in his last administration did the long-time New Order leader Soeharto realize that there must be a concentrated strategy to bring out the potential of the SOEs, long known only for being inefficient, mismanaged, and cash cows for political groups and individuals. The democratization that came with the fall of Soeharto and the New Order era has brought pressure in terms of economic logic and political necessity for Indonesian SOE reform. At the same time, however, democratization has also made the reform process less easy, as more groups of stakeholders can have a say in the process.
The performance of Indonesian SOEs has drawn criticism due to their low profitability, especially in terms of the Return on Investment (ROI), in comparison with their counterparts in the private sector. Indonesian SOEs are also prone to corrupt practices, which poses a different set of potential problems. Agency theory (Jensen & Meckling, 1976) would lead one to argue that the problems at SOEs derived from the lack of an ultimate principal, though the state should be, in theory, the owner of SOEs. This situation is more problematic, as the control of the state over strategic natural resources is mandated by the constitution. The Indonesian government under President Yudhoyono and Vice President Kalla has vowed to improve SOE performance, but satisfactory results have yet to be seen. Programs for the enforcement of good corporate governance (GCG) and a master plan for SOEs, dubbed the rightsizing program, under which SOE numbers will be gradually reduced, are underway.

Neoliberal doctrine perceives the ownership of companies by the state as suboptimal, if not destructive, for companies’ value. Therefore, the privatization of SOEs is seen not only as a means of generating revenue for the state budget, which seems to be the
primary aim of the Indonesian government, but also of steering SOEs into market discipline by functioning as a driver for efficiency. In much of the privatization process in Indonesia, the role of foreign parties has been quite significant in acquiring SOE shares divested by the Indonesian government. The main reason is that after the crisis, not many of the big Indonesian businesses, especially the conglomerates most severely hit by the crisis, had the capital necessary to acquire the divested shares.

However, the view of economic nationalism seems to be dominant in Indonesia's response to globalization. It is especially prevalent since Article 33 of Indonesia’s 1945 Constitution states that “Sectors of production that are important for the country and affect the life of the people shall be controlled by the State” (point 2) and “The land, the waters and the natural riches contained therein shall be controlled by the State and exploited to the greatest benefit of the people” (point 3). The above article serves as the principal argument for economic nationalists who oppose foreign ownership in certain
sectors such as telecommunications. The case of Indosat is a good example of this phenomenon. By contrast, the performance of government-linked companies (GLCs) in neighboring Singapore and Malaysia shows that SOEs can be profitable and excel in global business by functioning as investment houses actively seeking opportunities overseas, mainly in Asia. Business expansion by Temasek Holdings, the Singaporean government’s investment holding company controlling GLCs, and Khazanah Nasional Berhad, a similar holding owned by the Malaysian government, showcase the success of Southeast Asian SOEs. In managing the economy, the government has three critical roles: developer and public goods provider, regulator, and investor seeking profits for the state. The investment holding companies serve as a means to separate the tasks of the profitable management of enterprises belonging to the state and social-incentives-driven public services. As strategic investors and government-linked investment companies (GLICs), Temasek and Khazanah also seek to make strategic investments on behalf of their governments in new

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industries and markets. It is in this respect that the GLICs expand to new sectors and countries beyond their territorial boundaries.

Problems facing Indonesian SOEs will be elaborated on in greater detail in the next section. In the following, I will discuss several issues which are at the heart of three main challenges facing SOE governance:

1. **Conflicting Objectives**

SOEs tend to have conflicting objectives because they are usually mandated by the constitution and enforced by legislation or different government agencies. SOEs tend to have not only commercial objectives, just as private sector firms do, but also social objectives such as providing jobs, serving public interests, and providing basic necessities. These multiple goals make it harder to judge SOEs’ success, in comparison to private sector firms, which usually have clear financial performance targets as measures of success. Differing government agencies will also seek to gain control of programs if these objectives are met by SOEs, which sometime leads to conflict,
as each government agency also has its own objectives mandated by the public.

One example is the recent case of the Indonesian PLN’s (Perusahaan Listrik Negara – Indonesian state provider of electric power) plan to raise the electricity base rate due to an increasing amount of subsidy it has to bear. The plan catalyzed protest and resistance from the public and businesses and was especially heavily criticized by the parliament. On the one hand, PLN has little choice, as the energy supply is steadily decreasing while energy consumption keeps rising with the growth of industrialization. On the other hand, it is legitimate for the public to demand that PLN serve its interest, as is mandated by the 1945 constitution: “Earth and all its resources underneath is under state control and must be utilized for the maximum welfare of the people”\(^43\).

2. Agency Issues (Political Interference)

The above situation becomes worse when the legislators or government officials who are supposed to oversee the SOE

\(^43\) Article 33, Section 3 of the Undang-Undang Dasar (UUD) 1945, the Indonesian constitution drafted and passed on August 18\(^{th}\) 1945.
managers push their own personal or political interests on them. The state and, in terms of capital providers, the people as taxpayers, are the actual owners of the SOEs and thus considered to be the principal from the perspective of agency theory. However, these ‘principals’ have difficulty looking after their own interests in SOEs. Given the condition mentioned above, politicians and bureaucrats are typically poor overseers of SOEs, and thus are not suited to serve as principal on behalf of taxpayers. As ordinary people, they are self-interested individuals who seek to attain and maintain power. As politicians, they sometimes also have to serve the interests of the political party, faction, or lobby groups which brought them to power as compensation for their vote. Instead of being impartial in order to serve the needs of the people, they are driven by certain groups toward meeting their (the groups’) needs. They also lack interest in seeing that SOEs perform profitably, as they do not benefit financially or otherwise from it. On the contrary, they will be blamed if SOEs undertake commercial measures that might be not popular, such as laying off employees when the circumstances require it. This exacerbates the condition of multiple objectives, as the overseer is accountable for specific performance
targets but at the same time has the opportunity for intervention to satisfy political needs. Instead of acting as principal on behalf of the taxpayers, they become ‘agents of government agencies’ in undertaking their oversight role.

An example of this problem in Indonesia is the privatization of certain SOEs by the Ministry of State-Owned Enterprises (SOEs) in 2003. The Ministry of SOEs was mandated by the government to privatize a number of SOEs in order to fill gaps in its government budget. On the other hand, parliament was very critical of this undertaking since politicians were toying with nationalistic ideas and deemed such privatization as a selling-off of state assets. The problem was exacerbated by the involvement of government officials in the ministry in irregular dealings during the transaction of the privatization itself, as the ministry officials were also political party officials who were tasked with filling the party coffers to gear up for the 2004 election.  

3. Lack of Transparency

The case of the Indosat sell-off is still under scrutiny, due to improper dealings which are believed to involve top government officials, including the former Minister of SOEs.
The last challenge SOEs have is the lack of transparency in the face of insufficient external scrutiny. Many countries do not provide enough information on the business results of SOEs, or the information provided is unreliable. There is also sometimes a lack of communication by the government regarding its objectives and its plan to monitor and influence the pursuit of those objectives. It is certainly unfavorable for the public as principal, as they need to have a clear picture of how their interests are being taken care of. It might be that the lack of transparency is intentional, since it favors politicians and bureaucrats whose self-interest in the business of SOEs will then remain unexposed.

The reform of Indonesia’s Financial Accounting System (Rosser, 2005) provides clear evidence of this problem. Strongly driven by the changes in oil prices in the late 1980s, which caused the politico-bureaucrats to undertake measures demanded by international mobile capital controllers such as the IMF and the World Bank in order to invite foreign investment, the reform was able to be pushed through by technocrats in the government. However, the implementation and enforcement of the accounting reform, which included a higher degree of openness, especially with regard to the
quality of financial reports, was never vigorously pursued. The major auditing firms, particularly Arthur Andersen, which was later also involved in Enron’s downfall, cultivated strong links within the Ministry of Finance to secure political protection (Backman, 2002).

**Corporate Governance Problems at Indonesian SOEs**

Indonesia does not represent an especially extreme case of the dominance of SOEs in comparison with China (where SOEs controlled 57% of industrial assets and employed half of China’s 750 million workers in 2003); however, the number of SOEs in Indonesia is also high, given that the SOEs in Indonesia were founded approximately 50 years ago by the Indonesian government to fulfill two goals (Purwoko, 2002):

1. Economic goal: Fully managing ‘strategic’ business sectors (mainly oil & gas, electricity, and other utilities, etc.) as is mandated by the constitution. The rationale behind this goal is to ensure that the public will be equally served and given equal

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45 (Desvaux, Wang & Xu, 2004).
access to resources, something that was considered doubtful under a free market regime.

2. Social goal, in the form of job creation and local economic development: This goal is meant to be achieved by empowering small and medium-sized enterprises in the immediate vicinity of the SOE to take part in the value chain creation.

The fulfillment of these two goals is the concern of the government as the principal.

Unfortunately, the performance of Indonesian BUMNs has been disappointing to date. In 2004, only 59 of 158 BUMNs were able to provide dividends to the government, while 46 BUMNs recorded losses during 2003-2004. A total dividend of IDR 9.1 trillion (USD 980 million) was collected in 2004. This figure demonstrates the shocking inefficiency of many BUMNs, especially when one looks at the number of loss-making BUMNs. Some of the causes of these inefficiencies can be traced back to poor corporate governance practices, especially with regard to the monitoring and controlling of BUMN management boards, which is essential in preventing the corrupt behaviors that lead to inefficiency.

However, if we view the situation of corporate governance at SOEs from the agency theory perspective, the actual problem lies in defining who the principal is. The phrase ‘state-owned’ implies that the state, the Republic of Indonesia, enjoys full rights of ownership of the enterprises. The Indonesian people, as the holder of highest sovereignty in the republic, give the mandate to the Indonesian government, as the owner of the SOEs, to be the principal. Problems arise when it comes to the issue of monitoring and controlling an SOE’s management board, as the agent in charge of executing the interest of the principal. It is difficult to find a governmental body which is supposed to have solely the interests of the Indonesian people at heart and to then assign it the tasks of monitoring and controlling Indonesian SOEs.

Indonesian SOEs are governed under the structure of the Ministry of SOE, which is a governmental body with bureaucratic character. The representatives of the ministry always sit on the Board of Comissioners of the SOEs. The role of the Ministry’s representatives on the Board of Comissioners is to ensure that the behavior of an SOE’s management board is aligned with the interests of the state as principal. However, it is difficult to
guarantee that the Ministry is an appropriate and interest-free body that can represent the principal in the context of agency theory. In fact, past experience shows that many of the ministry’s officials have misused or been misused as ‘agents’ to raise funding for the political parties in control of the ministry or for individuals seeking financial benefits as well as to strengthen their position and power in the government. 47

It is difficult for the Ministry of SOEs to ensure that its monitoring role reflects the SOEs commitment to the economic and social goals in the form of:

- maximizing long-term shareholder return for the state as the principal, since an enterprise in any form is an economic institution seeking profitable return, and not acting as a social agency (although as a state-owned enterprise, it has non-profit goals as well)

- serving the needs of public sectors, especially with regard to the use of strategic resources belonging to the state, which are to be managed for the good of the Indonesia people, as mandated by the constitution.

The appointment of a Minister of SOEs who comes from a political party might have the consequence that s/he has an interest in staying in power for the next legislative period. Lane (2003) mentions that such political self-interest is one of the private incentives that also figures into the equation. This situation can develop to the point that the Ministry will be somehow driven by interests other than the above-mentioned main goals of an SOE. There is growing pressure, within the current government, for the Ministry of SOEs to be put under the leadership of a professional, non-partisan figure. That might serve as a good starting point for the Ministry of SOEs to break free of conflicting interests. However, it is still difficult to ensure that the government, which is controlled by a political party or coalition, will not exert its influence on the non-partisan figure in the governments to act in favor of the ruling party or coalition.

The Indonesian House of Representatives, the Parliament, consists of representatives of the different political parties who champion differing ideologies, views, and interests. It is even harder to rely on this body to be independent and interest-free enough to conduct controlling and monitoring on behalf of the principal. The Indonesian constitution also regulates the existence of government
institutions. These regulatory bodies are the Agency for Financial Audit (Badan Pemeriksa Keuangan, abbreviated BPK, in the Indonesian) and the Agency for Financial and Development Supervision (Badan Pengawas Keuangan dan Pembangunan, abbreviated BPKP) and have the authority to conduct supervision and financial audits of the BUMNs and governmental agencies. However, the role of the BPK has an auditing function, that is, it serves as a post-activity check or an end-gate for the corporate governance framework. However, it does not entail all of the corporate governance pillars, which include the aspects of risk management, internal audit, external audit, and the corporate governance structure itself.

In the end, any government body is full of agents with their own interests and thus cannot be regarded as the principal. Gaining momentum is the skeptical view that any control system for the monitoring of SOEs, no matter how sophisticated it might be, will be doomed to fail due to inter-agents acting with conflicting interests. This poses a dilemma for Indonesia, especially within the framework of the currently heightening public debate over privatization. The debate revolves around the issue of whether the
privatization program that the Indonesian government is currently undertaking is actually the best way to solve the BUMN problem of inefficiency. The program is facing strong resistance from Indonesian society since it is perceived as a process of selling-off state assets and strategic resources. The privatization of these SOEs is seen as a possible solution to their efficiency problem and may help to avoid the possible conflict of interests arising between various parties managing and having vested interests in SOEs. Thus, it is sometimes tempting for us to ask whether it is really necessary at all for governments to have firms that manage their strategic resources. Questions also arise about whether privatization a la Thatcherism in Great Britain in the ´80s can be the right solution to the governance problems of state-owned enterprises. This poses a dilemma for Indonesia, especially with respect to the currently heightening public debate about whether the privatization program that the Indonesian government is currently undertaking is actually the best way to solve the problems of BUMN inefficiency. Coupled with that issue is also strong resistance to the program on the part of the general society since the process is perceived as a selling-off of state assets and strategic resources.
However, before employing the Thatcher solution too quickly and losing the potential of SOEs to create value and grow prosperously, we have to examine carefully and discuss empirical cases in which a state-owned enterprise shows evidence of good corporate governance practice or even the best practice in Asia. This best practice is based on principles focusing on sound corporate governance as an important pillar of an ongoing commitment to achieving long-term shareholder value through corporate excellence and sustainable growth. Therefore, it is important to highlight the master plan of the Indonesian government to group its SOEs into a holding structure along the lines of Temasek Holdings which should later serve as the holding company for Indonesian SOEs.

**Indonesian SOEs: Contemporary Issues in Corporate Governance**

This section aims at analyzing the situation of Indonesian SOEs, the challenges they are facing in implementing good corporate governance (GCG), and the master plan by the Indonesian government to restructure, ‘profitize’ and privatize its SOEs. Taking political changes and globalization into account, a special focus is
placed on the plan to set up a national holding company for SOEs which is aimed at emulating the style of government-owned investment holding companies such as Temasek Holdings in Singapore and Khazanah Nasional in Malaysia. A strategy that has been mapped out since 1998, the master plan seemed to be making significant inroads in 2007, but cautiousness in relation to political complexity must be considered in the discussion.

It is also important to review the privatization process that occurred within several SOEs in 2007. Although none of them was undertaken with a strategic sale, as in Indosat’s case, and thus were much less politically controversial, it is important to assess the level of maturity and the political economic dynamic of the privatization process in Indonesia. In 2007, a number of companies privatized via public offerings, making them less subject to nationalistic sentiments compared to strategic sales.

Finally, it is also imperative to highlight leadership changes at the helm of the Indonesian State Ministry for State-Owned Enterprises (MSOE). Having transferred from the position of Minister for Communication and Information, Dr. Sofyan Djalil is the fifth person to hold the position of State Minister for State-Owned
Enterprises within an 8-year timeframe. This chapter will begin with a brief historical summary of the leadership changes and what political implications they have had, especially in relation to the goal of replacing the MSOE with a national holding company for Indonesian SOEs.

**Indonesian Minister of SOEs: Leadership Changes amid Political Democratization**

The appointment of Sofyan Djalil as the new minister for SOEs seems to have resulted in a number of breakthrough decisions with regard to the management of Indonesian SOEs. His statement that newly appointed directors of SOEs would not automatically serve the 5-year term, as had been the case previously, but would be subject to a 1-year probationary period instead, is the latest in a string of measures aimed at establishing stringent discipline and a strong work ethic at the SOEs. In line with good corporate governance practices, the current key jargon of the ministry, these SOE directors are to be assessed by a set of key performance

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48 Wicaksono, Agung: “Learning from the success of Temasek, Khazanah”, The Jakarta Post, 9 July 2007 has also discussed part of this section.
49 “Direksi BUMN Baru Dikenai Masa Percobaan 1 Tahun” (New SOEs Board To Get 1-Year Probation), Detikfinance.com, Tuesday, 26 June 2007.
indicators (KPIs) aimed at boosting SOEs’ performance, known to be poor compared to their private sector peers. According to Sofyan, the ministry would also seek capable and experienced individuals from the private sector to serve as members of the Board of Comissioners at the SOEs. These professionals are expected to inject credibility, independence, and professionalism into SOEs by controlling the performance of the directors. However, the idea of hiring experts to the board based on professionalism regardless of nationality still faces the challenge of nationalistic sentiment and has been regarded as ‘just a discourse’.  

On privatization, the most politically sensitive issue related to SOEs, Sofyan intends to increase the number of SOEs to be privatized.  

Fifteen SOEs are planned for privatization in 2007, with toll-operator Jasa Marga, Bank Negara Indonesia (BNI) and construction company Wijaya Karya being the priorities for that year. Sofyan also said that he would make whichever SOEs make into public

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50 “Angkat WNA Hanya Wacana” (Hiring Foreigner Just an Idea), Kompas on Tuesday, 26 June 2007.
51 “Privatisasi BUMN Diperbanyak” (More SOEs To Be Privatized), Detikfinance.com on Monday, 14 May 2007.
companies that he could\(^5\). The government has decided to slash the number of its 139 SOEs in half by 2009\(^5\) through merger, divestment and liquidation. A decision to further slash the number to 50 by 2012 or 25 by 2015 is also in part of the plan, which has been dubbed the ‘rightsizing’ scenario.

**Table 0-1 Indonesian SOEs Rightsizing Scenario (MSOE 2007)**

<table>
<thead>
<tr>
<th>Year</th>
<th>Number of SOEs</th>
</tr>
</thead>
<tbody>
<tr>
<td>2006</td>
<td>139</td>
</tr>
<tr>
<td>2007</td>
<td>102</td>
</tr>
<tr>
<td>2008</td>
<td>87</td>
</tr>
<tr>
<td>2009</td>
<td>69</td>
</tr>
<tr>
<td>2012-2015</td>
<td>50</td>
</tr>
<tr>
<td>&gt;2015</td>
<td>25</td>
</tr>
</tbody>
</table>

For many within the circle of Indonesian business and politics, these steps come as no surprise. First of all, Sofyan has a strong capital market background. An Acehnese with an undergraduate degree in business law, Sofyan then went to study at Tufts University, Massachusetts, USA, for two master’s degrees, in public policy and


\(^5\) “Jakarta To Halve Number of State Firms”, The Straits Times, Singapore, 21 February 2007.
law and diplomacy, and a Ph.D. in international financial and capital market law and policy. Since then, he has been a professional, managing his own consulting firm and advising various SOEs on issues related to GCG, and an academic, teaching at various universities. In short, he should have the right training and the appropriate experience for the job.

Secondly, he is one of the few non-politicians in President Susilo Bambang Yudhoyono’s cabinet. Of the 36 ministers in the current cabinet (dubbed the United Indonesia Cabinet to reflect the nature of coalition across various political parties) only about a third of them do not come from political parties. Sofyan is one of them. This is an important factor for the post of Minister for SOEs. It is well known that SOEs, and not only those in Indonesia, are potential cash cows for political parties facing elections. Having somebody who is not from a political party is important for breaking that trend.

However, it remains unclear whether Sofyan’s lack of political party affiliation will allow him to enjoy the support of political parties. This can be seen as a double-edged sword. Without that support, the minister might not be able to get the necessary parliamentary support for key policies, e.g., privatization, a necessity in
Indonesia’s contemporary multi-party democracy. However, political party support can also be perceived as a negative factor for a Minister for SOEs, as the person is expected to be neutral in maintaining the principles of professionalism in managing the SOEs. The case with Sugiharto, whom Sofyan replaced, serves as an important reminder of the problematic nature of party backing. Sugiharto actually had the backing of political parties but finally had to be replaced when the parties deserted him.

Finally, Sofyan’s steps are seen as no surprise since he was actually one of the deputy ministers under the pioneering Minister for SOEs, Tanri Abeng. In fact, the master plan calling for SOEs to be put under a holding company was first planned by Tanri, with Sofyan as one of his right-hand men especially tasked with the issues of socialization and communication. Sofyan is considered to be one of the heirs apparent to Tanri, since he is one of the deputy ministers at Tanri’s office, which is composed of bureaucrats, business professionals, SOE officials, and military officers.

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54 “Sugiharto Layak Diganti, Boediono Disayang-sayang” (Sugiharto Deserves Replacement, Boediono Still Desired), Detikfinance.com, Thursday, 03 May 2007.
55 Author’s interview with Tanri Abeng, former Minister of SOEs, Sunday, 18 March 2007.
A person with many years of professional experience and relatively little political flair, Tanri Abeng was appointed as the Minister for Empowerment of SOEs in Soeharto’s short-lived last cabinet in 1998. His initial main task was to find ways to unleash the potential of SOEs, which were seen by Soeharto as the last resort for paying Indonesia’s mounting foreign debt\(^5^6\). With long experience in multinational companies resembling the structure of global conglomerates, Tanri viewed this as the appropriate model for the Indonesian government to manage its companies, dubbed Indonesia, Inc.

Tanri stayed on for another term under Habibie’s cabinet after the *reformasi* wave that ended Soeharto’s term of 32 years as the longest-serving leader in Southeast Asia. It was actually during Tanri’s period that the master plan for setting up a holding company structure to manage the SOEs was outlined, with the help of a number of consulting firms.\(^5^7\)

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\(^5^6\) “Tanri Abeng: Saya Tidak Rela Menjual Obral BUMN” (Tanri Abeng: I Did Not Agree to Cheap Sales of SOEs), Interview with Tanri Abeng by Eben Ezer Siadari, Agung Widayatmoko and Alfian Kartim in Warta Bisnis, 11 July 2003.

Thus, it is quite logical that Sofyan would continue to implement the master plan, and he seems to be the one most committed to it. The three SOE ministers who came in between them – Laksamana Sukardi, Rozy Munir, and Sugiharto – were either too distracted by more heavily politically loaded agendas or were simply not particularly fond of the master plan, as they came from different political camps than Tanri and Sofyan\(^{58}\). That made continuity in the ministry’s policy rather difficult. Political changes can always happen after the election in 5-year or in an even shorter time period, reminding us that we should not become too excited about Minister Sofyan Djalil’s actions.

<table>
<thead>
<tr>
<th>No.</th>
<th>Name</th>
<th>Year</th>
<th>Presidency</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Laksamana Sukardi was a politician at Megawati’s PDI-P (Indonesian Democratic Party in Struggle), Rozy Munir is an aide to Abdurrahman Wahid from the PKB (National Awakening Party) and Sugiharto, though a professional, joined Yudhoyono’s cabinet as a member of the PPP (United Development Party) and later was backed by the PKS (Prosperous Justice Party).</td>
<td></td>
<td></td>
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<td></td>
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<tr>
<td></td>
<td></td>
<td></td>
<td>BJ Habibie (May 1998 – October 1999)</td>
</tr>
</tbody>
</table>

**Three-Step Strategy of Restructuring, ‘Profitization’ and Privatization**

When appointed as the State Minister for Empowerment of SOEs by Soeharto in 1998, Tanri Abeng outlined the three-step strategy to unleash the potential of Indonesian SOEs: restructuring them, making them profitable (profitizing), and privatization. Given Indonesia’s huge foreign debt, what Soeharto had in mind was indeed to reap money from the SOEs to repay the debt. Soeharto himself tried to conduct privatization, but was only partially successful. It was against this backdrop that Tanri was tasked with
leading the new ministry. However, Tanri had preferred the form of a national holding company for the SOEs rather than a new ministry. The legal hindrance resulting from the lack of Indonesian laws regulating such a holding company forced him to opt for this second best option, something which proved to be part of the problem in managing SOEs as time went by.

Of the three steps in the strategy, it is obvious that privatization has been the most difficult of all. One factor is the capital market. Privatizing companies through public offerings is certainly not an easy task when the capital market is not in good shape. In the case of Indosat’s privatization, which drew the biggest public outcry, it was obvious that a strategic sale was undertaken as a step toward privatization due to the bearish condition of the Jakarta Stock Exchange⁵⁹. Another factor is certainly nationalistic sentiment. Despite Sugiharto’s effort to emphasize that the goal of privatization

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⁵⁹ Author’s interview with Laksamana Sukardi, former Minister of SOEs, Saturday, 24 March 2007 and “Laksamana:harga di bawah Rp12 Ribu, Divestasi Indosat Batal” (Laksamana: If The Price Goes Below Rp. 12000, We’ll Cancel Indosat’s Divestment), Tempo Interaktif, 20 November 2002.
is the distribution of share ownership\textsuperscript{60} and not “selling off state assets”, it is always difficult to shake off public opinion that privatization creates the likelihood that strategic sectors of the economy will fall into the hands of foreign parties, which is a politically sensitive issue in Indonesia. The issue will always inspire controversy because of the diverse and sometimes conflicting interests of stakeholders, including the government, employees, investors, and the public.\textsuperscript{61}

Apparently with this thought in mind, Sugiharto, after his appointment to Minister of SOEs in 2004, took the stance of “go for the dividends” and mentioned privatization only as a last resort to help to cover the state budget deficit. This was also backed by Vice-President Jusuf Kalla, who stated that selling government stakes in SOEs was the “lowest priority” for the government.\textsuperscript{62}


\textsuperscript{61} “More IPOs planned for SOEs this year”, The Jakarta Post, 02 August 2006.

\textsuperscript{62} Guerin, Bill: “Privatization stalls in Indonesia”, Asia Times online, 09 May 2006.
However, in 2007, the government seems to have reversed its earlier stance and targeted 3.3 trillion rupiahs (about US$ 350 million)\(^{63}\) from privatization. Of those targeted results, about 1.3 trillion rupiahs is planned to be re-invested as capital placement in eight financially hemorrhaging SOEs in need of more capital (among others, the flag carrier Garuda Indonesia), while the remaining 2 trillion rupiahs are expected go to state coffers. Up to 15 SOEs have been scheduled for the privatization plan\(^{64}\), as outlined in the table below.

There is hope that privatization programs will not only aim at covering the state budget deficit. Starting in 2008, funds generated from the privatization program will not go to the state budget and instead will be re-invested to finance SOE growth\(^{65}\). This is a positive signal for the Indonesian economy for two reasons: It means that fiscal balance is improving and privatization is perceived as a means to improve the performance of SOEs. In 2007,

\(^{63}\)“Target Privatisasi 2007 Rp 3,3 T” (2007’s Privatization Target is 3.3 Trillion Rupiahs), Detikfinance.com on Thursday, 16 August 2006.


\(^{65}\)“Dana Privatisasi BUMN 2008 Tidak Disetor ke APBN” (Gain from SOEs’ Privatization in 2008 Would Not Be Submitted to The State), Detikfinance.com, 16 May 2007.
Privatization was targeted to contribute 3.3 trillion rupiah (about US$ 360 million), while in 2008, it is predicted to be only about 1 trillion rupiah (about US$ 110 million).

**Table 0-3 List of State-Owned Enterprises for Privatization in 2007 (MSOE, 19 February 2007)**

<table>
<thead>
<tr>
<th>No</th>
<th>SOEs</th>
<th>State ownership</th>
<th>Planned method for privatization</th>
<th>Share to be divested</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>PT. Jasa Marga (Persero) – toll operator</td>
<td>100% Initial Public Offering (IPO) / Dilution / Divestment</td>
<td>Gradually up to 49%</td>
<td></td>
</tr>
<tr>
<td>2</td>
<td>PT. Bank BNI Tbk. – the second biggest state bank</td>
<td>99.12% Secondary Offering (Dilution/Divestment)</td>
<td>Up to 20%, plus 20% of the enlarged capital (state should retain at least 51%)</td>
<td></td>
</tr>
<tr>
<td>3</td>
<td>PT. Permodalan Nasional Madani (Persero) – trust funds to develop SMEs</td>
<td>100% Strategic Sales (SS) (Divestment/Dilution)</td>
<td>Up to 30%</td>
<td></td>
</tr>
<tr>
<td>4</td>
<td>PT. Wijaya Karya (Persero) – construction</td>
<td>100% IPO / Dilution (issuing new shares)</td>
<td>Up to 35%</td>
<td></td>
</tr>
<tr>
<td>5</td>
<td>PT. Industri Soda Indonesia (Persero) – consumer goods</td>
<td>100% Strategic Sales /Divestment</td>
<td>Up to 100%</td>
<td></td>
</tr>
<tr>
<td>6</td>
<td>PT. Garuda Indonesia</td>
<td>100% Strategic Sales</td>
<td>Up to 49%</td>
<td></td>
</tr>
</tbody>
</table>
From the above-listed companies, potential for backlash exists in the case of Garuda. The flag carrier is regarded as the pride of the nation, despite the tragic accident involving the GA-200 in
Yogyakarta on 07 March 2007\textsuperscript{66}. The accident provides impulse to consider the need for better governance of the company as well as the issue of mounting debt. Ironically, 2007 was the first year that Garuda was expected to book profit after making losses for three consecutive years\textsuperscript{67}.

Lawmakers signaled that they would oppose a sale of Garuda, despite its being in default on a US$55-million principal debt payment that was due at the end of 2005. Dradjad Wibowo is a senior legislator from PAN (National Mandate Party) who sits on the parliamentary commission in charge of budgetary affairs and who also showed strong opposition to the ownership of Indosat by ST Telemedia. Wibowo stated that since the country’s strategic sectors such as telecommunications, banking and mining were already controlled by foreign companies, Garuda was not to not be sold to foreigners. The privatization of six SOEs on the list

\textsuperscript{66} “Jumlah Tewas Versi Garuda 22 Orang” (Death Toll was 22 According to Garuda): Kompas, 7 March 2007.

\textsuperscript{67} “Garuda posts profit in Jan-April after three yrs of losses”, Antara News, 5 June 2007.
including Garuda and Merpati, the other state-owned airline, has yet to be approved by the parliament. Despite those glitches, the government managed to push through the privatization of the biggest target, Bank BNI. The deal generated lower gains than expected due to the weakening Indonesian rupiah against the US dollar as a result of the subprime mortgage crisis in the US. Toll operator Jasa Marga and construction firm Wijaya Karya are the other big targets of privatization. Jasa Marga’s IPO is scheduled for 12 November 2007.

Some Benchmarks on Key Sectors of Indonesian SOEs
As Indonesia ranks poorly in various ratings of corporate governance, it is seen as imperative for the country’s companies to improve the practice of good corporate governance. This becomes even more important for Indonesian SOEs, whose total market

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68 “Privatisasi Enam BUMN Belum Disetujui DPR” (Privatization of 6 SOEs Has Yet To Be Approved By Parliament), Detikfinance.com, Wednesday, 16 May 2007.
69 “SBY Puas Secondary Offering BNI” (SBY Satisfied with BNI’s Secondary Offering), Detikfinance.com, Thursday, 9 August 2007.
70 Among others, in Credit Lyonnais SA, Emerging Market 2001- The Saint and The Sinner, which ranked 495 Blue Chips in Emerging Markets, with 18 samples from Indonesia. There were five Indonesian companies in The Worst 25, with the worst ranked 495th, and none ranked in the Top 50.
capitalization of 493.26 trillion rupiahs is equal to 40.23% of the total market capitalization at the Jakarta Stock Exchange\textsuperscript{71}.

However, the performance of SOEs generally lags behind their private sector counterparts. In 2006, of 139 SOEs, about 20 recorded losses, amounting to about 2.27 trillion rupiahs (close to US$ 250 million), and 114 were profitable\textsuperscript{72}, with total net profits of about 54.42 trillion rupiahs (almost US$ 6 billion). Benchmark of SOEs with private sector counterparts in certain key industries such as banking and plantation on the efficiency indicators show that they are lagging behind. In the banking sector, state-owned banks show lower rates in Return on Assets (2.2, in comparison to private banks’ 2.6) but higher Non-Performing Loans and Non-Performing Earning Assets compared to private banks, as shown in the figure below.

\begin{figure}
\centering
\includegraphics[width=\textwidth]{chart.png}
\caption{Comparison of SOE and Private Banks on Various Efficiency Indicators}
\end{figure}
Figure 7.1 Performance Benchmark of Indonesian State Owned Banks versus Private-Owned Banks (Bank Indonesia, November 2006)

In the plantation sector, the performance of the state plantation companies (known as PTPN, with a total area of 1.4 million hectares) shows a rising trend, but is still below key players in the sector such as PT. Astra Agro Lestari, which has about 300,000 hectares of land. This is especially true for the upstream business. The table below shows the benchmark between PTPN and Astra Agro Lestari.

Table 0-4 State-Owned Plantation Firm PTPN versus Industry Leader Astra Agro Lestari: Lagging though Improving (MSOE, 19 February 2007)

<table>
<thead>
<tr>
<th>Indicators</th>
<th>Astra Agro Lestari</th>
<th>PTPN</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2003</td>
<td>2004</td>
</tr>
<tr>
<td>Net Sales</td>
<td>2,543.2</td>
<td>3,472.5</td>
</tr>
<tr>
<td>Gross Profit</td>
<td>994.5</td>
<td>1,526.0</td>
</tr>
<tr>
<td>Operating Profit</td>
<td>753.0</td>
<td>1,284.8</td>
</tr>
<tr>
<td>Net Profit</td>
<td>280.7</td>
<td>800.8</td>
</tr>
<tr>
<td>Total Asset</td>
<td>2,844.7</td>
<td>3,382.8</td>
</tr>
<tr>
<td>Total Liability</td>
<td>1,138.1</td>
<td>1,028.3</td>
</tr>
<tr>
<td>Total Equity</td>
<td>1,515.5</td>
<td>2,065.3</td>
</tr>
</tbody>
</table>
In the mining industry, one of the key sectors with state ownership, it can be seen that generally, performance is improving. Based on a comparison between the state mining firm PT. Aneka Tambang (ANTAM) and the private nickel company PT. Inco Indonesia (INCO) – both are however listed companies – performances of the two are equivalent. In fact, ANTAM had better Return on Equity (ROE) and Net Profit Margin (NPM), though still underperformed compared to INCO in ROA for the year 2005.

Table 0-5 State-Owned Mining Firm Aneka Tambang versus Private-Owned INCO: Better ROE and NPM but Still Worse in ROA (MSOE, 19 February 2007)
The above benchmark makes it imperative for SOEs to embark on the GCG program. Various government regulations and acts\textsuperscript{73} are in place for the program, but apparently, the devil is more in the details and implementation than in the letter of the law, which is not an uncommon case in Indonesia. As Simanjuntak (2006)\textsuperscript{74} puts it, the gap between the spirit and letter of the laws and practices is by no means the only difficult obstacle to corporate governance reform in Indonesia, but is clearly the principal hindrance.

\textsuperscript{73} Among others, Law No.19/2003 on SOEs, Law No. 8/1996 on Capital Market, Law No. 1/1995 on Listed Company, Minister of SOEs Decree No.117/M-BUMN/2002 on Implementation of Good Corporate Governance.

\textsuperscript{74} Simanjuntak, Djisman. “Indonesia’s Tolerated Low-Speed Reform of Corporate Governance”. In Reforming Corporate Governance in Southeast Asia: Economics, Politics and Regulations, edited by Ho Khai Leong, pp. 157-179. Institute of Southeast Asian Studies, Singapore, 2006.
The three-step action plan is in place with regard to GCG implementation: socialization, assessment, and review. The socialization of GCG is aimed at creating understanding and preparing SOEs for the implementation of GCG. The assessment of GCG is aimed at the identification and evaluation of GCG in SOEs. The review of GCG is an action plan to describe and explain to the public the current state of development and implementation of GCG at SOEs. Of the 139 SOEs available, 102 had received socialization, 68 had been assessed, and 40 had been reviewed by June 2006.\footnote{Djajanto, Pandu. “Good Corporate Governance in BUMN: Implementation, Achievement and Acceleration in Fight Against Corruption, Collusion and Nepotism”. Expert Staff on GCG, Ministry of State-Owned Enterprises, obtained during an interview on 2 April 2007.}

Results have shown improvement, as indicated, for example, by the International Monetary Fund in its IMF Country Report 2006,\footnote{International Monetary Fund. “Indonesia: Selected Issues”. IMF Country Report No. 06/318, August 2006.} which characterizes Indonesia as having a sound corporate governance framework. However, cases on corporate governance scandals at SOEs, such as at PGN (Perusahaan Gas Negara), the state-owned gas company,\footnote{“PGN Digoyang Rumor Skandal Keuangan” (PGN Shaken By Rumors of Financial Scandal), Detikfinance.com on Friday, 12 January 2007.} have marred the Ministry scorecard on
GCG implementation. The scandal, which was reportedly caused by irregularities in PGN’s annual report, caused the company’s share price to plunge 23.32% overnight.

The implementation of GCG is also aimed at eradicating the practice of corruption, collusion, and nepotism (known in Indonesian as KKN – Korupsi, Kolusi and Nepotisme). The struggle against KKN through GCG uses a double-pronged approach: preventive and repressive action. Preventive action is mainly conducted by providing training and workshops on KKN eradication targeted at SOEs managers, while repressive action is focused on urging SOEs to be more active in responding to complaints and reports made by the public regarding indications of corruption practices. As Hamilton-Hart (2001) argued, such internal reform programs that aim to improve organizational self-discipline have received much less attention so far in anti-corruption strategies in Indonesia. The focus has been mainly on acts to introduce monitoring and sanctioning mechanisms that are external to the particular organizations.

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It remains to be seen whether such a move will be adequate because, as described in the next section, there is an even more persistent problem in Indonesian SOEs that is rooted in the very fact of ownership by the state. Wong (2004)\textsuperscript{79} argues that the poor performance of many SOEs (not only in Indonesia) can be attributed to the three main challenges facing SOE governance in comparison to private sector enterprises: conflicting objectives, multiple agency problems, and lack of transparency.

It is against this backdrop that the Indonesian government developed the master plan to build a national holding company for the SOEs along the lines of Temasek Holdings in Singapore\textsuperscript{80} and Khazanah Nasional Berhad in Malaysia. The holding structure is also believed to be able to serve as a layer shielding the SOEs from politics and governmental intervention. As Wong stated above, the three stumbling blocks of SOEs governance are multiple conflicting objectives, political intervention, and a lower degree of transparency. The holding structure seems to well serve the purpose


\textsuperscript{80} “Indonesia plans Temasek-style holding company”. Reuters, Thursday, 31 May 2007.
of remedying the first two problems at SOEs, while transparency can be best improved by opening access of ownership to the public.

**Indonesian SOE Master plan: Building a Temasek-style Holding Company**

Active in strategic expansion and praised for corporate governance practices in Asia, yet perceived with envy and cautiousness in regard to its massive presence in Indonesia and other regions, the Temasek form of holding company has been identified by Indonesian SOE Minister Sofyan Djalil as the mechanism for managing Indonesian SOEs. Malaysia, another close neighboring country, also has investment holding companies to manage its assets. Khazanah Nasional is the most expansion-oriented in its resemblance to Temasek and also has a strong presence in Indonesia’s banking and telecommunication sector. The existence of Khazanah Nasional simply underlines Sofyan’s conviction that a holding company is the most appropriate path to follow.

The Indonesian SOE master plan mainly consists of a set of restructuring strategies for classifying the SOEs into three categories, stand-alone, merger, and sectoral holding, seeks to
emulate the success of Temasek Holdings, the investment holding company of the Singaporean government. The sectoral holding companies would then build the foundation for the super-holding company, just as Temasek functions as the holding company for Singapore’s government-linked companies (GLCs). Immediate priorities for creation seem to be in the plantation, mining and cement sectors.

![Diagram of 3 Types of Structure for SOEs]

- **‘Stand-Alone’ SOEs** (39 companies)
- **Focused Holding** (38 SOEs in 10 Holding)
- **Roll-Up** (54 SOEs merged to 21)

**Figure 7.2 Masterplan for Indonesian SOE Rightsizing (as of 26th January 2005)**

The main arguments for building a holding structure for Indonesian SOEs are strategy alignment and synergy creation. This can be unleashed by weaving various SOEs from different sectors into one
strategy, operational or financial holding, as mapped out in the table below. The issue of economies of scale and economies of scope, often used by Sofyan, is another key argument. Such a holding structure would be able to pool resources, lower risk, and provide access to lower cost financing. The Ministry confidently stated that the combined assets of Indonesian SOEs can reach US$ 400-500 billion, far greater than Temasek’s US$ 75 billion and Khazanah’s US$ 20 billion\textsuperscript{81}.

The Ministry has also named five companies to be “SOE Champions” able to grow and compete globally, with the plantation holding and mining holding among them. The three other SOEs to be transformed into “champions” are the telecommunications company PT. Telkom (through diversification and growth), national energy company PT. Pertamina (through internal restructuring), and state gas company PT. Perusahaan Gas Negara/PGN (through growth). The Indonesian government intends to have only about 25 SOEs by 2015 as the result of its “rightsizing” master plan.

\textsuperscript{81} “BUMN Jangan Minder dengan Temasek dan Khazanah” (Indonesian SOEs Should Not Feel Inferior to Temasek and Khazanah), Detikfinance.com on Wednesday, 15 August 2007.
SOE Champions belong to the government’s long-term vision for its SOEs.

Table 0-6 Indonesian SOE Masterplan: Stand-Alone, Holding Company & Merger

<table>
<thead>
<tr>
<th>Industry</th>
<th>Stand-Alone</th>
<th>Holding</th>
<th>Roll-Up</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agro &amp; Consumer</td>
<td>Sakt, Soda, Igas, Bio Farma</td>
<td>15 Plantation and 2 Fertilizer</td>
<td>2 Pharmaceutical, 4 Fisheries and 2 Seedlings</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Telco &amp; Media</td>
<td>Telkom, TVRI</td>
<td></td>
<td>2 Printing Companies</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Forestry &amp; Paper</td>
<td></td>
<td></td>
<td>5 Forestry into 3 and 2 Paper Manufacturers into 1</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Construction</td>
<td></td>
<td>2 Cement Manufacturers</td>
<td>9 Construction into 3 and 5 Civil Engineering into 2</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Mining</td>
<td></td>
<td>4 Mining: Bukit Asam, Timah, Aneka Tambang,</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Sarana Karya</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Logistics</td>
<td>Survey Pesas, Pos Indonesia, Jasa Marga, Satriah,</td>
<td>4 Shipping Companies and 5 Industrial Areas Management</td>
<td>4 Ports, 3 Surveyors (Sucofindo, SI, BKI), 4 Ship Industries (DKB, DPS, PAL, Industri Kapal Indonesia), KAI &amp; INKA (merged)</td>
</tr>
<tr>
<td></td>
<td>Pengenalan, BGR, VTP, Bertiklan, PPI, Sandang,</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Nasantara, Primasena</td>
<td></td>
<td></td>
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<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Energy</td>
<td>Koneba</td>
<td>Pertamina, PLN and PGN</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Travel &amp; Tourism</td>
<td>Garuda, Merpati</td>
<td>3 Tourism Companies</td>
<td>2 Airport Companies</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Financial Services</td>
<td>All State Banks, ASKES, Dinareksa, PNM, PPA,</td>
<td></td>
<td>Jamsostek &amp; Jasa Raharja (merged), Asuransi Ekspor Indonesia &amp; Askrindo (merged) and 5 Insurances</td>
</tr>
<tr>
<td></td>
<td>Klling</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Strategic Industry</td>
<td>DI, Pindad, Dahara, Borna Bisma Idr, Krakatau</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Steel, LEN Industri, Init, Batara</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Announced just a few weeks after the swearing in of the new minister for SOEs, the master plan is actually nothing new. It was initially mapped out under Tanri Abeng’s restructure-profitize-privatize strategy. The creation of holding companies was identified as a priority in the restructuring phase\(^\text{82}\). The key sectors of the holding companies having priority of formation are plantation, mining, cement, fertilizer (currently already in existence but with poor performance and, depending on the outcome of the central bank regulations on ownership\(^\text{83}\), the banking sector. The development of some SOE sectoral holding companies is reviewed in the cases below. The reasons for choosing the sectors (plantation, mining, banking, and cement) as priorities are size, potential, and significance for the Indonesian economy.

\(^{82}\) “Restrukturisasi BUMN Diutamakan Lewat Holding” (Restructuring SOEs Primarily Through Holding), Detikfinance.com on Tuesday, 26 June 2007.

\(^{83}\) “BI moves to push mergers, acquisitions among banks”, The Jakarta Post, Friday, 06 October 2006.
Plantation SOEs’ Holding Company: The Challenge of Scattered Locations

The holding companies for plantation and mining are expected to be formed before the end of 2007\(^\text{84}\), though progress is yet to be seen. With assistance from financial advisers Danareksa Securitas and Bahana Securitas, the holding company for plantations is expected to leverage the PTPN, the plantation SOEs, which have been held back by their past problems. It aims at value creation by improving its capital structure and enhancing its financing capacity through the synergy effect of a holding company. One issue remains a potential hindrance to the formation: the lack of a legal basis for the holding company. However, creation of regulation (PP) for this is a priority the government.

Several critics have expressed objection to the formation of this holding company. The most prominent among them is a leading economist, Faisal Basri\(^\text{85}\), who asserts that the plantation holding company would not be effective for improving PTPNs’

\(84\) “Holding BUMN Kebun & Tambang Dibentuk Sebelum Akhir 2007” (Holding Company for Plantation and Mining To Be Formed Before End 2007), Detikfinance.com on Tuesday, 26 June 2007.

\(85\) Basri, Faisal. “Penciutan BUMN” (Downsizing SOEs), Kompas, 26 February 2007.
competitiveness as the plantations are scattered across the archipelago. Therefore, expected saving on average cost in the long run would be difficult to achieve, particularly given the differences in soil conditions, social factors, and port infrastructure, which supports logistic arrangement as a key cost factor.

**Integrated Resource Company (IRCS) as the Holding Company for Mining SOEs**

The holding company for mining SOEs is to be formed based on a plan drawn up by Citigroup and a local firm as financial advisors. To be named the IRC (Integrated Resources Company), the company is to hold shares of the three mining SOEs: PT. Aneka Tambang (ANTAM), PT. Timah (TIMAH), the tin mining company, and PT. Tambang Batubara Bukit Asam (PTBA), the coal mining company. In addition, it is also planned that the government’s shares in Freeport also be put under this holding company to achieve a sizable value.

The holding company aims to enhance economies of scale to create value for the government as shareholder. Similarly to the plantation
holding, preparation for the legal basis for the firm is a priority for the government. Also of paramount importance is the organizational arrangement between the planned holding company and the mining SOEs as subsidiaries.

Faisal Basri has also argued against this idea, stating that the key to competitiveness lies in reaping benefits from the entire value chain of the mining industry, especially with respect to the aspects of financing and trade, since they represent the areas of the greatest potential value-added.

**Building a Holding Company for Cement SOEs: Turning Conflicts Into Synergy**

The holding for cement companies, which would hold shares of the three state-owned cement manufacturers, Semen Gresik, Semen Padang, and Semen Tonasa, already exists in the form of Semen Gresik. It is the operating holding company for the three companies and will reportedly be named PT. Semen Indonesia as a financial
and strategic holding\textsuperscript{86}. The decision has been approved by shareholders and is to be implemented in 2008\textsuperscript{87}.

A key goal to be achieved is to reduce potential conflict between the three companies and turn it into potential synergy. This was evident in the pressure for spin-offs of Semen Padang from Semen Gresik which arose from nationalistic and primordial sentiments from interest groups\textsuperscript{88}.

However, other issues on the tax, commercial, and legal implications of the holding company still also need to be resolved\textsuperscript{89}.

For the moment, though, efforts toward synergy creation have resulted in the steadily improving performance of Semen Gresik in the last 2 years\textsuperscript{90}, which increased its profit almost three-fold, from

\textsuperscript{86} “Semen Gresik Bentuk Holding” (Semen Gresik Forms A Holding), Detikfinance.com on Thursday, 15 February 2007.
\textsuperscript{87} “Holding Semen Disetujui” (Holding Company for Cement Approved), Detikfinance.com on Thursday, 28 June 2007.
\textsuperscript{89} “Pemerintah Kaji Dampak Pajak Holding Semen” (Government Studies Tax Implication of The Cement Holding), Detikfinance.com on Friday, 30 March 2007.
\textsuperscript{90} “Kajian Holding Semen Diharap Selesai Bulan Mei” (Study on Cement Holding To Finish in May), Detikfinance.com on Thursday, 22 February 2007.
500 billion rupiahs (US$ 55 million) in 2004 to 1.3 trillion rupiahs (US$ 142 million) in 2006.

**Holding Company for SOE Banks: Potential Implications of Single Presence Policy (SPP) Ownership Banking Regulation**

The holding company for SOE banks might be formed based on a regulation by the central bank that prohibits shareholders from holding controlling stakes in more than one bank. In order to adjust to the new regulation, the central bank has asked banks to consolidate by 2010, either through mergers, acquisitions, or the setting up of a holding company, or through the divestment of its stake. State banks and private national banks will be affected by the policy, but foreign lenders and joint-venture banks will be exempted, according to international banking practices. This is known as the “single presence policy”.91

This makes it imperative for the government, which currently owns four banks, to consider which option it should take by 2010 with regard to the structure. Building a holding company for SOE banks

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91 Bank Indonesia Regulation Number 8/16/PBI/2006, concerning the Single Presence Policy in Indonesian Banks.
is a plausible option, especially since merging would eliminate the specific function that each bank has. Bank Mandiri and Bank Negara Indonesia (BNI), the country's top-two largest lenders by assets, have similar segments but with differentiation. Bank Mandiri aims to position itself as the “dominant multi specialist and regional champion bank,”\(^{92}\) signaling its aspiration to be an Indonesian player within the bigger context of the regional market. The same aspiration applies to BNI, but the government aims for BNI to play the role of a development bank\(^{93}\). Bank Rakyat Indonesia (BRI) is positioned as a micro-financing bank, with a credit portfolio mostly for SMEs, and Bank Tabungan Negara (BTN) focuses on the financing of low-cost housing mortgages.

However, implementation of the holding is currently not the government’s priority. Developing growth and improving the health of the banking system, whose unsound fundamentals led to more severe consequences from the crisis, take priority over the creation of a holding company. For example, lowering the rate of NPL (non-

\(^{92}\) Author’s interview with Pahala Mansury, Chief Financial Officer and Executive Vice President Coordinator, Bank Mandiri, Thursday, 1 February 2007.

\(^{93}\) “Bapindo akan dihidupkan lagi” (Indonesian Development Bank Would Be Rejuvenated), Detikfinance.com on Tuesday, 10 July 2007.
performing loans) and improving CAR (Capital Adequacy Ratio) at state banks are considered more important\textsuperscript{94}.

A key factor behind the idea of building a holding company for the SOEs is to inject professionalism into the leadership, which will allow the SOEs to operate with commercial interests as the main driver. Given the experience of Temasek and Khazanah, this is an important factor. The new Indonesian State Minister for SOEs, Sofyan Djalil, emphasized that the government’s current main agenda involves gradually switching from control by the bureaucracy to control by corporations\textsuperscript{95}. The ultimate aim is to have a strong group of Indonesian SOEs which will become the champion of Indonesia’s economy and regional or even global players.

<table>
<thead>
<tr>
<th>No</th>
<th>Company</th>
<th>Sector</th>
<th>Revenue</th>
<th>Net Profit</th>
<th>Assets</th>
</tr>
</thead>
</table>

\textsuperscript{94} “Implementasi Holding Bank BUMN Tunggu Penurunan NPL” (Implementing Holding Company for SOE Banks Should Wait Until Lower NPL), Antara, 12 June 2006.

\textsuperscript{95} “Changing attitudes; creating value at SOEs”, interview with State Minister for SOEs Sofyan Djalil, Globe Asia, Volume 1 Number 8, September 2007.
<table>
<thead>
<tr>
<th></th>
<th>Company</th>
<th>Industry</th>
<th>Revenue</th>
<th>Profit</th>
<th>Assets</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Pertamina</td>
<td>Oil and gas</td>
<td>33,333</td>
<td>1,256</td>
<td>15,000</td>
</tr>
<tr>
<td>2</td>
<td>Perusahaan Listrik Negara (PLN)</td>
<td>Electricity</td>
<td>7,859</td>
<td>(214)</td>
<td>27,546</td>
</tr>
<tr>
<td>3</td>
<td>Telkom</td>
<td>Telecommunication</td>
<td>5,699</td>
<td>1,223</td>
<td>8,348</td>
</tr>
<tr>
<td>4</td>
<td>Bank Mandiri</td>
<td>Banking</td>
<td>3,240</td>
<td>269</td>
<td>29,724</td>
</tr>
<tr>
<td>5</td>
<td>Bank Rakyat Indonesia (BRI)</td>
<td>Banking</td>
<td>2,341</td>
<td>473</td>
<td>17,191</td>
</tr>
<tr>
<td>6</td>
<td>Bank Negara Indonesia (BNI)</td>
<td>Banking</td>
<td>2,004</td>
<td>214</td>
<td>18,823</td>
</tr>
<tr>
<td>7</td>
<td>Garuda Indonesia</td>
<td>Transportation</td>
<td>1,371</td>
<td>(22)</td>
<td>897</td>
</tr>
<tr>
<td>8</td>
<td>Semen Gresik</td>
<td>Cement</td>
<td>970</td>
<td>144</td>
<td>832</td>
</tr>
<tr>
<td>9</td>
<td>Perusahaan Gas Negara (PGN)</td>
<td>Gas</td>
<td>730</td>
<td>210</td>
<td>1,679</td>
</tr>
<tr>
<td>10</td>
<td>Aneka Tambang</td>
<td>Mining</td>
<td>625</td>
<td>173</td>
<td>810</td>
</tr>
<tr>
<td>11</td>
<td>Bank Tabungan Negara (BTN)</td>
<td>Banking</td>
<td>481</td>
<td>41</td>
<td>3,619</td>
</tr>
<tr>
<td>12</td>
<td>Adhi Karya</td>
<td>Construction</td>
<td>481</td>
<td>11</td>
<td>318</td>
</tr>
<tr>
<td>13</td>
<td>Timah</td>
<td>Mining</td>
<td>453</td>
<td>54</td>
<td>384</td>
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<td>14</td>
<td>Bukit Asam</td>
<td>Mining</td>
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<td>54</td>
<td>345</td>
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<td>15</td>
<td>Wijaya Karya</td>
<td>Construction</td>
<td>339</td>
<td>10</td>
<td>295</td>
</tr>
<tr>
<td>16</td>
<td>Waskita Karya</td>
<td>Construction</td>
<td>308</td>
<td>6</td>
<td>215</td>
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<tr>
<td>17</td>
<td>PTPN III</td>
<td>Plantation</td>
<td>295</td>
<td>33</td>
<td>332</td>
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<tr>
<td>18</td>
<td>Pembangunan Perumahan</td>
<td>Construction</td>
<td>271</td>
<td>9</td>
<td>219</td>
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<tr>
<td>19</td>
<td>Jasa Marga</td>
<td>Toll road</td>
<td>255</td>
<td>51</td>
<td>1,139</td>
</tr>
<tr>
<td>20</td>
<td>Kimia Farma</td>
<td>Pharmaceutical</td>
<td>243</td>
<td>5</td>
<td>140</td>
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</tbody>
</table>

The development of SOE holding companies in Indonesia should begin with the goal of rightsizing the number of SOEs to a number which is not only manageable but also able to provide returns for the country, as currently a mere 22 of the 139 SOEs hold 90% of the
total assets and revenues, contributing to about 80% of total net profit of all SOEs. Of the above SOEs, the plan is to have at least five SOE champions: Pertamina, Telkom, PGN, and two SOE holding companies in the plantation sector (which will house PTPN III and 14 other plantation SOEs) and mining (attempting to reap synergy from Aneka Tambang, Timah and Bukit Asam, added to government shares in Freeport and Inalum).

After the sectoral holding companies have been built as the foundation for solid SOE governance, a super-holding company will be created to house them all, just as Temasek and Khazanah are the holding companies for the Singaporean and Malaysian GLCs. The SOE minister has also stated on a number of occasions that he aims to be the last (SOE) minister, meaning that when his tasks are done, the ministry for SOEs will be dissolved and replaced with the SOE super-holding company. This would transform the SOEs from being part of the bureaucratic machinery to being based on business principles.

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Unfortunately, even if the government understands that moving away from bureaucratic and political intervention to professionalism is a key success factor, whether the government will be able to do it is another question. The reason lies in the rapid democratization and decentralization that Indonesia is facing. Singapore and Malaysia underwent the exercise of creating their government investment holding companies in a political environment that was less competitive, under tighter control and less open to participation. Unlike those countries, the Indonesian government would have to juggle between the pressure of globalization, adopting economic neoliberal doctrine, and the impact of democratization, which would open the way for stronger voices of economic nationalism.

The Indonesian parliament (DPR) – dubbed by some as ‘stakeholders eager to play the role of shareholders’ – often has its say in decisions regarding SOEs. This is one critical element making the case of Indonesia different compared to its two neighbors. Given

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97 Freedom House (2006) in its recent assessment of Southeast Asian countries’ degree of freedom – with focus on criteria of civil liberties and political rights – put Indonesia at the top ranking among the neighbors, based on a survey.
98 Author’s interview with Laksamana Sukardi, former Indonesian Minister of SOEs, 24 March 2007.
that framework, decisions on SOEs are always political, despite agreement that it should be commercially driven, and therein lies the difficulty. The Indonesian government’s decision making with regard to its managing of state resources would unavoidably be more cautious and considerably slower.

It is therefore interesting to see the cases of two other countries, China and Vietnam, which will be briefly outlined in the next chapter. Both are countries in transition from communist to market economies and able to implement a master plan with regard to SOE transformation. More interestingly, both countries have a political system and culture at the other end of the spectrum, compared to Indonesia whose system is arguably the most liberal democracy among Southeast Asian countries. This might serve as a reminder that Indonesia has a rather idiosyncratic political context when compared to the countries which have successfully implemented an investment holding structure. Those structures were all launched in less competitive political systems and cultures.
Political considerations aside, the holding company structure as a way to manage state assets “under one roof” is now a global trend, especially in countries defined as being in a developmental state. In countries like the UK and Australia, the government’s one-roof structure performs monitoring and management functions, although the structure does not hold equity in the companies.

The business logic of such a structure is clear: strategy alignment and synergy creation can be unleashed by weaving various SOEs of different sectors into one strategy, operational or financial holding. The issue of economies of scale and economies of scope, used frequently by Sofyan as a key argument for the structure, clearly favors a holding structure that would be able to pool resources, lower risk, and provide access to lower cost financing. The holding structure is also believed to be able to serve as a layer shielding the
SOEs from politics and government intervention. As Wong (2004) stated, the three stumbling blocks of SOEs governance are multiple conflicting objectives, political intervention, and a lower degree of transparency. The holding structure seems to well serve the purpose of remedying the first two problems at SOEs, while transparency can be best improved by opening access of ownership to the public.

In a nutshell, a conclusion can be drawn that managing state-owned enterprises under the holding company structure is a global trend. Within Southeast Asia, it is not only Singapore and Malaysia managing their GLCs under a holding company structure. The table below shows various other countries with a holding company structure to manage state-owned enterprises. It is evident that not only countries in emerging markets but also the United Kingdom and New Zealand have such structures.  

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99 Although in the case of CCMA (Crown Company Monitoring Unit) in New Zealand and UK’s Shareholder Executive in United Kingdom they do not hold equity in companies, but perform monitoring and management controlling.
We can therefore argue that it is only logical for Southeast Asian countries to also follow this path. However, as institutionalists would argue, much needs to be considered before applying the same
model in a different context. As testimony to that, the situations in Thailand and Vietnam in ASEAN are described below. A brief overview of the situation in China is also given simply because the country is too significant to be left out.

**Thailand**

Apart from Singapore and Malaysia, it might be worthwhile for Indonesia to look at the experience of other neighboring countries in ASEAN which have also built or attempted to build a holding company for their SOEs. In order to manage state assets, Thailand planned to build an investment holding modeled after Temasek and Khazanah\(^{100}\) in which the super-holding company will collect profits and dividends from 60 Thai SOEs.

In Thailand, according to its Budget Procedure Act 1959, SOEs are enterprises in which state agencies or enterprises own more than 50 percent of the equity share. In 2002, there were 77 enterprises regarded as SOEs by official definition. Certainly, the influence of the Thai state on the economy is much larger than that, as enterprises where state agencies own less than 50% of equity share

\(^{100}\) “Thailand plans investment unit”, Bloomberg News, 6 April, 2005.
are high in number and are thus not considered as SOEs by this definition. The enterprises under this definition alone have generated revenues of 1.46 trillion Thai Baht, which equals 26.71% of the Thailand’s GDP, and employed 274,570 workers or 13.7% of all government employees and 0.8% of the country’s workforce. The combined assets of these enterprises amounted to 4.64 trillion Thai Baht or 85.54% of the GDP (Nikomborirak and Cheevasittiyanon, 2005).

SOEs in Thailand also suffer similar agency problems as in the case of Indonesia. Efforts taken for corporate governance reforms have been underway, however, with a focus on boosting efficiency rather than transparency (Montreevat, 2005). Thai SOEs will be able to achieve effective corporate governance if a clear separation policy and regulations are in place to ensure that Thai SOEs are free from political interference, one of the recipes for SOE governance reform. Singapore’s Temasek Holdings has also been influential in the case of Thai SOEs. Thailand plans an investment holding to manage state assets modeled after Temasek and Khazanah\(^{101}\). A super-holding

company will collect all profit and dividends from 60 Thai state-run companies. The goals are:

1. To generate funds for a US$38 billion government infrastructure project for building subways, railroads and irrigation works. The government of Thailand needs to build up the infrastructure, especially after the tsunami catastrophe, which ravaged the country at the end of 2004.

2. To ease access to dividends of 60 Thai SOEs and enable government investing funds from one SOE to another. In 2004, those dividends amounted to US$ 1.33 billion. Once such dividends get into government coffers, it would be difficult to take them out again for investment in other SOEs. Such a holding structure would enable cross-financing and cross-investment among SOEs.

3. To improve efficiency in management and reduce political interference in running SOEs. This is aligned with Wong (2004) framework of SOE reforms, where the political insulation of SOEs can be achieved by applying one master for all SOEs.

However, there are concerns raised by the Thai public with regard to this plan, especially the transparency of the set-up process and
whether the formation of such a holding would be used for ‘political instead of economic purposes’. This concern does not come without reason. Tainted privatization, where individuals connected to the ruling power were able to secure large numbers of the coveted shares in privatized SOEs, is the main source of this concern.

This privatization case ironically has to do with the role of Temasek Holdings in the country. Temasek's purchase of shares in the Thai telecom giant Shin Corp from the Thaksin family for US$1.9 billion triggered a political crisis that forced Thaksin to announce that he would step down. The public condemned the tax-free windfall reaped by Thaksin's family members from the sale. This situation has been reported to have also forced changes within Temasek designed to repair its scandal-tarnished image.102

An economic nationalist response to cross-border investments in ‘strategic assets’ was strong when the tax-free sales of the telecommunications group ShinCorp by Thaksin to Singapore’s Temasek Holdings also became one of the triggers for a political crisis. Again, the situation was coopted by political groups, making

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it a matter of protecting national interests, thus bringing economic nationalist sentiments into public discourse.

As of now, there has not been any news on the implementation of this plan. Political uncertainty still looms in Thailand, at least until the next general election is held in the middle of December 2007. It will be interesting to see what the changes to this plan for a holding structure will be after political change has occurred. Nevertheless, the case of Thailand’s SOEs is certainly an interesting comparison for Indonesia and provides food for thought with respect to the implementation of the holding company.

**Vietnam**

The case of Vietnam is different. Apparently, the government has made significant progress with regard to a similar master plan to build a holding company for its SOEs\(^{103}\), as elaborated by Doanh (2007). Based on the master plan, the SOEs are to undergo a transformation process with two directions: creating big state-owned

holding companies to act as conglomerates of SOEs, and equitizing small and medium-sized SOEs. The significance of SOEs in Vietnam’s economy cannot be overstated, as they control 70% of the total assets, operate 20% of the total investment capital, use 60% of the total credit supply of commercial banks, provide 5% of total employment, and contribute 39% to GDP. Therefore, the right strategy in SOE governance is imperative for Vietnam’s economy, and apparently, the model in the plan is similar to Temasek. In fact, Temasek also acknowledged that it had inspired the development of Vietnam’s model (however, in the case of Malaysia’s Khazanah and Indonesia’s master plan for an SOE holding company, Temasek has refrained from making the same claim).

In fact, the super-holding company has been formed for Vietnamese SOEs. Under the name of the State Capital and Investment Corporation (SCIC), it holds the state’s share in the equitized SOEs. With 2000 SOEs in hand, the total book value is about 9,800 billion VND (over USD 600 million), with market value estimated to be around USD 3 billion.

Similarity also exists with Indonesia in regard to the sectoral holding company it aims to form. Vietnam’s SCIC has so far built
conglomerates in eight different sectors deemed strategic for the economy: coal and mineral; electricity (EVN); telecommunications; ship-building (Vinashin); rubber; oil and gas (PetroVietnam); insurance (BaoViet); and textiles (Vinatex). All of these companies together control 80% of the total SOE assets, with many of them enjoying monopoly positions or holding the dominant market share. This is akin to Indonesia, where the key sectoral holding companies together with champion SOEs are mainly in sectors where the companies have either monopolistic power (such as in the case of oil and gas) or have great potential based on comparative advantage (such as the planned mining and plantation holding companies).

Another interesting comparison is with regard to the rapid-expansionist behavior of the Vietnamese state-conglomerates in investing and diversifying to various sectors. Indonesian SOE Minister Sofyan Djalil also sees the logic of economies of scale and scope behind the plan to build SOE sectoral holding companies, enabling them to flex their muscles for expansion and growth.

Finally, the issue of legal hindrance exists in the case of both countries. Vietnam still lacks a clear legal framework, requires more transparency, and, as a country in transition from a socialist
command economy, must deal with some management issues in SOEs. Indonesia also has to deal with a lack of regulation on the holding companies, which the government is currently addressing, and needs much improvement in transparency and the development of managerial talent.

**China**

China is another example where the model is currently being implemented. Though not a Southeast Asian country, China is too important to be excluded from the analysis. China is set to be an economic as well as political superpower in the future, and the talk often focuses on how China is the market of the future. The fact that it is now also setting up an investment company to make more profitable use of its over $1 trillion in foreign currency reserves makes a consideration of the corporate governance of its SOEs important. The finance minister, Jin Renqing, said that Beijing would try to learn from the experience of other governments. He cited the

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example of Singapore’s Temasek Holdings. The growth in China’s foreign exchange reserves, the largest in the world, stand at about US$ 1.33 trillion. They are the result of the growth in China’s reserves, which is driven by the rapid growth of its exports, which in turn brings in dollars, euros and other foreign currency, and by the billions of investment dollars being poured into the country.

The investment agency China Investment is the biggest state-owned investment company in Asia with US$ 200 billion sovereign wealth fund. This is bigger than Temasek’s US$ 107 billion and second only to Norway’s $327 billion global pension fund. Having started operations on 29 September 2007, the investment agency is under the direct supervision of the nation's cabinet, the State Council.\(^{105}\)

The company may also help major Chinese SOEs expand overseas.

Similarly to Vietnam’s approach toward SOEs, China’s two-pronged strategy is based on the principle of “grasp the large, let go of the small” (Oi, 2005). China adopted a differentiated policy for dealing with firms of different size and importance. The large SOEs

\(^{105}\) “China Investment starts up operations”, International Herald Tribune, 30 September 2007.
are given different options for corporate restructuring, while the small and medium-sized SOEs are geared toward amalgamation with one core group of firms forming a conglomerate-style holding company.

One has to take into account that a key driving factor for the creation of this company is China’s accumulated foreign exchange reserves, with which the government seeks to increase returns, something very necessary in the context of China’s increasing trade surplus and trade frictions with other countries. It is therefore important to note that Indonesia’s planned SOE holding company, with foreign exchange reserves of only slightly over US$ 50 billion\textsuperscript{106}, would also have a different context in terms of economic prowess compared to its Chinese counterpart.

Lessons from China with regard to the restructuring of its SOEs are also important for Indonesia. It is especially so because China has also adopted this strategy of “restructure first, privatize second” in\textsuperscript{106} Based on the IMF’s data on current foreign exchange reserves, August 2007.
terms of rightsizing the SOEs. China has also been very careful to phase its restructuring by adopting the least disruptive strategy first and then privatizing (Oi, 2005). A study by Oi (2005) reveals important issues on China’s path to privatization which will also be important for Indonesia:

- Shareholding
  Shareholding becomes an option as a way to minimize the social impact of privatization in the form of lay-offs leading to unemployment. In fact, Oi argues that the distribution of shareholding in ownership of China’s SOEs to their employees is a source of jobs, economic turnaround, and capital.

- “Grasp the large, let go of the small”

- Merge resources and management skills

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107 It is important, as explained later in the chapter on Indonesia’s SOE governance, that the Indonesian government also carved out the “restructure-profitize-privatize” strategy.
Discussion and the Way Forward: The Political Economy Context of Managing Indonesian SOEs

Globalization and Democratization: Shareholder Value vs. Stakeholder Interest

The analysis found in this research work was based on the context of corporate governance in managing state-owned enterprises. It is very important to note that definitions in corporate governance have the tendency toward either one of the two orientations in business: Shareholder Value and Stakeholder Interest. The approach of New Corporate Governance, where principles of good corporate governance applied in a firm should be kept situational, strategic, integrated, and controlled (Hilb, 2004), believes in a balance between both value-orientations. This approach is emerging and in fact shows evidence of being taken as the main principle for defining corporate governance. New Corporate Governance (Hilb, 2004) is defined as a system "by which companies are strategically
directed, integratively managed and holistically controlled in an entrepreneurial and ethical way in accordance with a particular context”. The emphasis of this definition attempts to cover the value-orientations of both the shareholder and stakeholder perspectives. Particularly important in the definition is its emphasis on taking into account a particular context when applying corporate governance principles. In the context of Indonesia, political dimensions become important distinctive factors in comparison to its neighbors in Southeast Asia.

The political changes that have taken place in Indonesia have become even more important in the context of balancing shareholder value and stakeholder interests. The fall of the Soeharto regime in 1998, which ended the 32-years rule of the New Order era, was a turning point in many aspects of life in Indonesia, including business decision-making. Not only has that political process become more participatory, with a higher number of stakeholders involved, but also compromises between the interests of various stakeholders have become more likely. The relatively drastic transformation from a quasi-monoparty rule under Soeharto’s New Order, with a number of controlled opposition parties, to a multi-
party liberal democracy after the reformasi movement in 1998 is the dominant framework for the analysis in this study.

In the context of political decision making that influences state-owned enterprises, the discourse in the Indonesian parliament makes obvious which political economy doctrine in managing the SOEs is dominant. As elaborated above, Article 33 of the 1945 Constitution includes a very strong economic nationalism mandate regarding the role of the state in controlling strategic resources for economic development.

At the same time, globalization has brought increasing pressure for the profitable management of enterprises, not excluding the state-owned enterprises. Neoliberal doctrine on globalization also dictates that market openness become the recipe for economic growth and asserts that such openness will benefit the public at large. For example, Singaporeans have benefited from market liberalization in the country's telecommunications industry. Prices for international calls have fallen by 90 percent, while international leased line rates
have been cut by up to 95 percent since the government launched its full liberalization policy in 2000.\textsuperscript{108}

It is imperative for Indonesia to find a balance in managing its SOEs amid globalization, the concomitant pressure from shareholders to deliver value, and democratization, which means that more stakeholders’ interests are in play. That balance must be achieved in light of the expansive investment from neighboring state governments, which certainly triggers some degree of economic nationalistic sentiment. It might be the best option for the Indonesian government itself to play the role of strategic investor and manage its SOEs under the structure of a holding company to make strategic investments in various sectors and regions, as mapped-out in the government’s SOE master plan.

\textit{Contesting Political Economy Doctrines: State’s Sovereign Wealth Fund as Strategic Investor and Economic Nationalist Reactions}

Economic nationalist reactions to the takeover of strategic assets by foreign entities are understood as a response to the economic neo-

liberal recipe of economic growth and strategic expansion regardless of national boundaries. With the fall of the Berlin Wall and the end of the Cold War in the early 1990s, the role of economic socialism as one of the key schools of thought in political economy began to fade. This left economic nationalism and economic liberalism as the remaining competing doctrines.

In Thailand, economic nationalist responses to cross-border investments in ‘strategic assets’ were strong after the tax-free sale of the telecommunications group Shin Corp by Thaksin to Singapore’s Temasek Holdings. The event became one of the triggers for a political crisis, and political groups easily co-opted the situation, making it a matter of protecting national interests, which then brought economic nationalist sentiments into the public discourse.

Expansions by sovereign wealth funds like Temasek could have political implications that are problematic for diplomatic relations especially among ASEAN member states, as shown in the case of Temasek’s ventures in Thailand and Indonesia. Temasek’s strategic acquisition of majority ownership of Shin Corp, Thailand’s largest telecommunications company, as well as its purchase of a stake in Indosat, the second largest telecommunications operator in
Indonesia, drew heavy political fire, especially from the economic nationalist camp. Economic nationalists believe that strategic assets such as telecommunications should not fall into the hands of foreign parties. In the case of ShinCorp, it even helped to trigger a political crisis, which was followed by a military coup that brought down the government of Thaksin Shinawatra. Shinawatra’s family had formerly controlled ShinCorp and sold it to Temasek.

Another example of economic nationalist sentiment involves the recent series of debates on Malaysia’s Iskandar Development Region (IDR) in southern Johor, in which there was a prevalent sense that Singaporean investors were not welcome, despite the region’s being set to become a special investment zone with a set of more relaxed policies on requirements for equity ownership. Malaysia admits that Johor will benefit from the policy, as was acknowledged by PM Abdullah Badawi, who noted that this project aimed at making growth in the zone comparable to Singapore’s growth. However, economic nationalist sentiments, or in this case, with a touch of economic racism, are still strong within some factions of the Malaysian political leadership.
Elsewhere in the world, we find instances of economic nationalist responses, e.g., resistance to a proposed takeover of the French steel company Arcelor by Mittal of India, to a takeover bid for one of America’s oil giants, Unocal, by China’s CNOOC, and the French government’s listing of Danone as a 'strategic industry' to pre-empt a potential takeover bid by Pepsi.

Helleiner (2002) is therefore convinced that while economic nationalism should still be seen as a powerful ideology, its relationship to the policy goals of economic liberals is ambiguous. It is clear that, in Asia’s industrializing countries, many of the key policymakers in are actually technocrats who subscribe to economic liberalism as a political economy school of thought. It is, however, the politicians, most of who are not in the executive branch but members of parliament, who wield economic nationalism in order to influence policymaking.

Some researchers such as Baughn and Yaprak (1996) have found economic nationalism to be linked with personal job insecurity, authoritarianism, and intolerance of ambiguity, as well as to be negatively related to individual cosmopolitanism. Some might go even further and say that it reflects a “xenophobic” response, giving
voice to a nation’s own inferiority complex in the face of more advanced nations\textsuperscript{109}.

However, corporations and governments cannot help but to always take this matter into account when thinking of making cross-border investments, especially in sectors deemed strategic for the host country’s nation. Risk management is an absolutely essential element in managing investment portfolios. From among a number of risks entailed in doing business, country risk, with the political climate being the dominant variable, might be the most difficult to measure but is clearly not the least important. Political risk can also be crucial as it might be the least known by the investing parties, especially if the investment target happens to be in a completely different political system, structure, and culture.

Potential economic nationalist response in the home country of the investment target is a country risk that might be beyond calculation, but can be very costly if neglected. Nationalism as a political ideology has a long tradition and history. Economic nationalism as a political economy school of thought has strong roots in a number of political parties and among the political elite, especially in

industrializing Asia. Its importance cannot be underestimated, making the issue of engaging stakeholders more relevant than ever. It is imperative for corporations and governments alike to have political risk soundly incorporated into an investment decision-making framework and to have the right strategy in engaging the critical stakeholders.

Managing the Impact of Economic Nationalism in Indonesia’s Quest To Build an SOE Holding Company

In Indonesia, the view of economic nationalism seems to be dominant in response to globalization, especially since Article 33 of Indonesia’s 1945 Constitution stipulates that “Sectors of production that are important for the country and affect the life of the people shall be controlled by the State” (paragraph 2) and “Land, water and the natural riches contained therein shall be controlled by the State and exploited to the greatest benefit of the people” (paragraph 3). These serve as the principal argument used by economic nationalists to promote the limitation of foreign ownership in certain sectors and thus require a strong role of the SOEs. Their
argumentation also includes the notion that the telecommunications sector is a strategic sector which should not fall under foreign ownership.

In its recent negative list of investments, the Indonesian government has included a number of key sectors with limits on new foreign investment. This list, covering, among others, the telecommunications sector, is seen by analysts as an attempt to limit overseas control of strategic industries. Telecommunications was not the only sector included in this list. In fact, the list deals with 15 sectors and more than 200 types of businesses. Analysts also believe that the economic nationalist lobby, especially within the parliament and other stakeholders, including interest groups, is behind this move, which is believed to be seeking limitations on the presence of Temasek and Khazanah.

Temasek’s and Khazanah’s international expansion is viewed by the Indonesian public with both awe and envy, especially since Temasek and Khazanah have a strong presence in Indonesia's telecommunication and banking sectors.
Indonesia's mobile telephone sector has been the most penetrated by foreign investment.\textsuperscript{110} Temasek’s subsidiary Singapore Telecom (SingTel) Group owns 35% of Telkomsel, Indonesia’s biggest mobile operator, while the remaining 65% is still owned by the Indonesian government. Singapore Technologies Telemedia (STT), a wholly-owned subsidiary of Temasek, indirectly owns 31.4% of Indosat, the second largest operator, through its own subsidiary Asia Mobile Holdings (AMH). AMH, which has a total stake of 41.94% in Indosat, is 75% owned by STT and 25% by Qatar Telecom. The state holds a 14.6% stake in Indosat, with the investing public owning the remaining 43.4%. Not only Singapore’s Temasek, but also Khazanah Malaysia owns 16.81% (direct) and 59.67% (via Telekom Malaysia) of Excelcomindo, Indonesia’s third largest mobile operator. There are further examples of the foreign presence in the Indonesian telecommunication sector: Saudi Telecom has bought a 51% share of Natrindo (Lippo Telecom) from Maxis Malaysia and Qatar Telecom, together with STT, has a 25% share in AMH.

\textsuperscript{110} Sources: various Annual Reports 2006.
The Indonesian banking sector also has a significant foreign presence\textsuperscript{111}, again with Singapore’s Temasek and Malaysia’s Khazanah as the dominant foreign investors. Through Asia Financial Holdings, Temasek owns 59\% of Bank Danamon and 35\% of Bank Internasional Indonesia (BII). Khazanah owns 88.73\% of Lippo Bank through Santubong Investments. Through Bumiputra Commerce Holding Berhad, it also owns 63.86\% of Bank Niaga. Apart from Temasek and Khazanah, the presence of Singapore and Malaysia is also indicated by their ownership of other entities.

A combination of economic nationalism and eagerness to also reap the benefit of economic globalization are driving Indonesia to think of ways to have SOEs also be regarded with dignity as global or at least regional players. Of the current 139 Indonesian SOEs, few are active internationally. One of the very few is Pertamina’s recent partnership with China National Petroleum Corp. to explore potential for oil reserves in Sudan\textsuperscript{112}. Being the most profitable SOE with a supposedly high potential to leverage the competitive

\textsuperscript{111} Sources: various Annual Reports 2006.
\textsuperscript{112} Ng, Eric. “PetroChina parent joins Sudan oil venture; CNPC entrenches position as top foreign investor in country targeted over rights”, South China Morning Post, July 3, 2007.
advantage of Indonesia as an oil-producing country, Pertamina is one of the logical choices for an Indonesian SOE ‘champion’. Even so, in this case, Pertamina was not seen as taking the initiative to go forward, since its Chinese counterpart was the one calling the shots, thanks to its intensive relationship with the African nation.

It is against this backdrop that the master plan for Indonesian SOE rightsizing aims at creating strong and profitable SOEs able to deliver benefits for the state as well as to become regional champions, thereby building the backbone of ‘Indonesia, Inc’ (Abeng, 2001). In order to achieve success, the plan must have the support of the political leadership.

**Democracy and Yudhoyono’s Presidency: Challenge and Opportunity in Managing Indonesian SOEs**

It is well understood that the Indonesian government plan to build a holding company structure is the path to building a “sense of
corporation” and to minimizing the sense of bureaucracy that is prevalent in a government structure like the ministry of SOEs. However, it is clearly too simplistic to think that Indonesia can merely follow Singapore’s and Malaysia’s example and set up an investment holding company to manage its GLCs and expect it to succeed in transforming its Badan Usaha Milik Negara (BUMN), the Indonesian term for SOEs. First of all, the term BUMN itself presents a challenge for Indonesian SOEs to define their role and responsibility in the context of Indonesian socio-political mindset. The term “Badan Usaha” (profit-making institution) is unfortunately less emphasized than “Milik Negara” (state-owned) in the context of Indonesian SOEs. Although it has been noted by some that the assets of Indonesian SOEs do not equal the assets of the Indonesian government, it is still difficult to shake off the assumption that the government, or even other political elites, has

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113 Nahadi, Bin: “Penguatan Sense of Corporation di BUMN” (Strengthening The Sense of Corporation at SOEs), Bisnis Indonesia, Friday, 16 March 2007.
114 Rajagukguk, Erman: “Kekayaan BUMN Persero bukan kekayaan negara” (Assets of SOEs does not equal state assets), Kompas, 4 October 2006. Under Company Law, Law No. 1/1995, it is stated that SOE banks are regulated by this law, and that assets of SOE banks are ‘separated’ from state assets.
the right to interfere in SOE decision making processes\textsuperscript{115} in the name of protecting the state’s interests.

Democratization in Indonesia has become even more important in the context of balancing shareholder value and stakeholder interests. Not only has the political process become more participative, with a higher number of stakeholders involved, but also compromise between the interests of various stakeholders is more likely. It is imperative for Indonesia to find a balance in managing its SOEs amid globalization, the pressure from shareholders to deliver value, and democratization, with more diverse stakeholder interests. The parliament is a clear example of these stakeholders (dubbed by some as ‘stakeholders eager to play the role of shareholders\textsuperscript{116}’), who often have their say in decisions regarding SOEs. The difficulty lies in the fact that decisions regarding SOEs will always be politically-driven, even though it is understood that they should be commercially-driven.

\textsuperscript{115} “BUMN Sering Diintervensi” (SOEs Are Often Intervened), Detikfinance.com on Thursday, 12 April 2007.

\textsuperscript{116} Author’s interview with Laksamana Sukardi, former Minister of SOEs, Saturday, 24 March 2007.
Take the example of the nomination and appointment of SOE directors: Although a closed recruitment process within the company’s circle is preferred by the government, as it is a matter of economic regime, some in the parliament argue that it is in the political realm and thus requires a more open process involving the public. The government says that the enterprises’ business interests must be protected, while parliament insists that all agencies with state money should be subject to public scrutiny.\(^{117}\)

The master plan for SOE restructuring to form sectoral holding companies is also subject to scrutiny by the parliament. Though the scrutiny is well intentioned, parliament’s involvement may have to be limited to a certain degree, especially if one considers past experience in this area, where the effort to build holding companies for fertilizers and ‘strategic’ industries did not yield the expected results. The government also expects that SOEs will act more like autonomous corporations in the future, without the need for a special ministry\(^ {118}\). Although some may question it, the success of Temasek Holdings is due to its principle of running the business

\(^{117}\) “Appointment of state firm heads must be out in the open”, The Jakarta Post, 16 August 2007.

commercially without political interference from Singapore’s Ministry of Finance\textsuperscript{119}.

The current Indonesian presidency of Susilo Bambang Yudhoyono can be seen as an opportunity for the SOEs to reform themselves. Having been elected on the platform of fighting corruption, he has urged heads of SOEs to put this struggle high on their agenda\textsuperscript{120}. However, he has also said that the government’s commitment to wiping out corruption-, collusion-, and nepotism-tainted practices should not make the management of state firms afraid to implement all the existing programs, as such fear would adversely affect the companies` performance.

This is an important statement since some now believe that the heavy-handed anti-corruption drive can be ‘blamed’ for the low government expenditure and lack of lending to the real sector and hence also blamed for lack of development\textsuperscript{121}. The president has

\textsuperscript{119} As stated in “Temasek Review 2007” and author’s interview with Myrna Thomas, Managing Director for Corporate Affairs, Temasek Holdings, Friday, 14 September 2007.

\textsuperscript{120} “President asks state firms to shake off stigma as hotbed of corruption”, Antara, 12 April 2007.

\textsuperscript{121} Salim, Felia: “Public Forum on Governance in Indonesia”, presentation at Institute of Southeast Asian Studies, Singapore, 30 August 2007. This is based on cases where many state-banks are now reluctant to disburse loans
assured SOE chiefs that SOE losses in doing business do not automatically count as corruption, unless there is misuse of funds and authority for self-interests\textsuperscript{122}. Although a relief, it might not be sufficient as an assurance, given the fact that the charge of corruption has become a weapon for political groups to fight against each other. He has also increased pressure to yield profits, telling some SOEs to end their streak of loss-making performances\textsuperscript{123}.

However, he has also asked that profit not be achieved by extraordinary measures, by ‘forcing people’\textsuperscript{124}. This refers to the need to apply a level playing field between SOEs and private sector firms with regard to access to financing, marketing of products as well as equitable treatment of shareholders, which are among the principles for corporate governance of state-owned enterprises\textsuperscript{125}.

to businesses out of fear that bad loans could be deemed as act of corruption since it can cause losses to the state.

\textsuperscript{122} “SBY Minta Direksi BUMN Tak Takut” (SBY Told SOEs Directors Not To Fear), Detikfinance.com, Thursday, 12 April 2007.


Summing up briefly, there seem to be high hopes placed on the leadership of President Susilo Bambang Yudhoyono and SOE Minister Sofyan Djalil in transforming Indonesian SOEs to be professional and profitable corporations. The master plan for streamlining the number of SOEs to achieve the ‘right size’ also has the right target, inspired by how Singapore and Malaysia manage their government-linked companies. However, caveats to the plan are appropriate due to higher complexity in decision-making in the context of democratic governance. It remains a challenge for the Indonesian government to use democratic governance as the basis to achieve good corporate governance for its enterprises.

Conclusion
The contextual differences between Indonesia and its two Southeast Asian neighbors managing the GLCs under an investment holding company cannot be neglected. Apart from the differences stemming from their disparate colonial legacies (Singapore and Malaysia have the British common law system, while Indonesia inherited civil law from the Dutch), the political economy dimension and political environment are key issues that need to be taken into account.

States in civil law countries like Indonesia have historically been more interventionist than states in common law countries and have consequently tended to provide lower levels of protection to private property (La Porta et al. 1998, 2000). The political economy dimension is important, as it will provide the foundation for policies on the strategy development of SOEs/GLCs expansion. It is even more important in the context of Indonesia’s young multi-party democracy. Making politically sensitive decisions with regard to state assets would be subject to scrutiny from various groups of stakeholders: from SOEs’ labor unions, members of parliament, civil society organizations and vested interest groups. All of these groups can, in one way or another, still throw a wrench into the SOE master plan for the formation of a holding structure. Rosser (2005)
sees the political economy dimension within the context of a power struggle between the politico-bureaucrats, who prefer to maintain the current corporate governance structure from which they benefit, and the technocrats, aiming toward the Anglo-American model of corporate governance.

In brief, the formation of an Indonesian national SOE holding company might be the right means to build a better structure for the corporate governance of Indonesian SOEs. There is a global trend toward managing state-assets “under one roof” as a logical consequence of the need for better performance control and strategy direction. This would be in line with Wong’s (2004) three pillars of SOE reform: avoiding conflicting objectives, minimizing political intervention and improving transparency. It is the process of building this structure in Indonesia that we need to watch cautiously and vigilantly. Caution is required to make sure that various stakeholders of SOEs do not hold the master plan hostage to political bickering, and vigilance is needed to make certain that the government as an SOE shareholder does not overlook the contextual differences Indonesia has with its ASEAN neighboring countries. If
those two elements are not applied, then the vision for Indonesia Inc. will only be wishful thinking.

It is surely a challenge to find a way to solve the problems of corporate governance in Indonesia especially for its state-owned enterprises. The pessimistic view of agency theory is that both principals and agents are human beings controlled by rational self-interested motives. This view expects a more difficult situation for social objectives to be achieved by state-owned enterprises while also not forgetting their goal of maximization goals. Singapore’s government investment arm, Temasek Holdings, needs to be proven as a compelling model of corporate governance for state-owned enterprises where both shareholder- and stakeholder-oriented outcomes can be achieved. Once there are more opportunities for than hindrances to applying the model to the Indonesian context, it might be worthwhile to consider the model for a governance structure of Indonesian state-owned enterprises.

A case study to compare the two different models, with both Temasek and Khazanah as the GLCs investment holding arm model and Indonesia and Thailand as countries planning to adopt such model, will be a suitable method for culling lessons from the
Temasek Holdings model for Indonesian state-owned enterprises. However, a careful consideration of differences must be taken into account to examine whether it is possible for Indonesia to adopt such model.

The agency theory perception on state-owned enterprises has been very pessimistic, especially with regard to conflicting interests that may arise in the monitoring and controlling by government institutions. This is especially true in the case of Indonesia, leading to a situation where privatization might be the best way to ensure that the governance of these enterprises is properly conducted.

The analysis of Temasek Holding’s corporate governance, however, shows that being the holding of Singapore government-linked companies does not necessarily make it unable to practice good corporate governance. In fact, the corporate governance of TLCs won several awards and recognition in Singapore as evidence of its good practice. Finally, the value created by Temasek for its shareholders, yielding over US$ 100 billion portfolio value with a 27% shareholder return, is clearly also a result of its focus on sound corporate governance as one of its important pillars.
It poses another question for Indonesia: Can its SOEs be managed under the structure of a private investment holding, with the government as its major shareholder, instead of under the Ministry of SOEs as a government body with a strongly bureaucratic character? This will enable the structure to have the nature of a private institution, while ensuring that government ownership of state assets and strategic resources still remains.

In a nutshell, the Indonesian government will face a more dynamic situation in its effort to form and manage a holding company for its state-owned enterprises. This is especially true in comparison with Singapore and Malaysia, which undertook the creation of their government investment holding company in a political environment which was less competitive, under tighter control, and less open to participation. These differences will doubtless lead to a situation in which the Indonesian government has to juggle pressures from globalization and neoliberal economic doctrine with the impact of democratization, which would open the way for stronger voices of economic nationalism.

As a result, it is predicted that the Indonesian government’s decision making with regard to its managing state resources will unavoidably
be more cautious and considerably slower. This could come at the expense of being less responsive to global competition, but would arguably be better for the long run as more concerns are taken into account.

In conclusion, the Indonesian government’s goal of having its SOEs managed under a holding structure requires that the government rightsize its presence and ownership of domestic strategic resources, and that cross-border strategic investment be undertaken in order to establish an international presence. It remains to be seen whether and when Indonesia follows the trend of managing state assets “under one roof”, as is now the trend among Asia’s industrializing countries.
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School of Public Policy, National University of Singapore.


APPENDIXES

Appendix 1: List of Interview Questions

Singapore’s Government Investment Holding and the GLCs
1. What is the role of the state in Singapore in driving the GLCs to success?
2. What are the key success factors of the government investment holding?
3. How does such a holding structure help GLCs to strike a balance between shareholder value and stakeholder interest?
4. How does the holding structure help to build 3 pillars of SOE reform (Wong, 2004)?
   i. by avoiding conflicting objectives
   ii. by insulating companies from political interference
   iii. by improving transparency
5. What are the key advantages and disadvantages of the holding structure?

The Impact of Singapore GLCs on the Formation of Malaysia’s Government Investment Arm (Khazanah Nasional Berhad) and Indonesian SOEs’ Holding
1. How significant is the impact of Singapore’s Temasek Holdings as a model for government investment holding in the formation of Khazanah in Malaysia?
2. Are there **contextual differences** – historical, legal, social and political issues – in Indonesia compared to Malaysia and Singapore, which could make this recipe for strong state involvement not work the same way elsewhere?

3. On the other hand, **what supporting factors** do you think would make such a model applicable for Indonesia?

4. What are **the lessons learned for Indonesia** from this case for:
   - fostering **competitiveness and efficiencies through synergy**?
   - **corporate governance** principles and conduct?
   - **strategy alignment and value creation** to be regional/global players?

**History of Indonesian SOEs Holding (BUMN Holding)**

1. Can you explain the **development of and progress on plans for the creation of an Indonesian BUMN Holding** from the era of Mr. Tanri Abeng up to now?

2. In your opinion, has this been a **significant and valuable development**?

3. What are the **obstacles to the development of an Indonesian BUMN Holding**?

4. How significant is the **impact of Singapore’s Temasek Holdings** as a model for government investment holding for the formation of BUMN Holding?
The Single Presence Policy (SPP) and Its Implications on the Formation of BUMN Banks Holding

1. What is your opinion on Bank Indonesia’s Single Presence Policy (SPP) on:
   a. **encouraging banking consolidation** to conform to the Indonesian Banking Architecture (Arsitektur Perbankan Indonesia-API)?
   b. pushing forward the **creation of holding companies for banks with the same controlling shareholder**, in particular the state-owned banks leading to the formation of BUMN Banks Holding?
   c. affecting the **climate for –especially foreign– investment** in Indonesia?

2. How do you perceive the **creation of an Indonesian –especially BUMN– Bank holding** structure would help in:
   a. **synergy** and **value creation**?
   b. **efficiency improvement**?
   c. **strategy alignment**?
   d. enhancing **economies of scale to be regional or global banking players**?
   e. **corporate governance improvement**, both from the compliance (**conformance**) and the performance perspective?
Appendix 2: List of Interviewees

Singapore

- Ms. Serena Khoo and Ms. Daliea Mohamad: Director for Corporate Affairs, Temasek Holdings Pte. Ltd., Singapore, 14 September 2007
- Mrs. Kuan Kwee Jee: Senior Vice President for Strategic Relations/Corporate Communications, Singapore Technologies Telemedia (STT)\textsuperscript{126}, 14 September 2007

Malaysia

- Mr. Ahmad Shahizam Shariff: Managing Director Office’s Senior Vice President of Khazanah Nasional Berhad, 9 February 2007
- Dato’ Dr. Michael Yeoh: CEO of Asian Strategy and Leadership Institute (ASLI), a Malaysian policy think-tank, 8 February 2007
- Paul Chan: Secretary General of Malaysian Institute of Corporate Governance, 17 January 2007

Indonesia

- Prof. Dr. Djisman Simanjuntak: Corporate Governance Expert at CSIS (Centre for Strategic and International Studies) Indonesia and Executive Director of Prasetiya Mulya Business School, 13 December 2006
- Mr. Umar Juoro: Commissioner of Bank International Indonesia and Senior Fellow The Habibie Center, 13 December 2006

\textsuperscript{126} Written interview per email.
• Mr. Martiono Hadianto: President Commissioner of PT. Pertamina, 14 December 2006
• Mr. Setyanto P. Santosa: Commissioner of PT. Indosat, 18 January 2007
• Mr. Sumaryanto Widayatin: Commissioner of PT. Jasamarga, 19 January 2007
• Mr. Pahala N. Mansury: Executive Vice President (EVP) Coordinator Finance & Strategy and Chief Financial Officer (CFO) PT. Bank Mandiri, 1 February 2007
• Dr. Jos Luhukay, National Committee of Good Corporate Governance and former CEO of LippoBank, 27 March 2007
• Dr. Tony Prasetiantono, Chief Economist of Bank Negara Indonesia, 28 March 2007
• Ms. Felia Salim, Commissioner of Bank Negara Indonesia, 28 March 2007
• Mr. Pandu Djajanto, Expert Staff on Corporate Governance for the Minister of State-Owned Enterprises, 2 April 2007
• Mr. Laksamana Sukardi, former Minister of State-Owned Enterprises, 24 March 2007
• Mr. Tanri Abeng, former Minister of State-Owned Enterprises, 18 March 2007
ABOUT THE AUTHOR

AGUNG WICAKSONO

CURRENT STATUS

- Ph.D. in International Management in Asia from the University of St. Gallen, Switzerland with dissertation on “The Holding Company as Corporate Governance Structure of Government-Linked Companies in Singapore and Malaysia: Applicability for Indonesian State-Owned Enterprises”
- Coordinator of Jakarta Executive MBA Program at School of Business and Management, Institut Teknologi Bandung (SBM ITB) and Assistant Professor in Business Ethics, Cross Cultural Management and International Business.
- Affiliated to the Institute of Southeast Asian Studies (ISEAS) Singapore as Visiting Fellow and The Indonesian Institute for Corporate Governance (IICG) as Senior Researcher and assessor of Corporate Governance Perception Index (CGPI).
- Experience in management consulting and practice-oriented management research in Southeast Asia and German-speaking part of Europe

PERSONAL DATA

- Place and Date of Birth: Surabaya, Indonesia, 13th December 1976
- Citizenship: Indonesia
- Marital status: Married, one child
## MANAGEMENT CONSULTING EXPERIENCE

### Ministry of Trade, Republic of Indonesia – Advisory for Creative Industry Roadmap

**February – April 2008**
- A team member of Indonesia Design Power (IDP) as advisory group for Indonesian Ministry of Trade to develop the roadmap for Indonesian creative industry
- Conducted desk research and focus group discussions (FGD) with Indonesian creative industry players to identify necessary policy areas and develop strategic plan for the respective sub-sectors of creative industry
- Provided benchmark on the governance mechanism of creative industry in ASEAN neighboring countries (Thailand and Singapore)

### Case4de – Part-time Advisor to Regional Director Asia

**2005 – 2007**
- Advised the set-up process and conducted market research for Southeast Asian (Indonesia) and Northeast Asian (China) representative offices of Case4de, a German-based engineering design & technology consulting firm in the area of transportation industry

### A.T. Kearney, Southeast Asian Practice

**April – September 2004**
- Business Analyst in a top-tier strategy consulting firm
- Projects: 3G strategy for a Malaysian mobile telecommunication provider, as well as involved in developing client acquisition at several banks in Indonesia and Malaysia

### Ernst & Young Advisory Services, Indonesia

**June 2003 – April 2004**
- Associate Consultant at Business Risk Consulting Division
- Projects: risk management at two Indonesian major private banks; corporate governance and performance audit at a state-owned enterprise (transportation)

### Roland Berger Strategy Consultants, Hamburg

**November 2002 – March 2003**
- Post-Graduate Intern at a European leading strategy consulting company
- Competence Centre: Corporate Strategy (strategy projects at two leading European business school and due diligence study for a German chemical conglomerate)
# ACADEMIC EXPERIENCE AND EDUCATION

<table>
<thead>
<tr>
<th>October 2004 – October 2007 (graduation in Spring 2009)</th>
<th>Universität St. Gallen (HSG), Switzerland – Ph.D. International Management in Asia</th>
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<tbody>
<tr>
<td>■ 2004-2005: Awarded Swiss Government Scholarship and attached as researcher at Asia Research Centre, Universität St. Gallen (ARC–HSG)</td>
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<td>■ 2006: Chaired the Singapore-Indonesia Study Trip 2006 for students from Swiss universities (St. Gallen, Bern and Geneva) as a business study mission of ARC-HSG</td>
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<td>■ 2005-2007: Teaching Assistant to Prof. Chong at the HSG Asia Term in SMU and supervised bachelor students’ Integration Seminar projects</td>
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<th>July 2006 – October 2008</th>
<th>Institute of Southeast Asian Studies (ISEAS), Singapore</th>
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<tr>
<td>■ July 2006 – October 2007: Research Associate in Regional Economic Studies (RES) to conduct fieldwork for Ph.D. dissertation on corporate governance of SOEs. Also an Assistant to Energy Forum Coordinator &amp; Assistant Editor, ASEAN Economic Bulletin</td>
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<tr>
<td>■ October 2007- October 2008: Visiting Associate (affiliated non-resident expert on a voluntary unpaid basis) with research area on corporate governance of SOEs, internationalization strategy of firms and Indonesian political economy</td>
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<th>November 2007 – January 2008</th>
<th>School of Business and Management, Institut Teknologi Bandung (SBM – ITB)</th>
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<tr>
<td>■ Project leader of Social Enterprises for Economic Development (SEED) and International Colloquium on Context-Based Management Research in cooperation with Prof. Chong Li Choy of Asia Research Centre, Universität St. Gallen (ARC-HSG) to improve cross-cultural learning and research at SBM ITB</td>
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<tr>
<td>■ Research on Knowledge Management and Smart</td>
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<td>Year Range</td>
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<tr>
<td>1995–2000</td>
<td>Institut Teknologi Bandung (ITB), Indonesia</td>
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<tr>
<td></td>
<td>Bachelor of Science in Industrial Engineering</td>
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<td>Ranked 3rd among graduates of Industrial Engineering on July 2000 graduation with GPA 3.12 (in a scale of 4.00). Awarded the EPSON Scholarship during final year</td>
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<td>2000–2002</td>
<td>Technical University Hamburg Harburg (TUHH), Germany</td>
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<td>Master of Science in Int’l Production Management</td>
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<td>A leading technical university offering the first English-taught international master program in Germany</td>
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<td>Best graduate in class with GPA of 1.8 (in German grading system 1.0 represents the best grade and 4.0 is the minimum grade to pass)</td>
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<td>2000–2002</td>
<td>Northern Institute of Technology Management (NIT), Germany</td>
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<td>Professional Master in Global Technology Management</td>
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<td>The private partner of TUHH funded by German leading companies offering courses in management, business administration and soft-skills qualifications</td>
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<td>A double-degree course with TUHH, granted for selected students, with scholarship from Körber Foundation</td>
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<td>Top 5% in class with GPA of 1.6 (in German grading system 1.0 represents the best grade and 4.0 is the minimum grade to pass)</td>
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<td>Selected to deliver convocation speech at Graduation Ceremony in Hamburg City Hall</td>
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<td>July – December 2005</td>
<td>Singapore Management University (SMU)</td>
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<td>Research proposal (Vorstudie) for Ph.D. fieldwork</td>
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National University of Singapore (NUS)

Exchange Student in Faculty of Business Administration

- Courses: Industry & Competitive Analysis, Asia Pacific Business, Creative Thinking & Problem Solving with scholarship from Singapore International Foundation.

INTERNSHIPS AND STUDENT JOBS

Basler Vision Technologies AG, Ahrensburg

May - October 2002


Hauni Maschinenbau AG, Hamburg

August 2001 – March 2002

- Internship and student project in marketing and sales department of a tobacco machinery company, a market leader in delivering complete tobacco machinery system.

PT. Air Cerdas Ganesa, Bandung

Summer 1999

- Internship: production unit of a mineral water company

Studio Management of Industrial Engineering, ITB

1997–2000

- Research assistant, teaching assistant and final project in Business Ethics
- Head of Organizing Committee for National Seminar on Business Ethics & Good Corporate Governance (1999)

ORGANIZATIONAL ACTIVITIES

- 2007: Coordinator and Founder, IA-ITB Komisariat Singapura (ITB Alumni, Singapore Chapter)
- 2000-2002: Speaker of TUHH International Master Students, Germany
- 2001-2003: Executive Board (Department Head, Academic Seminar and Human Resource Development) of Indonesian Scientist and Academician Association in Germany (IASI)
- July-November 1999: Indonesian delegate in Singapore International Foundation (SIF) – ASEAN Visiting Student Fellowship, Singapore
- May 1999: Indonesian delegate to 3rd Hitachi Young Leaders Initiative (HYLI), Kuala Lumpur
Rektor for Election Watch and Democracy Development

- 1997-1998: President, Industrial Engineering Student Union (MTI) ITB
- February- November 1998: Secretary General, Forum for Student Union Presidents (FKHJ) ITB

**LANGUAGE PROFICIENCY**

- Bahasa Indonesia: mother tongue
- English: fluent in oral and written
- German: fluent, with *Zertifikate Deutsch* and *Zentrale Mittelstufe Prüfung* from Goethe Institut Hamburg

**PUBLICATION, OPINION AND CONFERENCE/SEMINAR**

- Speaker: “*Indonesian State Owned Enterprises: Between Economic Nationalism and Globalization*”, Seminar at The Truman Institute, Hebrew University, Jerusalem, 1 December 2008
- TV Interview: “*Economic Nationalism in Indonesia*”, Bloomberg TV, Emerging Asia, 28 November 2008
- Speaker: “*Coordination and Communication*” at Leadership Training for Education Officers of Nanggro Aceh Darussalam Province by the German Agency for Technical Cooperation (GTZ), Banda Aceh, 5 August, 2008
- Opinion: “*When business and politics collide*”, at The Jakarta Post, 28 July 2008
- Speaker: “*Knowledge Transfer in The Context of Indonesian Culture*” at Workshop by GTZ (German Agency for Technical Cooperation), Banda Aceh, 12 June, 2008
• Speaker: “Indonesia’s State Owned Enterprises Rightsizing: Toward Holding Companies?”, Seminar at ISEAS Singapore, 26 March 2008
• TV Interview: “Indonesia’s State Owned Enterprises Masterplan”, Bloomberg TV, Emerging Asia, 26 March 2008
• Speaker: “Governance of State-Owned Enterprises in Southeast Asia and Freedom of Information Act As an Anti-Corruption Measure”, Discussion at Indonesian Corruption Watch (ICW), 4 December 2007
• Paper & Presenter: “Indonesia as Offshoring Destination in Southeast Asia: Case Study on Internationalization of an Aerospace Engineering and Design Company To Indonesia”, co-authored with Madouii, N. & Ulya, A., 2nd Regional Conference on Aerospace Science, Technology and Industry, Institut Teknologi Bandung, 4 September 2007
• Opinion: “Indosat’s untangled Web: Government, STT, Altimo”, at The Jakarta Post, 3 September 2007

Chairperson: “Governance in Indonesia”, Public Forum at ISEAS Singapore, 30 August 2007

Opinion: “Kepemimpinan yang Melayani (Leadership that serves)“, Book Review on Servant Leadership: The Ultimate Calling to Fulfill Your Life’s Greatness by Donald Lantu, Erich Pesiwarissa, Augusman Rumahorbo (Gradien Books, 2007) in Kompas, Jakarta, 26 August 2007


Assistant Editor: “ASEAN Economic Bulletin”, Volume 23 Number 3, ISEAS, Singapore, December 2006


Paper & Presenter: “Situational Corporate Governance of State-Owned Enterprises in Southeast Asia: Applicability of Government Investment Holding Arm As Governance Structure”, 3rd Workshop on Corporate Governance, European Institute for Advanced Studies on Management (EIASM), Brussels, 9-10 November 2006
• Speaker: “Corporate Governance of State-Owned Enterprises in Southeast Asia: Balancing Shareholder and Stakeholder Value to Be Profitable and Socially-Responsible Firms”, IBEM Conference, San Beda College of Arts & Social Sciences, Manila, 16 September 2006
• Speaker: “E-Governance for Indonesia” at In-House Training to Government of Simeulue Municipality, Province of Nanggrooe Aceh Darussalam, 24 April, 2006
• Speaker: “Application of Lead Market Theory as A Framework for Product & Technology Policy: Case of Indonesia & South East Asia”, Seminar of Indonesian Scientist & Academician in Germany, at Indonesian General Consulate (KJRI) in Hamburg, March 2003