


**EU-Indonesia Vision Group**  
**First Meeting – Jakarta 2<sup>nd</sup> December 2010**  
**Hotel Borobudur**  
**AGENDA**

1.	9.00 – 9.30	Opening and presentation of the objectives of the group, expected timeframe and working method. <i>(Co-Chairs of the Vision Group)</i>
2.	9.30 – 12.00	State of play of EU-Indonesia trade and investment relations:
	9.30 – 10.15	Presentation of three studies <i>(Project Group)</i>
2.1		Trade and investment between EU and Indonesia: Opportunities and Obstacles
2.2		Indonesia market access to the European Union: Opportunities and challenges
2.3		Trade Sustainability Impact Assessment of the FTA between the EU and ASEAN with summary of the main issues related to Indonesia
3.	10.15 – 12.00	Tour de table/brainstorming (Co-Chairs moderate the discussions also on the basis on the material received from the Project Group)
4.	12.00 – 13.00	The view of the business sector: <i>presentations by KADIN and EuroCham</i> on the basis of the outcome of the second meeting of the EIBD
	13.00 – 14.00	<i>Lunch</i>
5.	14.00 – 14.45	Presentation on different models of bilateral agreements and the approaches to measure the economic benefits (4.1(b)  ).
6.	14.45 – 15.15	What we have already in place: Short overview of the Agreements of Indonesia and the EU with third parties <i>(Project Group)</i>
7.	15.15 – 16.00	Discussion
8.	16.00 – 16.20	The Partnership and Cooperation Agreement between EU and Indonesia: main content and timeframe for implementation including comparison with the Indonesia-Japan EPA <i>(European Commission)</i>
9.	16.20 – 16.40	Overview by EU on bilateral and regional economic cooperation activities and by Indonesia on currently foreseen needs <i>(EU Delegation &amp; Ministry of Trade)</i>
10.	16.40 – 17.30	Second tour de table/brainstorming
11.	17.30 – 18.00	Discussion on further analytical work to be completed
12.	18.00 – 18.30	Conclusions and agreement on date and agenda of next meeting
	19.00 - 21.00	<i>Dinner</i>

## 1. SYNOPSIS OF DOCUMENTATION

The purpose of this short paper is to highlight some issues extracted from the available literature in order to facilitate the reading of the relevant parts of the material provided. The review of the existing literature does not provide a clear cut picture of the EU-Indonesia trade relations. As highlighted in the **2009 IBM study**, there are several factors (demographic dividend, sectoral reforms, ASEAN regional integration and the appartenance to a highly dynamic region) that have positive influences on Indonesia's economic development. Therefore, there is considerable potential to build on the substantial trade and investment relationships between the EU and Indonesia. However, the level of EU trade and investment in Indonesia is proportionately lower than in other ASEAN countries (such as Singapore, Malaysia and Thailand), reflecting the less competitive background for FDI in Indonesia as compared to more dynamic ASEAN economies.

A similar complex picture arises from the more recent study made in 2010 by **TRANSTEC**, which background was that the EU share of Indonesian export markets has fallen from 14% at the start of the decade to around 10% now. This is partially due to that Indonesia's exports to EU and other developed markets have been redirected to the ASEAN regional market. This shift has increasingly allowed other ASEAN countries to use Indonesia's natural resources in their unprocessed forms to move up their value chains and produce greater quantities of processed and high-tech products. As a result, the fast-growing East Asian economies have been able to concentrate a growing proportion of their exports in manufactures and high value-added products, while Indonesia has remained entrenched in the production of raw materials and products having relatively small value-adding activities. One way for Indonesia to reverse this pattern is focusing its production on processing and other activities that add value to products. It has a relatively high degree of trade compatibility with EU imports and there are a large number of products in which Indonesia has already succeeded in increasing its market share in expanding market in the EU, i.e. electronic components, processed and prepared foods, and chemicals, while it has not taken advantage of the fast growth in the EU markets of products such as cosmetics, TV components, furniture, sea products, footwear. Indonesia could achieve enormous export revenue gains it were to overcome **Export Quality Infrastructure** and supply-related constraints to placing products on the EU market would be necessary.

However, the process of opening up the economy and climbing the added-value chain presents several constraints and could potentially have an initial negative impact on the industries more exposed to competition. This issue is addressed in the **Trade Sustainable Impact Assessment** studies that are usually prepared ahead of any major trade negotiation. The TSIA of FTA between the EU and ASEAN (Ecorys, 2009) puts emphasis on the "flanking measures" to be introduced, addressing prospects and problems of winners and losers.

The issue of the existing asymmetry in the economic relations between the two sides, and the need to address short-term adjustment costs to be incurred by Indonesia in possible FTA negotiations is discussed in an **IISD paper**, concluding that a number of factors would need to be incorporated in a possible future EU-Indonesia FTA. These include taking into account and striking a balance between Indonesia's interpretation of the ways in which a potential FTA should contribute to the development of Indonesia and EU's own interpretation of economic development. Some of the main concerns from an Indonesian perspective arising from both future negotiations and implementation of a bilateral FTA are highlighted. These range from the exclusion of sensitive products from liberalisation, GSP reform, IPR protection, technical

assistance and all the issues related to the possible diverging views on how to achieve economic development for Indonesia.

The different trade policy options available for Indonesia are analysed in the **UNCTAD paper**. The conclusion of this study is that, in the long run, developing countries have little choice but to continue liberalisation as the world becomes increasingly integrated. While a competitive exchange rate, fiscal discipline, trade liberalisation, a sound investment climate and secured property rights are considered necessary, they are no longer sufficient. Other variables play an important role and include good governance, low levels of corruption, flexible labour markets, inflation targeting and strengthened social safety nets. Indonesia's options on trade policy range from increasing protection to actively pursuing bilateral, regional and multilateral initiatives. Indonesia has still room to move on in its trade policy, but important questions arise about how to proceed, such as more liberalisation or not and wider or deeper. Much needs to be done for Indonesia to become internationally competitive and to be in a position to maximise the benefits from further trade liberalisation. The paper concludes that a gradual rather than a "big bang" approach to further liberalisation may be the most successful. Adjustment costs, especially in terms of unemployment, are likely to be reduced if reforms are phased in.

The views of the Indonesian Government are highlighted in the **Country Note on Trade and Investment Policy Coordination, presented by MFA at a UNCTAD Seminar in 2009**. The paper emphasises areas of intervention, where the Government has worked to improve the business climate and encouraging competition. From the trade policy perspective, tariffs are in the process of being lowered and made more uniform in line with the ASEAN Tariff Harmonisation Program. As a consequence of these changes and the deeper integration in the region and the world, the overall import weighted applied MFN rate has come down to 8.3% in 2006. Moreover, the Government of Indonesia follows a triple track strategy on the international trade negotiations: multilateral under WTO auspices, regional (centred on ASEAN and ASEAN+3 agreements) and bilateral FTAs/PTAs/EPAs. In terms of **investment policy**, the Government of Indonesia has succeeded to finalise the new Investment Law and Investment Negative List, as well as to introduce new policy reform packages. This rather positive assessment is also echoed in the most recent WTO Trade Policy Review of Indonesia, although it must be noticed that this report has been produced well before the financial crisis of 2008-2009 that saw the introduction of a number of non tariff barriers in Indonesia.

According to the **WTO**, in 2007 the Government of Indonesia progressed on trade policy. Tariffs were in the process of being lowered and made more uniform in line with the ASEAN Tariff Harmonisation Program. Non-tariff measures continue to be reduced or eliminated. Agriculture has started to benefit from a revitalisation programme which provides support for infrastructure, financial services, research and development and institutional reform. In international trade relations, Indonesia is an active participant in the current WTO negotiations. Indonesia's main concerns are to obtain improved access for its key agricultural and manufactured exports, while ensuring obtaining guarantees for its most sensitive sectors objectives and some flexibility to develop its industrial sector. The **OECD** regularly produces complete Economic Assessment of non-member economies with which OECD has an enhanced engagement. The one presented in the synopsis is not the most recent one (published early November was not available at the time of the research work) but contains a complete analysis of the economic developments over the last decade. It highlights a number of policy questions on elimination of price subsidies, the improvement of the business environment, investment, labour and social protection, that are all still very relevant for the future economic development of Indonesia.

The **Globalisation Index 2009** shows the extent to which the world's largest countries by GDP are connecting to the global economy. The Index uses 20 separate indicators that capture the key aspects of cross-border integration of business, namely openness to trade, capital movements, labour movements, exchange of technology and ideas, cultural integration. Indonesia is listed 56th out of the 60 largest countries, fallen 13 places since 1995. Movement of goods and services has declined steadily since its peak of 1998. A similar downward trend has impacted the movement of capital and finance, despite a largely positive government policy toward foreign investment, reasonable investment protection and a general lack of domestic favouritism. However, it is the exchange of technology and ideas that had the greatest impact on Indonesia's overall globalisation score. Although total trade as a percentage of GDP is low, the Government does have policies in place to encourage a more open trading environment. The overall level of globalisation is forecast to remain relatively stable until 2013, in the face of steady but limited increases in the movement of labour and the exchange of technology and ideas.

The World Economic Forum "**Global Competitiveness Index (GCI)**" 2010-11 ranks Indonesia 44th out of 133 countries, up 10 notches since the previous year. The GCI classifies Indonesian economy as an economy in transition between being a factor-driven economy and becoming an efficiency-driven economy. The primary reason behind the improvement in the ranking is the sound macroeconomic environment and improved education outcomes. Indonesia also ranks higher in more complex factors such as business sophistication and innovation. However, Indonesia scores low and has decreased its competitiveness related to government institutions, infrastructure (82 of 139 economies), technological readiness (91) and labour market efficiency. The **WB-IFC Doing Business Report 2011**, which presents quantitative indicators on business regulations and the protection of property rights, ranks Indonesia 121<sup>st</sup> out of 183 economies, a drop from last year's ranking 115. In the year under investigation, Indonesia eased registration procedures for new companies and improved in trading across borders but lost competitiveness in the categories paying taxes, enforcing contracts and protecting investors. Indonesia is in the lowest quartile globally in ease of paying taxes and enforcing contracts. The document **FDI and Growth in East Asia: Lessons for Indonesia 2010** emphasises the importance of FDI in East Asia's economic development. MNCs have come to account for about 10% of world output and 30% of world exports, and a large share of new technologies is developed and controlled by these MNC. Indonesia has not fully participated in this development, especially in manufacturing, and attracts less FDI than could be expected from its size and growth, due to a relative restrictive FDI regime and failure to continue with liberalisations. A relatively poor business environment with inefficient institutions seems to be an important explanation behind the low inflows of FDI.

Finally, the study "**Foreign Ownership and Employment Growth in Indonesia Manufacturing**" (2010) examined employment growth in Indonesia, which is relatively high in foreign-owned establishments. The study found a strong effect of shifts from domestic to foreign ownership in raising the growth rate of employment, but no significant effects of shifts from foreign to domestic ownership. If foreign ownership provides superior technology or better access to world markets, establishments should tend to raise their employment after foreign takeover. Even foreign firms that start producing only for the Indonesian market are more able to switch to export than are local firms. Foreign-owned establishments in Indonesia pay higher wages than domestically owned establishments, even given the educational level of their labour forces. They also pay a higher premium for the higher level of education. FDI determinants include good institutions, a skilled workforce, and openness to trade. Some of these are factors where Indonesia has shown improvements in recent years.

## **BRIEF FOLLOWING THE AGENDA**

This report provides the main preparatory documentation for the first meeting of the Vision Group to be held in Jakarta on 2nd December 2010, in order reflecting the agenda. It provides some bullets on top of each section that could be used to start discussions.

### **2. STATE OF PLAY OF EU-INDONESIA TRADE & INVESTMENT RELATIONS**

- **EU second export destination for Indonesia, providing trade surplus of EUR 6 billion**
- **Trade EU-IDN is picking up in 2010 after 2009 crisis year**
- **EU substantial investor in Indonesia, but could be much more.**

EU-Indonesia total trade grew over 25% between 2005 and 2009. Over the same period, the EU trade balance with Indonesia has recorded a deficit of EUR 6 billion on average. The EU is Indonesia's **fourth largest trading partner**, representing more than 10% of its total external trade with a value of almost EUR 17 billion in 2009. EU is following Singapore, Japan and China and ahead of the US. The **EU is Indonesia's second main export partner**, after Japan, accounting for over 13% of total exports, **and its fourth import partner**.

For the **EU**, Indonesia was the 30<sup>th</sup> largest trading partner in 2009. Indonesia supplies 0.7% of the EU's total merchandise imports, which mainly revolve around miscellaneous manufactured articles (23%), machinery and transport equipment (14%) and crude inedible materials (14%). Indonesian exporters of machinery parts have done well, with the EU market expanding at 10-15% per year, while Indonesian exports have increased at 25 to 50% per year during the last ten years. Processed foods, chemicals, textiles, machinery and electronic equipment are all high-growth sectors where Indonesian exporters are increasing their EU market penetration. In general, unprocessed products have less dynamic markets which mean Indonesian exporters will make more money and penetrate EU markets more if they can go up the value chain and process more. From unprocessed to processed vegetables, from unprocessed metals, minerals and lumber to finished metal products and furniture.

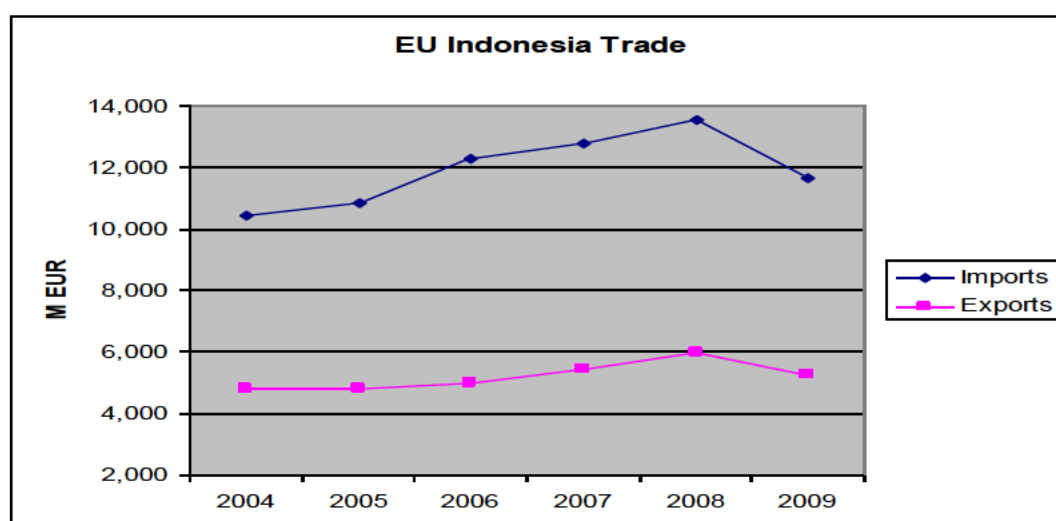
Although Indonesian exports into the EU in the whole of 2009 remained well below 2008 levels, the EU market has nevertheless been quite resilient compared to Asian markets, where exports are significantly below their 2008 level (between 20-40%). Initial figures for 2010 (up until Q3) show that total trade is up by over 15% compared to Q1-Q3 2009, representing 2008 levels (when total trade was EUR 20 billion)

Indonesia, exported EUR 83 billion in goods to the world in 2009 of which 44% in manufactures and 56% in foods /drinks & tobacco (6.6%), raw materials (20.8%) and mineral fuels /lubricants (28.3%). It is therefore a typical resource-driven exporter, with increasing but still not dominating manufacturing exports, only weakly reflecting the typical East Asian export-led growth model so far. Not surprisingly, manufactured imports in 2009 assumed no less than 67% of all imports. Indonesia ran a sizeable surplus with the world of EUR 14 billion, EUR 6.3 bn of which with the EU. In bilateral trade, Indonesia has kept a constant share of EU exports of goods but had difficulties maintaining its share in EU imports given the dynamism of other countries competing for EU demand such as China, Russia and, to a lesser extent, India, Turkey and Brazil.

### European Union, Imports from... Indonesia

SITC Codes	SITC Sections	Value (Millions of euro)	Share of Total (%)	Share of total EU Imports
<b>TOTAL</b>		<b>11,643</b>	<b>100.0%</b>	<b>1.0%</b>
SITC 8	Miscellaneous manufactured articles	2,883	24.8%	1.6%
SITC 4	Animal and vegetable oils, fats and waxes	1,892	16.2%	34.7%
SITC 7	Machinery and transport equipment	1,753	15.1%	0.5%
SITC 6	Manufactured goods classified chiefly by material	1,268	10.9%	1.1%
SITC 2	Crude materials, inedible, except fuels	1,219	10.5%	3.0%
SITC 3	Mineral fuels, lubricants and related materials	996	8.6%	0.3%
SITC 0	Food and live animals	888	7.6%	1.3%
SITC 5	Chemicals and related prod, n.e.s.	378	3.2%	0.4%
SITC 1	Beverages and tobacco	27	0.2%	0.6%
SITC 9	Commodities and transactions n.c.e.	22	0.2%	0.1%

When it comes to services, Indonesian exports roughly half of what it imports in 2009; the latter amounts to EUR 19 billion, some 27 % of goods imports. In services exports to the world, travel dominates (48 %), with transportation second and 'other business services' third (14.3%). Other sectoral services flows are very small. On the import side, transportation assumes no less than 49.3 %, with travel another 19 % and 'other business services' 13.7%; again, other sectoral service imports are minimal.



Indonesia and EU trade flows are largely complementary, i.e. do not overlap in terms of product groups broken down in detail. The EU is an important trading partner, but the level of EU trade and investment in Indonesia has been proportionally less than EU trade with other ASEAN countries relative to the size of the economy. This is primarily due to the relatively smaller role of FDI in the Indonesian economy. EU exports to Indonesia are particularly strong in transport equipment (cars, trucks and airplanes), chemicals, high-tech manufactured goods and processed food. Table below provides shares of total 2000 and 2008 exports for the six leading export sectors of the two trading partners which confirm this pattern.

<b>EU sectoral exports</b>	<b>2000</b>	<b>2008</b>	<b>Indonesian sectoral exports</b>	<b>2000</b>	<b>2008</b>
telecoms equipment	6	10	clothing & accessories	16	9
specialized (sect.) machineries	12	9	vegetable oils	6	13
machinery (gen.) & equipment	7	8	telecoms equipment	5	6
electrical machinery	5	7	footwear	6	5
organic chemicals	5	6	crude (natural) rubber	2	5
(other) transport equipment	6	6	electrical machinery	4	4

Source: IBM et al, 2009, Trade & Investment between EU and Indonesia, Part 1, pp. 28/9 (adapted)

### **Investments**

With regard to investments, there is a lot that Indonesia and the EU have to offer each other, especially in value-adding sectors such as infrastructure, chemicals, food, metal, manufacturing and services sectors (notably banking, express delivery and logistics and construction). EU foreign investments are centred on sustainable development and fair employment conditions and on high-quality products, services and technological solutions. The inflows from EU to Indonesia have increased over the last four years, from US\$ 800 million to US\$ 2 billion, according to BKPM data. Although Indonesia is home to 45 % of the ASEAN population, it barely receives 10 % of FDI destined for ASEAN. European companies have invested mainly in other ASEAN countries. Apparently, the investment climate and relatively sluggish growth (in such a dynamic region) reduce the (relative) attractiveness to invest in Indonesia. Most of EU FDI is of the (local) market-seeking type, with resource-seeking ones as a second. In particular, efficiency-seeking FDI would be a sign that Indonesia is becoming regionally competitive; it might also raise the Indonesian share of FDI going to ASEAN.

#### **Share of FDI realisation by country of origin (BKPM)**

<b>Country</b>	<b>2005</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>2009</b>
Japan	13%	15%	6%	9%	6%
<b>EU</b>	<b>9%</b>	<b>31%</b>	<b>10%</b>	<b>13%</b>	<b>18%</b>
South Korea	5%	8%	6%	2%	6%
Singapore	24%	8%	36%	10%	40%



**The EU is an important source of direct investments for Indonesia.** EU's total investment stock in Indonesia is estimated to amount to EUR 50 billion, with over 700 EU companies present employing over 500,000 persons. Still, potential for much larger investment flows is hindered by the challenging investment climate and regulatory aspects. Although investments have decreased since the 1997/98 crisis, the leading position of EU investors in Indonesia has been maintained where EU is one of the main sources of Indonesia's foreign investment. The United Kingdom, the Netherlands, Germany, and France are among the biggest sources of investment. EU investors are prevalent in trade and repair services, hotel and tourism, transport and communication, construction services, financial services and the food industry.

**European Union, Exports to... Indonesia**

<b>SITC Codes</b>	<b>SITC Sections</b>	<b>Value (millions of euro)</b>	<b>Share of Total (%)</b>	<b>Share of total EU Exports</b>
<b>TOTAL</b>		<b>5,257</b>	<b>100.0 %</b>	<b>0.5%</b>
SITC 7	Machinery and transport equipment	2,616	<b>49.8%</b>	<b>0.6%</b>
SITC 5	Chemicals and related prod, n.e.s.	805	<b>15.3%</b>	<b>0.4%</b>
SITC 6	Manufactured goods classified chiefly by material	642	<b>12.2%</b>	<b>0.5%</b>
SITC 2	Crude materials, inedible, except fuels	328	<b>6.2%</b>	<b>1.3%</b>
SITC 8	Miscellaneous manufactured articles	265	<b>5.0%</b>	<b>0.2%</b>
SITC 0	Food and live animals	255	<b>4.9%</b>	<b>0.6%</b>
SITC 9	Commodities and transactions n.c.e.	61	<b>1.2%</b>	<b>0.2%</b>
SITC 1	Beverages and tobacco	18	<b>0.3%</b>	<b>0.1%</b>
SITC 3	Mineral fuels, lubricants and related materials	12	<b>0.2%</b>	<b>0.0%</b>
SITC 4	Animal and vegetable oils, fats and waxes	6	<b>0.1%</b>	<b>0.2%</b>



## **2.1. Trade and investment between EU and Indonesia: Opportunities and Obstacles (Document 1, IBM, July 2009)**

- **Indonesia and EU economies complementary**
- **Indonesia high in potential, low in realisation**
- **Indonesia's reform agenda positive for attracting trade and investment**
- **Indonesia as a gateway to ASEAN**

This study examines the reasons behind the relatively low level of EU trade and investment towards Indonesia, identifying drivers and constraints to expanded trade and investment. The study also looks at the potential and opportunities offered by the Indonesian market, not only from the perspective of EU export interests, but also how EU goods, services, technology and investment could contribute to Indonesia's economic development and enhance the competitiveness of its industry. Indonesia has good economic prospects and substantial development potential. The Indonesian economy is exhibiting some resilience in the global downturn and has good medium-term growth potential. Several factors (demographic dividend, sectoral reforms, ASEAN regional integration and the appartenance to a dynamic region) have positive influences on Indonesia's economic development potential.

The conclusion of the study is that there is considerable potential to build on the substantial trade and investment relationship between the EU and Indonesia. This relationship is highly complementary with EU enterprises focusing on trade and investment in areas where they have technological or design capacities which provided a source of comparative advantage for Indonesia industry and exports. However, the potential is under-exploited, largely due to the obstacles and constraints identified in the analysis. The Report contrasts the potential of Indonesia as Southeast Asia's largest economy, with the fourth largest population in the world with the current regional reality that the EU trades more with and invests more in neighbouring countries. It furthermore looks at the future balance between reform and economic nationalism. It draws some positive conclusions, based on three positive factors driving Indonesia's economic development potential:

1. Indonesia will experience a demographic dividend thanks to falling birth rates and declining dependency rates resulting in a young and active labour force, strengthened by the increasing participation of women, in contrast to almost reverse demographic patterns in Europe where the population is ageing.
2. Indonesia is on the path to reform including infrastructure improvements, and business and investment climate, with efforts to improve performance of SMEs and education (included as a major component in the new EU Economic Partnership Agreement). The country also continues to tackle corruption.
3. Initiatives taken by Indonesia with ASEAN partners to deepen ASEAN integration, integrate regional production networks and supply chains and pull regional economies together through trade measures are already firmly launched.

The report further notes that EU-Indonesian trade and economic relationship is highly complementary with EU firms focusing on trade and investment where they have technological or design capacities, thereby potentially providing higher comparative

advantage for Indonesian firms and exports. Indonesia's attractiveness to FDI would draw in technology, enhance skills development and expand capital formation that could create employment opportunities for a young and expanding labour force. The report focuses around a Computable General Equilibrium Model (CGE), concluding that the level of EU trade and investment was proportionately less than for other ASEAN countries reflecting the more modest role for FDI in Indonesia compared to more dynamic ASEAN economies.

Indonesia supports trade liberalisation and regional integration whilst backing some trade restrictions and non-tariff barriers. Poor infrastructure and a middling business climate have held back the rate of development in trade and investment. Therefore, there is a need for greater trade facilitation and for further efforts to improve customs administration on the basis steps already taken including computerisation and progress towards the ASEAN single window. Indonesia has made progress in eliminating import licenses on 1,192 tariff lines since the 1990's but a spate of more than 140 new licences since 2008 along with a few import restrictions, primarily in the agricultural sector.

EU exports should have a growing comparative advantage in areas including power generation equipment, non-electrical machinery, consumer goods, pharmaceutical products and telecommunications equipment and services. EU industry would look to further progress in exports of telecommunications equipment, the manufacturing sector, for example in textile machinery, food packaging, the power machinery and infrastructure sectors and in road infrastructure and the automobile sector where EU firms are well placed to compete with ASEAN and Asian firms in a rapidly expanding and attractive market.

The report concludes that CGE analysis estimated potential gains from an FTA for Indonesia would be more than 2% of Indonesian GDP, with dynamic effects, such as the positive impacts of higher FDI drawing in technology, enhancing skills and expanding capital formation to possibly increase overall gains up to 4% of GDP. The division of labour between Indonesia and the EU is currently more vertical but the best prospects for increased EU trade and investment would be to move towards trade in industrial products rather than a big emphasis on unprocessed commodities. .

## **2.2. Indonesia market Access to the EU: Opportunities & Challenges (Document 2, TRANSTEC, July 2010)**

- **Large EU single market with diverse opportunities in terms of tastes, businesses.**
- **But IDN exports to the EU as a percentage of total exports dropped significantly (from 18% to 14%)**
- **IDN could focus on processing activities and activities that add value to products, in the areas of fisheries; agri-foods; consumer electronics; furniture; and cosmetics.**
- **And could consider capitalizing on competitive advantages and strengthening capacity to ensure quality standards. Overcoming supply constraints could lead to 28% higher export revenues in above sectors alone.**

The main objective of the report is to identify sectors and industries where Indonesia is currently competitive and where it has good potential to perform well in the EU market.

### ***1. The EU as an Important Market***

There are extensive market opportunities for countries like Indonesia in the European Union. As a single entity, the European Union is the world's largest economic power, accounting for nearly 30 percent of total world output and outranking the total gross domestic product (GDP) of the United States, and of Japan and China combined. With the value of total trade equal to more than 40 percent of GDP, the European Union's openness to trade is more than three times greater than that of either the United States or Japan. The total value of its imports last year was US\$1.7 trillion, representing over 18% of total world trade. From Indonesia's perspective, there are two important differences among the 27 member countries of the European Union. The first is the large variations in the size of member countries in terms of their domestic markets; the second is the considerable variation that occurs in consumer purchasing power across the countries. Under these conditions, Indonesian exporters have a wide range of market opportunities when looking for markets of different sizes and with consumer preferences for either high-end products or products that have more appeal to mass markets. The European Union is also home for almost half of the world's largest transnational corporations. These companies depend on linkages with foreign-based producers in sectors that are of particular interest to Indonesia, for example, in chemicals, electrical equipment, food and beverage, motor vehicles, and pharmaceuticals. By integrating their supplies into global value chains of these transnationals, local Indonesian producers are increasingly becoming part of networks of cooperating firms that are involved in the full cycle of activities that add value to the products that they supply to consumers.

### ***2. Indonesia's Trade Flows with the European Union and Other Important Markets***

The share of Indonesia's exports destined for that market has declined substantially, from 18% to 14% over the last decade. This contraction parallels similar reductions in the share of Indonesia's exports directed at the United States and Japan. As a whole, the absorption of Indonesia's exports by these three markets has fallen from 55% in 2000 to 40% in 2009.

Most of the decline in Indonesia's exports to these developed markets has been redirected to the ASEAN regional market. This shift has increasingly allowed other ASEAN countries to use Indonesia's natural resources in their unprocessed forms to move up their value chains and produce greater quantities of processed and high-tech products. As a result, the fast-growing East Asian economies have been able to concentrate a growing proportion of their exports in manufactures and high value-added products, while Indonesia has remained entrenched in the production of raw materials and products having relatively small value-adding activities. Indonesia could reverse this pattern by focusing its production activities on processing activities and other activities that add value to products. It has a relatively high degree of trade compatibility with EU imports. There are also a large number of products in which Indonesia has already succeeded in increasing its market shares in rapidly expanding markets in the European Union. Examples include electronic components, processed and prepared foods, and chemicals. In other products, however, Indonesia has not yet taken advantage of the fast growing EU markets for products like soaps and cosmetics, television parts, furniture, crustaceans, footwear and jewellery. In order to provide lessons and guidelines for developing high-value added exports with dynamic growth markets in the European Union, the present study focuses on five industries or sub-sectors of importance to Indonesia, which are prioritised according to criteria: (i) factors related to national development objective; (ii) factors related to foreign market determinants; and (iii) factors related to international competitiveness and internal factors.

### ***3. Focal Industries have a Huge Potential in the EU Market***

Demand for imports of the focal products is projected to grow by nearly 7% a year over the medium term. This forecast is based on econometric models that generated market estimates based on key assumptions about GDP growth, relative price changes for each of the traded products, and the euro-dollar exchange rate. EU market outlook highlights are as follows:

- *Fisheries:* The European Union is, by far, the world's largest importer of fishery products, and its strong demand for fishery imports largely reflects its high responsiveness to changes in consumer incomes. European fishery imports are projected to grow by a robust annual average of 8%.
- *Agri-foods:* The EU demand for agri-food imports has been strong, particularly in its response to changes in consumer incomes. Demand for agri-food imports is projected to grow by 3.5% a year in the medium-term. Among individual product categories, fruit and vegetable juices are expected to continue as one of the largest processed agri-food imported into the European Union. It alone accounts for nearly 20% of all agri-food imports and it is expected to continue its robust growth, especially in tropical and exotic fruits that are abundant throughout Indonesia.
- *Consumer Electronics:* The size of the consumer electronics markets far exceeds that of any other focal industry covered by this study. Demand is highly responsive to income changes, but year-to-year variations in EU imports are high. The medium-term forecast is for a 2% average annual growth of imports.

- *Furniture:* The European Union is the world's largest market for furniture. The medium-term outlook is for a 2% annual growth in imports, as foreign supplies become an increasingly larger proportion of the total furniture market in Europe.
- *Natural Cosmetics:* The cosmetic market of the European Union is nearly as large as the combined markets of the United States and Japan. There is a rapidly expanding demand for natural and organic products. Cosmetic imports is projected to grow by 5-6% annually in 2010-2012, and thereafter accelerate to 7% a year.

#### ***4. Market Potential of Focal Sectors Needs to be Counter-Balanced with Compliance of Quality Requirements***

While the EU market offers enormous growth opportunities for Indonesian exporters, its regulatory environment has strict controls that are largely aimed at protecting consumers and the environment. Requirements covering security, technical, sanitary, phyto-sanitary, environmental and other regulations are generally harmonized among EU member countries. General regulations cover food and feed safety, environmental protection, marketing standards, product safety, technical standardization, packaging and labeling. Industry and product-specific requirements are also detailed in this study. This information is readily available and transparent to Indonesian exporters interested in selling their products in the EU market.

#### ***5. Indonesia is Well Positioned to Tackle Enormous Trade Potential with European Union***

Indonesia has numerous advantages in the EU market that could help to reverse the under-representation of the EU market in its export portfolio. It has low labor costs and ready access to an abundance of resources. Its export prices to the EU market are generally competitive in local currency units, notwithstanding the undervalued currencies of other major suppliers that have undermined Indonesia's price competitiveness in some products. With the likely re-alignment of currencies in the coming year, Indonesia's stable currency will undoubtedly attract investors. Business associations have also provided extensive support to the private sector. However, for many small and medium size enterprises (SMEs) there remains a lack of awareness of EU market access requirements, product design needed for European customers, and available government support programs. Information dissemination by both Government and business associations are therefore important means of ensuring that SMEs are able to successfully participate in value chains supplying the EU market.

#### ***6. Most Challenges for Indonesia are in Supply-Side Aspects, Especially the EQI (Export Quality Infrastructure) System***

Indonesia has suffered important losses in EU market shares in the last decade. The estimates of the export relationships in the focal industries suggest that those losses were largely due to non-price factors, including supply impediments from EQI limitations. For Indonesia's exports to the EU market, EQI issues center on the system used to meet EU import standards and requirements, certification of products and management systems, competence of laboratories related to export, accreditation of laboratories, metrology and inspection. Testing and accreditation difficulties are common issues for Indonesian

industries, as are the inability of laboratories to perform all testing and analysis required by the European Union. As a result, accreditation by the large number of certification bodies in Indonesia is not always recognised internationally. Notwithstanding challenges in overcoming these obstacles, the results of this study point to the enormous export revenue gains that Indonesia could achieve if industries were to overcome EQI and other supply-related constraints and place their products in the EU market. For the five focal industries covered by this study, it is estimated that in the last decade the average revenue gain from exports to the EU market would have been 28% higher if those supply-constraints had been overcome.

### 2.3. Trade Sustainability Impact Assessment (TSIA) of FTA between the EU and ASEAN (Ecorys Research, May 2009)

- **Indonesia would be expected to benefit from an (at the time ASEAN) FTA:**
  - **Structural change of production patterns; Elimination of non-trade barriers; technology transfers and Market access, especially for Indonesian SMEs**
  - **More specifically, with a full liberalisation of goods and half the protection in services, Indonesian would experience 1.81% GDP welfare gain by 2020, through efficiency gains but also structural gains.**
  - **Impact effects not so much in agricultural sectors (fishing +1%), but more on industry sectors: apparel +13%; textiles +10%**
  - **Increase in skilled workers wages (+2.5%)**

This Study is relevant in the way in which it approached FTA issues with suggested key points and methodologies, rather than simply a theoretical analysis of the benefits of an EU-ASEAN CEPA-FTA. The policy implications for a possible bilateral arrangement between EU and Indonesia are however of interest and in particular the "FTA flanking measures" remain valid and relevant also for a bilateral context. Overall the FTA is expected to have substantial positive impacts (GDP, income, trade and employment) for ASEAN and small but positive effects for the EU. An alternative bilateral arrangement would clearly focus on benefits for Indonesia and the EU rather than at the regional level, although the regional integration backdrop would remain important.

In an EU-ASEAN FTA context **Indonesia** would be expected to gain in electronic equipment, textiles and wearing apparel sectors, while motor vehicles and parts, gas production and businesses services would be expected to decline. Positive real income effects at sector level are expected for the TCF sectors in Indonesia (textiles). The Study argues that the extent to which investments within and from outside ASEAN will materialise depends on improvements to the investment and overall business climate. As the cost of doing business, and trade and investment restrictiveness are still quite high in some ASEAN countries and for some sectors, further reforms in this area are likely to lead to substantial benefits to intellectual property rights, protection and competition policy and services liberalisation. FDI will be encouraged further if intra-ASEAN integration and harmonisation progress further. This will allow foreign investors to trade more easily within ASEAN, strengthening the region's role as a production base.

In terms of *social impacts*, the FTA is expected to have an overall positive impact on poverty alleviation, albeit at the disaggregate level, while some groups may see an increase in poverty rates in the short run due to negative net price and income effects in the case of liberalisation beyond simple tariff reductions. These downside effects should be identified and steps taken to adjust and mitigate the position. The increased employment opportunities in the TCF sectors, Indonesia is expected to facilitate the structural transformation processes taking place as agricultural workers could, without substantial retraining, be absorbed into these sectors, thus also contributing to poverty reduction. In cereals and grains (particularly rice) and the fisheries sectors in ASEAN, some short-term poverty increases may occur as fisheries communities and rural areas see young people in particular move to urban areas to find employment in other sectors. The expansion of the financial services sector may contribute to poverty reduction provided micro-credits will increase. Increased access to insurance will also



provide social benefits. Improvements in *health and education* levels in ASEAN are expected from the overall increases in welfare, wages and household income. The higher health, safety and hygiene standards achieved by ASEAN producers as a result of compliance with SPS would benefit public health in ASEAN, and the same would be true for Indonesia in a bilateral context. Removal of investment barriers as a consequence of an FTA may open up some previously restricted social and environmental goods services sector to private and foreign investments, which could encourage efficiency gains and services improvements. Employment of both skilled and unskilled labour would increase substantially across ASEAN as a consequence of an FTA. A bilateral agreement would have similar aims. In terms of *equality*, expected changes in wages indicate that in some countries high-skilled wages will increase more than low-skilled wages leading to increasing levels of relative inequality. Regional disparities may also increase in ASEAN as a consequence of inter-sectoral shifts and wage effects in favour of urban areas. This issue might also apply to Indonesia as a very large and diverse archipelago, with very different levels of economic development between different areas, notably between Java and Eastern Indonesia. The growth of the TCF sectors in ASEAN as a consequence of the FTA is expected to benefit female labour in particular, as the sectors tend to employ predominantly females. Ensuring the FTA does not impact negatively on logging practices (taking into account existing illegal, unsustainable logging and land clearance problems,) means issues need to be seen in an integrated way. The Study recommends including enhanced application of voluntary certification schemes and negotiation of FLEGT Voluntary Partnership Agreements.

### **FTA and Flanking Measures**

The FTA is part of a more general process of enhanced cooperation and dialogue between the two regions, that is increasingly built on mutual interests and reciprocity and as such has graduated from a purely assistance based form of cooperation. The FTA and flanking measures should encourage convergence and cooperation through incentives and positive ongoing initiatives.

- *Phasing of Tariff Reductions* - The larger the envisaged tariff reduction in goods, tariff equivalent reduction in services, or NTB reduction, the more pronounced the specific short-term effects may be. For those sectors where potential short run negative impacts have been identified as a consequence of opening up, or where issues with relation to e.g. food security exist, the parties may consider a phased reduction of tariffs at a slower rate than what is foreseen in general, to allow for longer adjustment periods including through appropriate policy and legislative reforms and/or the building up of competitiveness.
- *Inclusion of a Sustainable Development Chapter (SD)* - that includes agreements and commitments on cooperation and progress towards specific social and environmental objectives.
- *Set up of Monitoring and Evaluation System* - Continuous monitoring of implementation and enforcement of the FTA as well as periodic evaluations, which involve local stakeholders, so as to allow for awareness raising and capacity building among these stakeholders, should analyse the impact of the FTA between the EU and ASEAN. The aim should be to understand why, how and where sustainability impacts occur, and what can be done to ameliorate the sustainability impacts.
- *Continue to improve business and investment climate* - Further improving the business and investment climate, including infrastructure development in ASEAN, reduction of

red tape and other investment barriers and generally reducing the cost of doing business, is needed to achieve the longer term effects envisaged. Similarly continuing the progress towards removal of NTBs to trade and investments within ASEAN will enhance the attractiveness of the region as an investment location.

- *Encourage convergence and information exchange and provide assistance on technical trade issues such as SPS and RoO* - Understanding and complying with rules and standards set within the national markets for public health and safety reasons or to avoid trade deflection is crucial for both parties to be able to actually benefit from the preferential access that the FTA would provide. Measures to encourage understanding and compliance could include closer regulatory cooperation initiatives, TA programmes in standard setting, implementation and exchange of scientific testing methodologies, upgrading of laboratories, revising and alignment of SPS and other control systems (certification) and capacity building for relevant institutions.
- *Information dissemination and exchange on the FTA (set up FTA Enquiry Points)* - The parties should consider the setting up of FTA Enquiry Points that may assist ASEAN producers in accessing EU markets, understanding RoO, complying with EU standard, provide information on investment conditions, etc.
- *Promote trade and investment in innovative technologies* - The objective of trade and investment in innovative technologies as a mitigating action is to provide the technical means to reduce various forms of pollution, health and safety threats on the work-floor and increase overall quality standards. The sectors where such an action could prove useful include fisheries and agriculture, textiles, clothing & footwear, food processing, chemicals, and automotives.
- *Involvement of key stakeholders* - Broad based involvement of the private sector and civil society in trade policy making and implementation is important for ensuring the agreements made truly reflect the interests of a society and takes into account sustainable development issues beyond narrow economic interest. Within ASEAN initiatives towards greater involvement of civil society – e.g. through tripartite dialogue between employer federations, labour unions and the government that are being developed – should be further encouraged and integrated into the overall policy making process.
- *Addressing concerns of ‘losers’ and dealing with resistance* - There are two types of losers that can be identified: on the one hand people working in those sectors or regions that are expected to experience declines, on the other hand people and organisations with vested interest that will likely resist changes that jeopardise their positions and income. The latter could be politically connected business tycoons heading monopolies, but also includes civil servants in e.g. customs who may see a loss of income from reduced opportunities to ‘charge extra’ for their services, due to improvements (automation) in customs procedures.
- This resistance tends to be stronger than the support from those who benefit economically, mostly because these groups (e.g. consumers) are more dispersed and less organised. Resistance also comes from those in society that do not understand the implications of the FTA, thus eliminating the possibility of a fact-based and argued discussion on its risks and merits. It is important to address the concerns of people benefiting from the status quo for loss of their position, by considering ways to compensate for loss of income of some and by further improvement of competition policy and the rule of law to address and avoid abuse of dominant positions and corruption.

#### **4. THE VIEW OF THE BUSINESS SECTOR: PRESENTATIONS BY KADIN AND EUROCHAM ON THE BASIS OF THE OUTCOME OF THE 2ND MEETING OF THE EIBD**

- **What are the most important ideas that private sector identified to increase trade and investment (opportunities)?**
- **What are the challenges?**
- **How can we support business dialogue and cooperation?**

Kadin and the European chambers in Indonesia have worked hand in hand to set up the framework of the EU Indonesia Business Dialogue including sectoral working groups to prepare joint position papers and develop business opportunities and an annual high-level Conference to produce policy recommendations enabling business leaders to directly impact on governments' policies.

This business dialogue will have provided sectoral and thematic discussions in a number of areas, notably:

- Medical & Pharmaceutical, Textiles/Apparel/Footwear, Infrastructure, Automotives & Machinery, Food & Beverage
- As well as horizontal discussions on: legal & regulatory issues; trade facilitation and emerging issues for growth.

Final recommendations will be provided after the EIBD Conference, but, from the position papers drafted by the EIBD sectoral groups, the following can be expected:

- strengthening the economy by agreeing on a broad economic partnership agreement
- improve transparency on regulations and regulatory cooperation
- challenges for Indonesian exports to the EU due to NTB, particularly SPS standards, and some EU environmental laws (FLEGT, RED,...);
- Indonesian burdensome mandatory certification and registration system for industrial (SNI, ML licensing, labelling) and agro food products (Law 18/009, ..) and alignment of Indonesia with international standards in key sectors (UNECE regulations for automotives)
- improve investment climate in key sectors (infrastructure, medical and pharmaceuticals) and ensure better protection of IPR to allow more FDI from EU companies;
- Support of the EU for tackling infrastructure and energy bottlenecks in Indonesia
- business community highlights importance to enhance transparency in policy making and sharing draft regulations with traders so as to minimize a negative impact on trade.

Furthermore, improving cooperation and dialogue between the two business communities is key to ensure that EU and Indonesia trade and investment relationships will tap into its real potential.

## 5. WHAT WE HAVE ALREADY IN PLACE: SHORT OVERVIEW OF THE AGREEMENTS OF INDONESIA AND THE EU WITH THIRD PARTIES

- **Good elements of our FTAs?**
- **Lessons learnt in terms of process?**
- **Any examples?**

Comparative tables for Indonesia and the EU are provided in annex

**Regarding the EU,** The 27 Member States of the European Union (EU) share a common trade policy. This means that the EU, its institutions and its Member States, act as a single jurisdiction on trade-related matters. International agreements concluded by the EU are binding on the EU Institutions and on the Member States.

The EU trade policy was launched in 2006 with the *Global Europe* Communication and very recently reinvigorated with a new Communication Trade, Growth and World Affairs by Commissioner Karel De Gucht. In 2006 the EU started a policy of stronger engagement with major emerging economies and regions and a sharper focus on barriers to trade behind the border by negotiating FTAs aimed at strengthening EU competitiveness. A number of criteria for this new wave of FTAs were highlighted (deep, comprehensive, covering services and investment as well as NTBs and rules). These Agreements should include provisions going beyond WTO disciplines on competition, government procurement, IPR and trade facilitation, and provisions on labor and environmental standards and simplification of ROO. The 2010 Communication reinforces the above message, focusing on GDP growth potential and jobs by finalising DDA as well as ambitious trade agreements with selected countries.

The Commission secured a mandate for new negotiations from the EU Council in April 2007. Since then, with the economic criteria of “market potential (economic size and growth) and the level of protection against EU export interests (tariffs and non-tariff barriers)” in mind, negotiations have started with three Asian partners, India, ASEAN and Korea, and in the case of the latter, recently concluded. In *Global Europe*, the Commission stressed commercial criteria for its new FTAs aimed at strengthening EU competitiveness, through “*stronger engagement with major emerging economies and regions; and a sharper focus on barriers to trade behind the border*”.

In terms of content, *Global Europe*’s stated aim was to have strong, comprehensive “WTO-plus” FTAs, with elimination of tariffs and quantitative restrictions (presumably, this should apply to at least 90-95% of tariff lines and trade volumes in order to comply safely with the “substantially-all-trade” criterion in Article XXIV GATT), a “far-reaching” liberalization of services and investment (presumably, services provisions should be compatible with the “substantial sectoral-coverage” criterion in Article V GATS), and provisions going beyond WTO disciplines on competition, government procurement, intellectual property rights (IPR) and trade facilitation, as well as provisions on labour and environmental standards. Rules of Origin (RoO) should be simplified. More generally, there should be strong regulatory disciplines and regulatory cooperation, especially to tackle non-tariff barriers. This should involve improved transparency obligations, mutual recognition agreements, conformity with international standards, regulatory dialogues and technical assistance.

Through the Communication, the EU expressed its seriousness about serious, commercially-meaningful and economically-relevant FTAs. The benchmarks for such FTAs were identified as follows:

- comprehensive coverage of trade in goods, with zero tariffs and quotas on at least 95% of trade volumes (and without wholesale exemptions for “sensitive” agricultural products);
- strong coverage of services and investment, underpinned by solid disciplines on domestic regulation;
- reasonably strong coverage of competition rules, government procurement and trade facilitation;
- improved transparency obligations and better regulatory cooperation, especially on non-tariff barriers;
- serious efforts to simplify ROO requirements;
- 4.1(a) and 4.3

The EU links its “non-trade” goals to its trade agreements, preferably by having non-trade provisions in such agreements. *Global Europe*, under the heading of “social justice”, sought to “promote our values, including social and environmental standards and cultural diversity around the world”, which brought to the commitment to include core labour and environmental standards in FTAs. The EU is also increasingly interested in linking trade policy to climate change. New FTAs will likely contain trade-and-sustainable-development chapters, which could house climate-change provisions in the future. In general, declaratory language on climate change, democracy, human rights and other EU issues could well be inserted into FTAs and linked to other non-trade bilateral agreements.

## **6. THE PARTNERSHIP AND COOPERATION AGREEMENT BETWEEN EU AND INDONESIA**

- **PCA to be ratified**
- **Already contains substantial trade and investment, still need for more?**
- **Includes a lot of cooperation, sufficient tool?**

The PCA was signed end of 2009 and still has to be ratified by a number of EU member states. It provides for comprehensive cooperation in the area of trade and investment, as given in Title IV, namely:

### **General Principles**

1. The Parties shall engage in a dialogue on bilateral and multilateral trade and trade-related issues with a view to strengthening bilateral trade relations and advancing the multilateral trade system.
2. The Parties undertake to promote the development and diversification of their reciprocal commercial exchanges to the highest possible level and to their mutual benefit. They undertake to achieve improved market access conditions by working towards the elimination of barriers to trade, in particular through the timely removal of non-tariff barriers and by taking measures to improve transparency, having regard to the work carried out by international organisations in this field.
3. Recognising that trade plays an indispensable role in development, and that assistance in the form of trade preferences schemes have proven beneficial to developing countries, the Parties endeavour to strengthen their consultation on such assistance in full WTO compliance.
4. The Parties shall keep each other informed concerning the development of trade and trade-related policies such as agricultural policy, food safety policy, animal health policy, consumer policy, hazardous chemical substances, and waste management policy.
5. The Parties shall encourage dialogue and cooperation to develop their trade and investment relations, including the provision of technical capacity building to solve problems, in the areas referred to under Articles 9 to 16.

### **Sanitary and Phytosanitary (SPS) Issues**

The Parties shall discuss and exchange information on legislation, certification and inspection procedures, within the framework of the WTO Agreement on Sanitary and Phytosanitary matters (SPS), the International Plant Protection Convention (IPPC), the Office International des Epizooties (OIE) and the CODEX Alimentarius Commission (CAC).

### **Technical Barriers to Trade (TBT)**

The Parties shall promote the use of international standards and co-operate and exchange information on standards, conformity assessment procedures and technical regulations, especially within the framework of the WTO Agreement on Technical Barriers to Trade

### **Intellectual Property Rights Protection**

The Parties shall cooperate on improving and enforcing Intellectual Property protection and utilisation based upon best practices, and enhancing the dissemination of the knowledge thereof. Such cooperation may include exchange information and experience on issues such as the practice, promotion, dissemination, streamlining, management, harmonisation, protection

and effective application of intellectual property rights, the prevention of abuses of such rights, the fight against counterfeiting and piracy.

### **Trade Facilitation**

The Parties shall share experiences and examine possibilities to simplify import, export and other customs procedures, increase transparency of trade regulations and develop customs cooperation, including mutual administrative assistance mechanisms and also seek convergence of views and joint action in the context of international initiatives. The Parties will pay special attention to increasing the security dimension of international trade, including transport services, and to ensuring a balanced approach between trade facilitation and the fight against fraud and irregularities.

### **Customs Cooperation**

Without prejudice to other forms of cooperation provided for under this Agreement, both Parties state their interest, in considering the possibility, in the future, of the conclusion of a protocol on customs cooperation, including mutual assistance, within the institutional framework laid down in this Agreement.

### **Investment**

The Parties shall encourage a greater flow of investment through the development of an attractive and stable environment for reciprocal investment through a consistent dialogue aimed at enhancing understanding and cooperation on investment issues, exploring administrative mechanisms to facilitate investment flows, and promoting a stable, transparent, open and non-discriminatory investment regime.

### **Competition Policy**

The Parties shall promote the effective establishment and application of competition rules and the dissemination of information in order to foster transparency and legal certainty for enterprises operating in each other's markets.

### **Services**

The Parties shall establish a consistent dialogue notably aimed at exchanging information on their respective regulatory environments, promoting access to each other's markets, promoting access to sources of capital and technology, promoting trade in services between both regions and in third countries' markets.



## 7. OVERVIEW BY EU ON BILATERAL AND REGIONAL ECONOMIC COOPERATION ACTIVITIES AND BY INDONESIA ON CURRENTLY FORESEEN NEEDS

- EU is providing substantial economic cooperation to Indonesia
- ... and committed to continue doing so in the future
- Where does IDN see priorities for such aid, in context of an agreement?
- Ways to work closer in ASEAN context?

### Bilateral support

The EU is providing development assistance that supports Indonesia in its integration into the world economy as well as its economic development in a sustainable manner. Two main programmes are of relevance for the trade and investment climate issues: EU-Indonesia Trade Support Programme II (15 million Euro), EU-Indonesia Trade Cooperation Facility (12.5 million Euro) and the grant programme in support of the Indonesian civil society (2.5 million euro). As Indonesia is very attracted to development assistance, utilisation of these funds and linking them to the trade files can help open up dialogue. One such example is the recently completed study on Indonesian market access to the EU (see above).

The Trade Support Programme II (TSP II) which started in December 2009 has a particular focus on improving policies and infrastructure to support enhanced access of Indonesian exports to international markets. It amounts to EUR 15 million and is being implemented over a period of seven years. The Indonesian Ministry of Trade (MoT) will be responsible for operational implementation for the programme, implying that the main directions of the programme will have to be set by the Ministry of Trade in support of Indonesia's export strategy. The Programme Director of the TSP II is the Head of the Standardisation Bureau of the Ministry of Trade. There are two components of the programme: **Policy Development** will pursue a cohesive legal, regulatory and institutional framework for the strengthening of the overall export quality infrastructure system. It will support the design of a strategic roadmap towards strengthening export quality infrastructure, provide expertise to review trade policy processes across Ministries and capacity building to identify and prioritise areas and agencies for support related to export quality infrastructure, and define action plans for their improvement. **Institutional strengthening**: the component will provide technical assistance to the range of government institutions engaged in export quality infrastructure and related activities. The support provided will be based on the strategic definition and prioritisation concluded in Component I. This component will include activities such as upgrading accreditation facilities, capacity building in quality and management systems for competent authorities, laboratories and certifying bodies and pilot programmes to strengthen export capacity in some priority sectors.

To strengthen the Government of Indonesia's (GoI) reform efforts, this AAP is aimed at targeting areas that are critical for underpinning sustainable development, with a focus on the improvement of trade & investment climate as well as in the mitigation of the environmental impact of economic growth. This support will be provided along two complementary components:

The **Trade Cooperation Facility**, a flexible, demand driven facility, supporting those parts of the government that demonstrate willingness and interest in pursuing relevant reforms (EUR 12.5 million). The programme aims at being a flexible mechanism, responding to priorities and needs that may arise during the formulation of the yearly work programmes. Due to the

broad scope of the programme, the EU foresees to cover a wide range of sectors and government agencies in the areas of IPR, investment facilitation, trade policy formulation, energy, science and technology and trade related environment issues. The grant programme to support the Indonesian civil society organisations (CSOs) active in the trade and investment and environment areas to better enable them to effectively demand reforms and constructively engage with the government in elaborating such reforms (EUR 2.5 million) To strengthen the capacity of relevant CSOs to effectively advocate and engage with the government and other stakeholders in the pursuit of reform initiatives in selected areas related to the improvement of trade and investment climate in Indonesia.

### **Support to ASEAN**

ASEAN has ambitious objective of achieving the ASEAN Economic Community by 2015. While an important number of regional agreements have already been signed, the implementation of these agreements remains problematic. There is an important EU-ASEAN cooperation programme that aims at supporting ASEAN Economic Integration (6 on-going or about to start projects, amounting 38.7 M. Euro, covering areas such as customs, standards, IPR, single civil aviation market, statistics for trade and investment and other trade-related aspects). EU is looking at establishing a regular and wider dialogue (with SEOM on ASEAN economic integration and cooperation), to better link cooperation programme with policy objectives. **Some results:**

With the support of the ASEAN Programme for Regional Integration Programme Support – Phase II (APRIS II) and APRIS I and Standards previously, EU has contributed to develop building blocks of ASEAN Economic Community. Important steps in ASEAN Economic Integration, among which: The ASEAN Cosmetic Directive, which is now implemented by almost all AMS; The ASEAN Customs Transit System has been finalised and will be signed by the end of 2010 by the Economic Ministers; Standardisation of customs documents: the ASEAN Common Declaration Document (ACDD) ; Air Cargo Clearance Processing model developed. Pilot testing implemented in Malaysia and Philippine.; ASEAN Blueprints on Human Resource Management and Integrity adopted by ASEAN Customs DGs in 2010

MoU signed between Singapore, Brunei and Malaysia on Self Certification system for Rules of Origin

with the support of our EU-ASEAN Statistical Capacity Building Programme (EASCAB), the ASEAN chairman Statement issued at the 17th ASEAN Summit in Hanoi (28/10/10) did include a paragraph on the adoption of the ASEAN Framework of Cooperation in Statistics (AFCS) 2010-2015 by the ASEAN Heads of Statistical Offices Meeting (AHSOM) which would facilitate recognising the role of the ASEAN Community Statistical System to produce regular quality statistical data. This will pave the road for the implementation of a new strategy. ASEAN Cooperation Project on the Protection of Intellectual Property Rights (ECAP III): started in 2010, the programme will facilitate ASEAN regional integration by building capacity in the ASEAN Secretariat and the ASEAN Member States to manage and benefit from a reinforced IPR system.

New programmes will start in 2011 are support to ASEAN FTA negotiating process (2.5 M. euro) and the ASEAN Economic Integration Support Programme (15 M. euro). These projects will support ASEAN regional economic integration but will also provide room for policy dialogue between EU and ASEAN Secretariat