

Restructuring Garuda Indonesia: High Tide in Hard Times*

Rio Christiawan**

Ridha Aditya Nugraha***

Januar Agung Saputera****

บทคัดย่อ

บทความนี้จะพิจารณาวิกฤติการเงินของสายการบินการ์ดูตา อินโดนีเซีย และความพยายามในการช่วยเหลือสายการบินดังกล่าว โดยจะวิเคราะห์กระบวนการปรับโครงสร้างท่ามกลางจำนวนหนี้ก้อนใหญ่ของสายการบินที่ยังคงดำเนินการอยู่จนถึงเดือนพฤษภาคม พ.ศ. 2565 ประเด็นหลักที่จะอภิปรายในบทความคือทางเลือกการปรับโครงสร้างที่เป็นไปได้ อันได้แก่ การทำสวอปในตราสารทุน และการระงับการชำระหนี้ ทั้งนี้ ในบทความได้เสนอทางออกที่เหมาะสมในการปรับโครงสร้างของสายการบินการ์ดูตา อินโดนีเซีย เพื่อการเตรียมพร้อมให้สายการบินแข่งขันได้อีกครั้งหลังสถานการณ์โควิด-19 คลี่คลาย

Keywords:

การ์ดูตา อินโดนีเซีย การเงิน การปรับโครงสร้าง

* การปรับโครงสร้างสายการบินการ์ดูตา อินโดนีเซีย: กระแสน้ำเชี่ยวในเวลาวิกฤติ

** Associate Professor, Faculty of Law Universitas 17 Agustus 1945 Jakarta, Indonesia. Comments should be addressed to rio.christiawan@uta45jakarta.ac.id.

*** Air and Space Law Studies - International Business Law Program, Universitas Prasetiya Mulya, Indonesia. Comments should be addressed to ridha.nugraha@prasetiyamulya.ac.id.

**** Faculty of Law, Universitas 17 Agustus 1945 Jakarta, Indonesia. The views expressed are purely those of the authors.

วันที่รับบทความ 12 เมษายน 2565; วันแก้ไขบทความ 26 พฤษภาคม 2565; วันตอบรับบทความ 26 พฤษภาคม 2565

Abstract

This article examines Garuda Indonesia's financial crisis and the efforts taken to save it from the said crisis. The analysis follows the ongoing progress of Garuda Indonesia restructuring in the wake of its huge debt up until May 2022. The main issues discussed in this article are the possible restructuring options namely debt-to-equity swap option and suspension of debt payment. In the final chapter, this article offers the proper solutions in restructuring Garuda Indonesia while also preparing the flag carrier to compete in post Covid-19 era.

Keywords:

Garuda Indonesia, financing, restructuring

1. Introduction

Garuda Indonesia (“GI”) as the Indonesian flag carrier is in a worrying condition after their accumulated debts have exceeded their equity and valuation. GI is reported to have suffered losses of up to US\$ 100 million per month, with creditors claiming up to IDR 198 trillion of unpaid debt— albeit not all of them are verified, such amount is bigger than their equity as exposed to public during the Covid-19 pandemic.¹ Their cash flow is also expected to suffice for only a short time given its burden and high fixed cost.²

This article explores several options to rescue GI, which is an airline managed by a state-owned enterprise (*Badan Usaha Milik Negara* or BUMN), from this worrisome situation. GI became a listed company at the Indonesian Stock Exchange (IDX) since its initial public offering in February 2011. Bankruptcy proceeding is clearly not an effective and efficient option considering its status as a public company listed at IDX. Besides the long process of delisting, in reality state-owned enterprises have been immune towards bankruptcy through annulments of past bankruptcy verdicts at the supreme court.³ Even though the bankruptcy successfully takes place at court, executing state assets is another complex and difficult thing.⁴ Much of the trust in the airline from both investors and the public will also be greatly affected seeing that another Indonesian state-owned airline, Merpati Nusantara Airline, already stopped operating in 2014.

Additionally, GI’s bankruptcy will also impact the wider community. Aside from being a public company – in which 11.19%⁵ of its shares are owned by the public – GI is the only state-owned airline with the most widespread operational routes to date. It has a strategic value that needs to be preserved. The issue with this Indonesian flag carrier is not merely an operational one, but rather a financial one.

2. Restructuring GI

2.1. GI’s Financial Crisis and Survival Efforts

¹ Suparjo Ramalan, ‘Verifikasi Utang Garuda (GIAA) Rp198 Triliun Dijadwalkan 19 Januari 2022’ (IDX Channel, 13 January 2022) <<https://www.idxchannel.com/economics/verifikasi-utang-garuda-gjaa-rp198-triliun-dijadwalkan-19-januari-2022>> accessed on 10 April 2022.

² Monica Wareza, ‘Ini ‘Biang Kerok’ yang Bikin Utang Garuda Terus Menggunung!’ (CNBC Indonesia, 12 November 2021) <<https://www.cnbcindonesia.com/market/20211111184125-17-290879/ini-biang-kerok-yang-bikin-utang-garuda-terus-menggunung>> accessed on 10 April 2022.

³ Fitri Novia Heriani, ‘Ini Akibat Hukum Jika Perusahaan BUMN Pailit’, (Hukumonline, 28 October 2021) <<https://www.hukumonline.com/berita/a/ini-akibat-hukum-jika-perusahaan-bumn-pailit-lt617acbd738d73?page=all>> accessed on 25 May 2022.

⁴ Ibid.

⁵ Indonesia Stock Exchange Website, ‘PT Garuda Indonesia (Persero) Tbk Company Profile’ <<https://www.idx.co.id/en-us/listed-companies/company-profiles/company-profile-detail/?kodeEmiten=GIAA>> accessed on 10 April 2022.

The ratio of GI's debt to income and asset value is far from ideal, with a debt much larger than the assets. According to the Indonesian Law No. 37 of 2004 on Bankruptcy and Suspension of Debt Payment Obligations, as lastly amended by Law No. 40 of 2014 ("Law No. 37/2004"), the term 'over leverage' which means excessive debt risks is used to describe GI situation.⁶ While the Covid-19 pandemic has greatly affected GI's income, currently GI is still getting revenues from its operations, and their market share is relatively high compared to other Indonesian airlines. In this situation, GI's main problem is the payable fixed costs, which includes loan interest payments, loan installments payable to third parties, and other fixed costs that continue to increase from time to time.

Historically speaking, this situation is somewhat predictable ever since GI restated their financial statement for the fiscal year of 2018. Back then, in the materials published by GI in the Indonesian Stock Exchange (IDX) information disclosure, an adjustment to GI's records revealed that the airline suffered from a loss amounting to US\$ 175 million or equal to around IDR 2.45 trillion (exchange rate of Rp. 14,004/US\$). There was a US\$ 180 million discrepancy of loss with the financial statement that was previously conveyed for the same fiscal year. In 2018, the company reported a profit of US\$ 5 million or equivalent to IDR 70.02 billion.

In addition to the 2018 statement of income, the restatement also recorded a decrease of US\$ 204 million in the company's assets from US\$ 4.37 billion to US\$ 4.17 billion. The total liabilities decreased by US\$ 24 million from US\$ 3.68 billion to US\$ 3.44 billion. The total equity decreased by US\$ 180 million from US\$ 910 to US\$ 730 million. The net other income item was presented in the 2018 financial restatement with a figure of US\$ 38.9 million, from previously mentioned US\$ 278.8 million. There was a decrease in revenue of US\$ 239 million. The circumstances above shows that over leverage is something that has been slowly accumulating for quite a long time in GI. As the latest update per-November 2021, GI financial status was far worse with total liabilities of US\$ 9.75 billion and total equity of minus US\$ 2.8 billion with additional around US\$ 100-150 million monthly.⁷

Corporate action is needed to save the flag carrier. Speaking of the over leverage situation currently experienced by GI, there are three applicable rescue options. First, the government could provide bailout funds.⁸ Second, GI may settle a financial restructuring scheme

⁶ Indonesia, Law No. 37/2004 on Bankruptcy and Suspension of Debt Payment Obligations.

⁷ Ridwan Nanda Mulyana and Titis Nurdiana, 'Ekuitas Negatif US\$ 2.8 Miliar, Garuda Indonesia Siapkan Proposal Restrukturisasi' (KONTAN, 10 November 2021) <<https://insight.kontan.co.id/news/ekuitas-negatif-us-28-miliar-garuda-indonesia-siapkan-proposal-restrukturisasi>> accessed on 25 May 2022.

⁸ Titis Nurdiana, 'Menimbang untung rugi empat opsi penyelamatan Garuda (GIAA), mana pilihan terbaik?' (KONTAN, 30 Mei 2021) <<https://industri.kontan.co.id/news/menimbang-untung-rugi-empat-opsi-penyelamatan-garuda-giaa-mana-pilihan-terbaik?page=all>> accessed on 10 April 2022.

outside of the court; while the third option involves financial restructuring through a request for suspension of debt payment obligations (*Penundaan Kewajiban Pembayaran Utang* or “PKPU”) at the commercial court.⁹ PKPU lasts for maximum 315 days with aim to reach peace or settlement agreement with creditors to avoid bankruptcy.¹⁰ Each option will have its own pros and cons.

For the first option (i.e., the bailout funds), the Minister of State-Owned Enterprises must apply for a bailout through a legal proceeding as stipulated in the applicable regulations. The advantage of the bailout option is that the provision of bailout funds can be done relatively quickly compared to fundraising through other means. The proceeds from the bailout can also improve the flag carrier’s financial health through increase of equity which helps re-balance the debt-to-equity ratio.

Additionally, this bailout option will not negatively impact investors’ trust (including stock exchange investors in IDX – GI’s code: GIAA) in the flag carrier. This is because investors will see that the Indonesian Government, as GI’s majority shareholder, still provides financial support in the form of such bailout. Precisely, this bailout option will however affect the state finances as it will significantly dry out a portion of the state budget in the midst of a low economic growth due to the pandemic.

The next option is debt restructuring through an out-of-court agreement. GI can restructure the loan and adjust the loan maturity period along with interests and other obligations with a balloon payment model. This balloon payment clause is generally an ideal restructuring method particularly in case of over leverage currently experienced by GI.

The balloon payment model delays the maturity of debt, installments, and interest in the initial year (grace period) and set up payments in stages (small payments at the beginning, slowly increases as time goes) so that if operations are back to normal after the pandemic and the efficiency increases, the potential income will be even bigger. This option is ideally accompanied by a clause extending the period of obligations fulfillment to third parties. On the other hand, there will be no cash or equity received by GI; thus, the debt-to-equity ratio will not be impacted in the short term— at least not the way the bailout.

The third option is restructuring through a request for PKPU through the commercial court. On one hand, during the court process, GI does not need to pay installments and interest— known as a stand still situation, and the expected restructuring scheme will be achieved in accordance with GI’s proposal through a reconciliation process in a commercial court or homologation. Such process takes time as GI is still negotiating with its creditors as of May 2022.

⁹ Indonesia, Law No. 37/2004.

¹⁰ Indonesia, Law No. 37/2004, arts 222 and 228.

Furthermore, one of the main obstacles for GI in exercising stand still situation concept is the hell or high water clause applied globally in the aviation industry. The clause safeguards airline to pay its lease even though the aircraft is not flying – as for months during Covid-19 pandemic.¹¹ However, on the other hand, the third option still carries a risk of bankruptcy if the creditors refuse to accept the proposal submitted. Also, in the end, even if the settlement is achieved through commercial court, investors' confidence will be already affected and it might be harder for GI to carry out fundraising through corporate actions in the future.

Considering the various options above, the most proper option would be either bailout at the first place or out-of-court restructuring as the alternative. The existence of a bailout, even if such bailout only covers a part of the necessary portion, will restore the debt-to-equity ratio in a short time and will also restore the confidence of investors in GI's future given the willingness of Indonesian Government, as the majority shareholder, to provide equity to GI. This situation is preferable especially when the flag carrier needs to carry out fundraising through numerous corporate actions in the future.

A bailout to cover all of the necessary funding will however be a huge burden to the state finances. If the bailout only covers a part of the funding, then an out-of-court restructuring is still necessary to reduce the burden of fixed costs in the near future. It is reasonable to expect that this method may solve GI's over-leverage issue and allow GI to operate optimally in the next years in order to regain its market share.

2.2. Debt-to-Equity Swap Option

By virtue of the Regulation of the Financial Services Authority (*Peraturan Otoritas Jasa Keuangan* or "POJK") No. 36/POJK.03/2017 ("POJK 36/2017")¹² on the principle of prudence in equity participation, banks may opt to convert debt into equity. The POJK further provides that the nature of the banks' equity participation is temporary— since their main role is that of a financial institution, not an investor running a business.

The temporary nature of the banks refers to the fact that after the agreed period of equity participation ends, there are only two possible options, namely i) there are investors who are willing to buy GI's shares, or ii) there are none. Indonesian banks cannot legally participate as a permanent shareholder. If the debt-to-equity swap method is chosen to save the flag carrier,

¹¹ Ridha Aditya Nugraha and Anggia Rukmasari, 'Setting New Standards for Aircraft Lease Agreement' (The Jakarta Post, 14 December 2021) < <https://www.thejakartapost.com/opinion/2021/12/13/setting-new-standards-for-aircraft-lease-agreement.html> > accessed on 25 May 2022.

¹² Indonesia, Regulation of the Financial Services Authority No. 36/POJK.03/2017.

the regulation regarding the banks' exit clause must be clearly provided in terms of time, prices, and conditions.

The definition of 'prudence' under POJK 36/2017 implies that equity participation activities should not harm the banks or incur the potential to harm the banks, either in the short term or in the long term. According to the general explanation section of POJK 36/2017, it is also explained that equity participation activities by the banks are one part of the bank's fund investment activities in addition to other activities such as lending or financing, investing funds in the form of securities, and interbank money market activities. As an act of investment, in addition to receiving benefits in the form of income from equity participation, the banks remain exposed to the risks arising from these activities.

From a financial standpoint, the debt-to-equity swap option is very profitable. Assuming that all of the bank creditors exercise the option of equity participation, the GI's financial burden will be much lighter, and there will be no need for a bailout which will take up a significant portion of the state budget. The difference between the legal consequences of a bailout and debt-to-equity swap is that in a bailout scenario, the Indonesian government fully bears the financial risks arising from a failed financing, while in an equity participation scenario, the risks are borne by the banks.

As the creditors, the banks bear the full risk not only in the legal relationship between the creditor and the debtor, but by choosing the option of equity participation, the bank will have the position as an investor with the ownership portion equal to the value of the converted debt. The civil legal construction for this equity participation is the conversion of debt into ownership, known as convertible loan. This means that the value of the loan is considered as the payment price for a number of shares which will become the portion of the banks' ownership as the creditors.

In this case, the bank shall carry out a thorough due diligence to highlight the inherent potentials, risks, and liabilities in GI. With the due diligence, the banks are able to determine the right valuation and conversion value. Additionally, another point that needs to be taken into account is that if all creditors (banks) choose the conversion option, the Indonesian government's ownership in the flag carrier will shrink drastically giving rise to a revocation of the GI's status as a state-owned enterprise as the state is no longer the controlling shareholder. This possibility occurs under the assumption that all the bank creditors of GI exercise the option of equity participation.

In the restructuring process that is currently being carried out, it is necessary to consider the direction the government wants to take in regard to the ownership of GI. If the government still considers the airline as a strategic state-owned enterprise and wants to manage

GI as such, it is better to limit the equity participation option and prioritize the short-term debt that has been or will soon be due. On the other hand, if the Indonesian government thinks that the flag carrier is too difficult to save, then this momentum could be used to reduce the government's shares in GI.

Under current conditions, it is advisable to limit the equity participation option in GI only to short-term debts that have been or will soon be due given the prospective business opportunities and GI's expected operational plan in the next few years. The Indonesian government will remain the GI's controlling shareholder for a few more years. The financing restructuring agreement and the option to invest in the airline must be accompanied by a put and call agreement as an option to buy back or increase the ownership.

A put and call agreement is considered a middle ground in situations of uncertainty. Put and call option indicates that the ownership to be released to investors can be increased or decreased, meaning the government does not have to lose ownership in large amounts at once and has the time to determine the strategic steps for GI instead. Undoubtedly, in this case, put and call is limited in terms of time and price for each option, considering that if the government buys back ownership from the banks, it is necessary to formulate a different price from which the banks or investors buy ownership from the government.

If the equity participation option is chosen, a put and call agreement must also be entered into in order to maintain the government's position as the controlling shareholder. If the GI's situation improves and bounces back into a profitable state-owned enterprise in a few years, the government can still buy its shares back. Conversely, the government also has the option to sell their shares should the airline's situation turns out to be unfavorable.

The banks as the creditors need to consider the size of the option for equity participation and the exit clause for the bank with the two possibilities that i) there are investors who are willing to buy GI's shares or ii) there is none. The banks need to ensure that this equity participation option is not a way for the flag carrier to postpone the payment of non-performing loans, which will of course impact the banks' liquidity and the provision of additional bailout funds due to non-performing loans to maintain capital adequacy ratio.

2.3. Debt Restructuring

It is necessary to understand that the restructuring carried out by GI is actually a strategic effort, both in terms of resolving the flag carrier financial problems and in relation to the operational efficiency of the airline. Objectively speaking, it is also possible to solve the airline's financial problems through restructuring efforts.

GI does not have a fundamental problem other than the issue of over leverage— that is, the amount of debt way above the asset value. Restructuring is the most effective effort in solving such over-leverage problem. In addition, GI is still operating their business as ‘normal’ – even though less aircraft less flights, in the sense that all existing source of funds can still generate revenue to GI. When it comes to components of earnings before interest and tax, depreciation, and amortization (“EBITDA”), GI's situation is still feasible for debt restructuring.

One of the impacts of debt restructuring is the adjustment of the company's operations. In GI's case, such adjustment comes in the form of management strategy which eliminates certain routes or schedules that are considered ineffective and not profitable. Other adjustment, for example, is the fact that the flag carrier operations are heavily relying on efficiency based on Pareto law: focusing on efforts which can be carried out immediately and also produce immediate results. Ultimately, these strategies are intended to lessen the burden on the airline's financial situation.

There are two ways of restructuring, namely i) restructuring carried out by debtors and creditors directly without going through a court proceeding which refers to out of court settlement; and ii) restructuring as referred to in Law No. 37/2004 on Bankruptcy and Suspension of Debt Payment Obligations which points financial restructuring through a request for suspension of debt payment obligations (*Penundaan Kewajiban Pembayaran Utang* or “PKPU”) at the commercial court.¹³ Essentially, both types of restructuring – whether it is out of court or otherwise – are equally beneficial since the purpose of restructuring is to provide relaxation to the airline financial situation.

The terms bankruptcy and suspension of debt payment obligations in Law No. 37/2004 mentions that restructuring through suspension of debt repayment obligations, even though it is carried out through the courts, has a different meaning and purpose from bankruptcy. An important element in debt restructuring through the commercial court is shown in the Law No. 37/2004,¹⁴ which mentions that “... *proposing a reconciliation plan which includes an offer to pay a part or all of the debt to creditors...*” is the debtor's ability to seek settlement of debt payments to creditors. GI's financial situation supports both types of debt restructuring efforts.

There are five important factors in a restructuring agreement.

First, a considerably long grace period is required from each creditor (especially the major creditors) so the debtor's financial burdens are significantly lessened in the initial period of restructuring.

¹³ Indonesia, Law No. 37/2004.

¹⁴ Indonesia, Law No. 37/2004, Art. 222, par. (2) and (3).

Second, the repayment clause for major creditors shall include a deferred clause with a balloon payment model, because such payment model will not put a heavy burden on GI's finances. This is mostly because the balloon payment model allows a small amount of payment in the beginning even though such amount will later increase from year to year in line with the improvement of the debtor's financial condition. In connection with this, it is necessary to evaluate the costs and interests of the borrowed funds, known as the cost of fund.

Third, the restructuring agreement that will be agreed later in the homologation agreement in accordance with Article 281 of the Law No. 37/2004¹⁵ must be prepared in two phases of payment model. The initial period shall use a countercyclical model approach, in which payments are made in the minimum possible amount. After the debtor's financial conditions recover and operations are back to normal, the second phase, namely the procyclical model, shall begin marked by better financial projections and realization which in turn increase the debtor's ability to repay the loan.

Fourth, in restructuring efforts carried out outside of the court and through the commercial court, the countercyclical and procyclical phases should be similar. Therefore, it is easier for GI to submit a homologation proposal in the commercial court, and it is highly likely that during the voting process, in accordance with the mechanism of Law No. 37/2004,¹⁶ the debt restructuring strategy will be beneficial for both flag carrier and its creditors.

Finally, it is necessary to carry out loan management in relation to debt restructuring through the commercial court. GI needs to carry out loan management by deciding which loans must be paid before the voting process, and which ones will be included in the reconciliation proposal. This is a technical effort to ensure a smoother voting process because according to Article 281 Law No. 37/2004 in conjunction with Government Regulation No. 10/2005 on Calculation of Creditor's Voting Rights¹⁷, the voting right of each creditor depends not only on the amount of loan, but also on the amount of total creditors.

3. Conclusion and the Way Forward

Given GI's reputation as the best airline in Indonesia with prominent market shares in particular on domestic flights¹⁸, restructuring is the best solution for its current situation because such step does not burden the state finances like bailout does. Restructuring, whether carried

¹⁵ Indonesia, Law No. 37/2004, Art. 281.

¹⁶ Ibid.

¹⁷ Indonesia, Government Regulation No. 10 of 2005 on Calculation of Creditor's Voting Rights.

¹⁸ Ridha Aditya Nugraha, 'Reviewing Ownership and Control of the Indonesian Airlines' (2019) ASEAN Aviation Integration Platform, IKMAS Universiti Kebangsaan Malaysia.

out outside of the court or through a homologation process in the commercial court, shall preserve and maintain GI as the flag carrier with potential developments in the future.

The restructuring process is still on-going until May 2022. The result shall determine whether the Indonesian government will do everything to save its flag carrier even though it is less commercially viable – whereas such scenario shall boost investors trust in Indonesian state-owned airlines; or a new state of play shall occur whereas restructuring has its limits in case the conservative perspective towards the flag carrier has gradually changed.