ILO/ASEAN Joint Study on:

Social Implications of ASEAN Free Trade Agreement (AFTA) on Labour and Employment: The Case of Indonesia

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In May 2003, a joint ILO-ASEAN mission reviewed ILO Initiatives for Decent Work and ASEAN IAI *(Initiative for ASEAN Integration)* Priorities on Labour and Employment. The mission identified several areas of work and priorities for ILO-ASEAN cooperation on labour and employment issues over the following years, one of which was a review of the labour and employment implications of the ASEAN Free Trade Area (AFTA).

For the purpose of the review, studies were commissioned in four ASEAN countries, namely Indonesia, the Philippines, Thailand and Vietnam. The Indonesian study was conducted by Dr. Tirta Hidayat and Dr. Diah Widarti. The report was prepared following consultations with the government, employers, unions and other interested groups.

We hope that the results of the study will promote greater understanding of the employment and labour impacts of trade liberalization moves and will assist in the development of policies and strategies in ASEAN countries to deal with them.

Alan Boulton
Director
ILO Jakarta Office

December 2005

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CHAPTER 1
INTRODUCTION

1.1. Background

Globalization has promoted open societies, open economies and encouraged a freer exchange of goods, ideas and knowledge. Nevertheless there is a growing concern about the direction of the current globalization. Some observers consider that its advantages are too little for too many, while its threats are enormous.

Furthermore, although a country's economy is becoming increasingly global, social and political institutions remain largely local, national or regional. The existing global institutions do not provide adequate democratic oversight of global markets, or redress basic inequalities between countries. These imbalances point to the need for better institutional frameworks and policies if the promise of globalization is to be realized. The imbalance between the economy and society is threatening social justice. A growing division between a formal economy and the expansion of an informal local economy apparently exists in most societies. The majority of the people living and working in the informal economy continues to be excluded from directly participating in markets and globalization on a fair and equal basis.

In May 2003, a joint ILO-ASEAN mission reviewed ILO Initiatives for the Decent Work agenda and ASEAN IAI Priorities on Labour and Employment. The mission identified several areas of work and priorities for ILO-ASEAN cooperation on labour and employment issues over the next 3-4 years. One of the priorities is a review of labour and employment implications of the ASEAN Free Trade Area (AFTA) and other trade liberalization moves. The IAI Work Plan also calls for a tripartite seminar on the implementation of AFTA and its impacts on ASEAN labour/human resources, with a view to raising awareness and sharing lessons learnt among ASEAN member States.

With this background, this study aims to conduct a review of labour and employment implications of the AFTA and other trade liberalization initiatives particularly the accession to the World Trade Organization.

1.2. Objective

The *immediate objective* of the study is two-fold:

- To enhance understanding of the labour and employment implications of AFTA in the context of globalization, and increase awareness of these implications among tripartite constituents (various government ministries, employers' and workers' organizations) and other key stakeholders in ASEAN countries;
- To identify policy options for integrated economic, labour and social policies to address labour and employment implications of AFTA, as a basis for recommendations for consideration by ILO/ASEAN Governments;

The *medium term objective*

- The effort is intended to strengthen the ILO-ASEAN partnership to meet the challenges of globalization.

1.3. Methodology

The research will be based on primary and secondary data. An examination of primary and secondary sources, the analysis of statistical data and interviews with key actors as appropriate, including representatives of national and sectoral employers' organizations, workers' organizations, and of relevant ministries is conducted.

For the case study, three sectors, namely the garments, transport equipment and wood-furniture industries are taken up. The first two sectors are chosen by the ILO so that a comparative study with the other ASEAN countries can be conducted, while the selection of the last one is based on the criteria that the industry, to a large extent, is nationally owned and is a local industry with relatively high labour absorptive capacity, and are exposed to international trade.

The study is to address the following points

- Indonesian economy and trade (AFTA and WTO)
- Trade liberalization (unilateral, bilateral, sub-regional, regional and multilateral)
- Trade and industrial policies
- Labour and trade sector
- Gender and trade
- Production sharing
- Competition
- Migration
- The benefits and social costs of trade and growth arising from economic integration distributed between workers and employers

Analysis

The study will gather information and opinion from stakeholders. Such information will be analyzed by using the **Analytic Hierarchy Process (AHP)**, which hereafter is referred to as AHP. This method requires the availability of primary data, in this case is the perception of respondents that are considered as "experts" in terms of having the respective knowledge and understanding as well as having the decision making position. Ideally, to obtain optimum results, respondents should be gathered in a forum and are asked to discuss about the issues that are being faced and to give judgements that are jointly agreed upon. But, due to the limitation of space and time, this process can not be conducted. It is therefore to obtain grouped perception from various respondents and to maintain the consistency of the results, each perception should be multiplied and squared to the number of respondent that give assessment or the so-called geometric mean method $((a_1 \times a_2 \times a_3 \times \ldots \times a_n)^{1/n})$.

It should be noted that this study uses the net benefit approach (Benefit* Opportunity/Cost*Risk) or the so-called BOCR approach to know the magnitude of the ratio of Benefit-Cost of the existence of AFTA and other trade liberalization for labour and employment. Meanwhile, respondents giving the assessments cover three groups namely the government, employers and employees. The government group consists of the Deputy of Macro Analysis and Finance of the Coordinating Ministry of Economic Affairs; the Director of the Manpower and Economic Analysis Directorate of the National Development Planning Agency (BAPPENAS), the Head of the Centre for Foreign Relation Administration, the Ministry of Manpower and Transmigration, and the Chairman of Training and Productivity Board, Ministry of Manpower and Transmigration. The employers group is represented by the Association of Indonesian Employers (APINDO), while the trade union group is represented by the *Serikat Buruh Sejahtera Indonesia* (SBSI), the *Serikat Pekerja Seluruh Indonesia* (SPSI) and the *Koperasi Buruh Indonesia*.

1.4. Expected Output

The study findings and recommendations on policy options to address the labour and employment implications of AFTA will be submitted for consideration by the ASEAN Governments through the ASEAN Secretariat. The ILO will submit them to the tripartite constituents through appropriate meetings. Follow-up policy dialogues could be held with the Senior Labour Officials and ASEAN Labour Ministers through the network of the ILO offices. Publication of the country studies and synthesis report is planned.

1.5. Organization of the Report

The paper is organized as follows. Capter two discusses a brief review of Indonesian economy and followed by various aspects of trade liberalization that Indonesia has experienced in Chapter Three. Chapter Three also presents the efforts through the unilateral, Uruguay Round/WTO, APEC and AFTA processes and the policies adopted by Indonesia. The fourth chapter focuses on the implications of free trade, particularly of AFTA, on employment and labour issues such as wages, working conditions, and migration. The fifth chapter discusses case studies of three sectors (the garments, transport equipment and wood furniture industries). The sixth chapter presents the result of AHP analysis which elaborate the positive and negative impacts of free trade. The paper closes with a number of conclusions and recommendations.

CHAPTER 2
THE INDONESIAN ECONOMY AND TRADE SECTOR

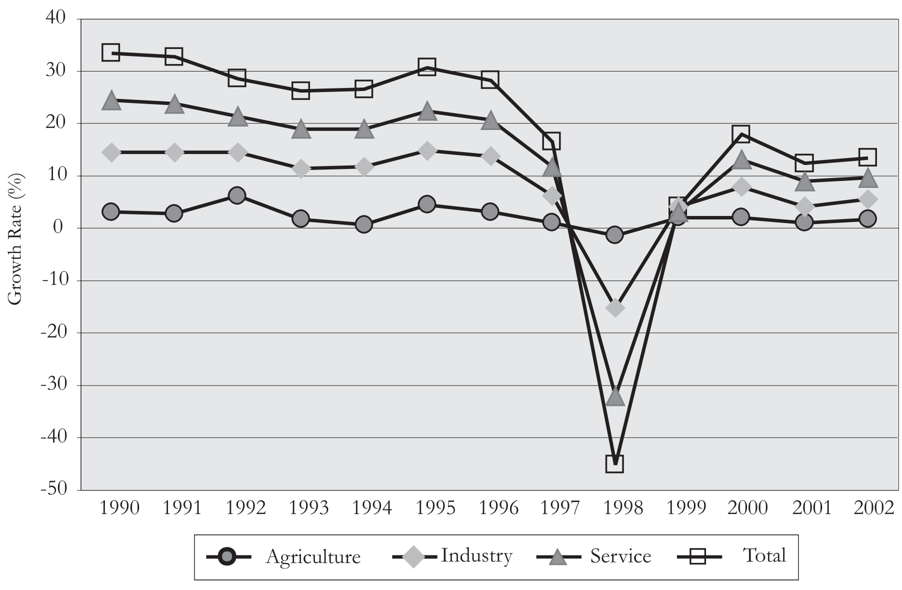
This chapter discusses the performance of the Indonesian economy, as basically indicated by its Gross Domestic Product (GDP), including changes in the sectoral composition of the GDP, and trends of investment and foreign trade of the economy. A review of these aspects is important to gain broader and deeper insights on their relation to employment and labour issues.

2.1. Indonesian Economy

Gross Domestic Product

In the early part of 1990s Indonesia enjoyed high economic growth that was particularly supported by the high growth of the manufacturing and service sectors (Chart 2.1.). Nevertheless, the 1997 Asian crisis has brought down the Indonesia economy to a severe recession in 1998. The growth of GDP fell significantly from 7.8 percent in 1996 to 4.7 percent in 1997 and dropped drastically to minus 13.2 percent in 1998. Signs of economic improvement in Indonesia started to emerge in 1999. In 1999 and 2000 GDP grew by 0.8 percent and 4.9 percent respectively, but declined to 3.4 percent in 2001 in line with the unstable domestic political climate and worsened global condition. The economy showed encouraging signs of recovery from mid 2002. GDP growth in 2002 was quite moderate at 3.7 percent (Chart 2.1.). This was supported by stable monetary conditions as indicated by the appreciation of the *rupiah*, declining inflation from 12.55 percent in 2001 to 10.03 percent in 2002 which allowed significant domestic interest rate reductions.

Chart 2.1. Growth Rate of the Gross Domestic Product (GDP) by Main Sectors, 1990-2002



Source: CBS, Statistics of Indonesia, various publications.

Recent macroeconomic policies, including continued tight monetary policy to control inflation, and a mild fiscal expansion (with the budget deficit increasing from 1.7 percent in 2002 to 1.8 percent in 2003), have helped consolidate fiscal sustainability. The faster than expected declines in public debt levels, are estimated to continue with continued fiscal consolidation. The government plans to reduce the budget deficit to less than 1 percent of GDP in 2004.[1]

In 2003 GDP growth was expected to be in the range of 3.5-4 percent. An improving international environment and further declines in interest rates are expected to support growth in the years ahead, although slowing investment may constrain GDP expansion in the medium term. Private consumption remains the main source of growth, accounting for 91 percent of GDP growth in 2002 and 83 percent in the first three quarters of 2003. The recent decline in interest rates contributed to higher consumption growth (Bank Indonesia, 2003). In August 2003 the government had decided not to renew the IMF supported program, which was broadly appreciated by the markets and the international community, and is warranted by the strong improvements in the country's recent macroeconomic conditions (WTO, 2003).

Economic structure is also improving. Table 2.1.. shows that Indonesia's GDP has significantly shifted from an agricultural base to manufacturing and services. In 1985, manufacturing sector only contributed 15.8 percent to the GDP, but rapidly increasing to 20.6 percent in 1990. In 1997, manufacturing sector's share to GDP gone up further to 24.8 percent, and to 26 percent due to the slight recovery of the Indonesian economy in 1999. Although declined slightly to 24.9 percent in 2000, in 2002 the share has reached 26.6 percent. Meanwhile the trade sector, including hotels and restaurants, had contributed 14.6 percent to the GDP in 1985, and slightly increased to 15.9 percent in 1990. The share of trade, hotels and restaurants went up to 17.0 percent in 1997 and has been slightly declining over the years, to reach 16.2 percent in 2002.

In September 2003, as a follow-up to the termination of the IMF supported program, the government issued the *"Economic Policy Package Pre and Post IMF"* or known as *the White Paper* through a presidential instruction (*INPRES* No.5/2003). The main objective of this policy package is to maintain macroeconomic stability over the medium term. This complements the measures included in the Instruction of the Governor of Bank Indonesia, that was aimed at continuing the prudential monetary policy of recent years.

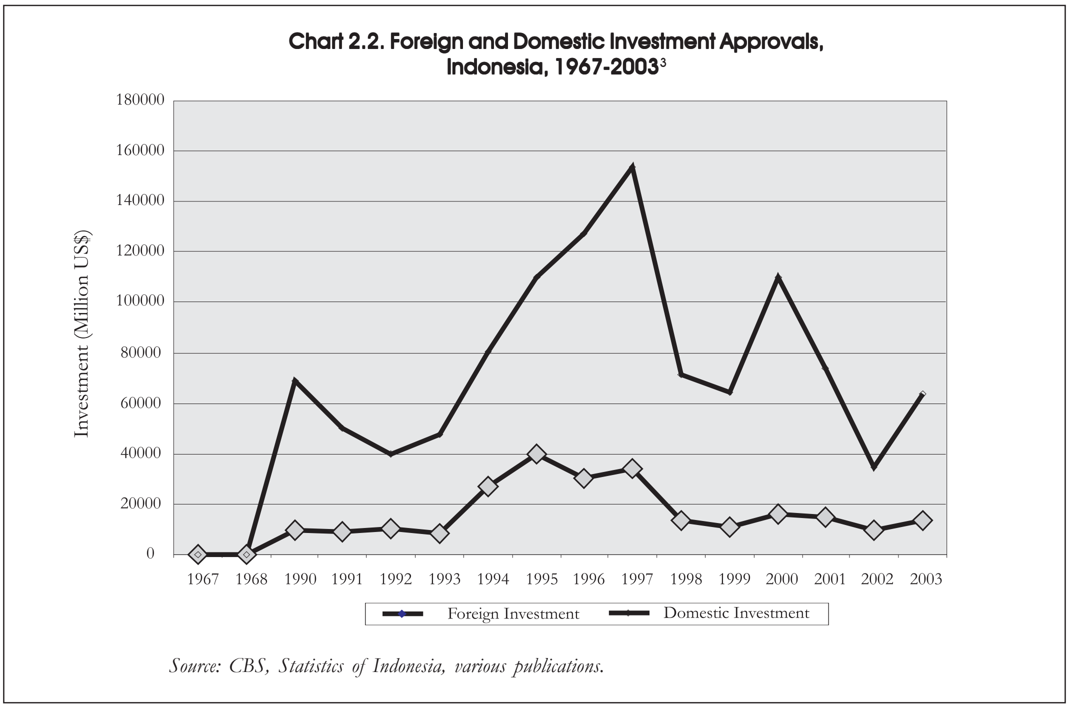
2.2. Investment

The progress of investment during the crisis has not been too supportive for Indonesian economic recovery. The total approvals of domestic investments had reached Rp 119.88 trillion in 1997. Then it fell to Rp 53.1 trillion in 1999. In 2000 domestic investment rose by 77 percent to Rp 92.4 trillion, but it declined to Rp 58.8 trillion in 2001 (Chart 2.2.). Throughout 2002, the approval of domestic investment fell sharply by 57 percent to Rp 25.2 trillion (CBS, 2002: 78).

Likewise, since the economic crisis, foreign investment in Indonesia has performed well below expectations. Out of 140 countries, Indonesia's investment performance index slumped from the 63rd during the period of 1988-1990 to the 138th during the period of 1998-2000 and the investment potential index plunged from the 73rd in 1988-1990 to the 110th in 1998-2000.[2] Since 1997, Indonesia recorded a net private investment outflow each year, reaching its climax at 14.2 percent of the GDP in 1998, and declining to 5.9 percent of GDP in 2001, and to 1.7 percent of the GDP in 2002 (Annex 1). The outflows were mostly originated from ethnic Chinese-entrepreneurs who felt threatened by ethnic conflicts that took place during the earlier part of the crisis.

1 Ministry of Finance (2003).

2 UNCTAD (2002). World Investment Report



Further observation reveals that the decline in foreign investment approvals[4] after the crisis occurred across all sectors **(Table 2.2.)**. The inflow of foreign investments into Indonesia's economy until 2000 showed that the greater part of these investments was directed to the manufacturing sector **(Table 2.2.)**. Most recent foreign investment approvals show that the share of services sector to total investment increases to 49 percent in 2002 from 29 percent in 1997. For the manufacturing sector the share was 44 percent of total investment approved in 2002, which decreased from 69 percent in 1997 **(Table 2.2.)**.

Within the secondary sector, foreign investments were mainly directed to chemical and pharmaceutical industry. Even though the foreign investment value in chemical and pharmaceutical industry declined after 1997, yet the share of investment in total manufacturing industry remained high, accounted for 70 percent in 1998. The amount of approved investments in textile industry was also declining, from US$ 178 million in 1997 to US$ 93 million in 2002 **(Table 2.2.).** A similar trend is also observed for machinery and transport equipment. In 1998 the value was only one third of the 1997 value; and in 1999 the value was around one ninth of the previous year **(Table 2.2.).**

In term of its country of origin, foreign direct investment approvals mainly originate from Asia, especially from Japan. In 1997 apart from Japan, 10 percent of total foreign investment came from Chinese Taipei. After the crisis, even though Japan was still a major investor to Indonesia, an increasing role was also demonstrated by Singapore, Malaysia, and Hongkong-China. In 1998 these three countries dominated over 90 percent of total approvals from Asia in 1998. In 2001 more than two third of foreign investment in Indonesia came from Asia **(Table 2.3).** European investment approvals, particularly from UK and Germany, have declined sharply during the crisis, from 35 percent in 1997 to 10 percent in 2001. Compared to other SEA countries the flow of foreign investment into Indonesia is very slow due to relatively less favourable investment and business climate in Indonesia as compared to other SEA countries.

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3 Note (1). Excluding of Oil & Gas, Banking, Non Bank Financial Istitution, Insurance and Leasing, Mining in Terms of contracts of Work, Coal Mining in Terms of Agreement of Work, Investment which licenses issued by technical/sectoral agency, Portfolio as well as household investment (2). Number of Projects = New Project + Change of Status (3). Investment Value = New Project + Expansion + Change of Status (4). Tentative data, including approvals issued by regions received by BKPM until May 31, 2004.Source: Investment Coordinating Board (website visited on 18 June 2004).

4 Investment approvals should be interpreted as an indicator of investor interest and intentions. This is not as a proxy for realized investment. In fact, studies show that investment approvals are weak predictors of realized investment and that only a small proportion, between 10-25 percent of approvals are usually implemented within three years after approval has been given (USAID, 2004).

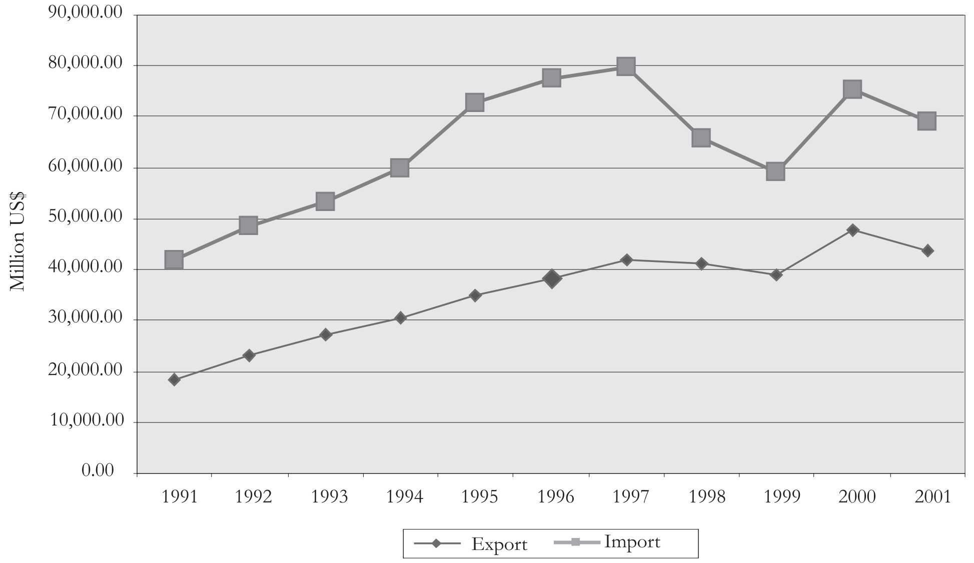
2.3. Trade

Indonesian exports, particularly after the crisis, had experienced significant fluctuations. Indonesia's exports steadily increased during 1991-1997 then declined in 1998. In 1998, total exports reached US$48.8 billion and rose to US$62.1 billion in 2000 and fell to US$56.3 billion in 2001. The strong exports in 2000 were due to increased oil-gas and non-oil-gas exports. In 2002, total exports only increased slightly to US$57 billion. Imports, however, has declined earlier than exports **(Chart 2.3.).** Even though merchandise trade had bounced back after the crisis, due to a worsening Indonesian political condition that induced economic uncertainties as well as depressed overseas markets, trade performance deteriorated in 2001 and 2002 both for non-oil/gas and oil/gas exports. To regain its export drive, the government provides some incentives.[5]

Non-oil/gas exports were dominated by manufacturing sector, which contributed the largest share in the structure of non-oil/gas exports, followed by mining and agricultural sector **(Table 2.4.).** The export values of some commodities in the agricultural sector increased in 2002 compared to the previous years, these included coffee, spices, fish and related products, tea, and cocoa. Such increase was most likely stimulated by price increase in the international market while export volume was relatively stable (Bank Indonesia, 2003).

Some main non-oil/gas export commodities such as garments, wood products, tulle and laces, basic metal, and footwear recorded a decline in terms of value **(Table 2.4.)**. The decline of garment exports were likely due to problems faced by producers such as aging machinery, limited sources of investment and the emergence of new competitors such as China and Vietnam. Meanwhile, the decline in wood product exports was due to the decreasing supply of raw materials due to the restrictions of wood logging under the Decree of the Ministry of Forestry and Forest Conservation No. 156/KPTS-II/2003. In addition, the difficulty in obtaining raw materials was also related to logs being smuggled out of the country, which was closely related with the practice of illegal logging (Bank Indonesia, 2003: 81). Likewise, footwear industry also experienced a decline which was likely due to tighter competition abroad.

Chart 2.3. Indonesia's Foreign Trade, 1991-2001 (exports excluded oil/gas)



Source: CBS, Statistics of Indonesia, various publications.

5 Such incentives provided for exporting manufacture products as the following (a) restitution (drawback) of import on the importation of goods and materials needed to manufacture the exported finished products (b) exemption from Value Added Tax and Sales Tax on Luxury goods and materials purchased domestically, to be used in the manufacturing of the exported products and (c) the company can import raw materials required regardless of the availability of comparable domestic products (BKPM website).

The slow growth in manufacturing exports may reflect increased competition from countries such as China and Vietnam, which compete in the same low-skill labour-intensive products in which Indonesia has a comparative advantage. It may also reflect the bleak performance in FDI over the years since the onset of the crisis. This stems from the fact that foreign-investment was the main driver for export growth prior to the crisis, but has been losing ground in recent years. Even if there is any improvement in exports, several constraints remained. These constraints were derived from the declining Indonesia's export competitiveness, a weak global economy and intense global competition. Indonesia's low competitiveness was reflected in a lower exports share in destination countries, while the share of major competitors such as China augmented. On the internal side, exports were constrained by security and labour issues, which caused several companies to relocate their operations abroad[6] (Bank Indonesia, 2002 Annual Report).

With regard to the Indonesia's manufacturing competitiveness, the UNIDO reveals that Indonesia lagged behind from its ASEAN neighbouring countries **(Table 2.5.)**. The competitiveness reflected in the index of manufacturing value added per capita shows that Indonesia ranked 67, while Singapore and Malaysia for example ranked 4 and 32 respectively. Moreover the final index of share of medium and high technology products in manufacturing exports shows that Indonesia was on the 49th position , while Singapore and Thailand were respectively on the 1st and 32nd, out of 87 countries.

In 2003 Indonesia's imports grew by 9.4 percent to reach US$ 39 billion, which was due to the increase in both oil /gas and non-oil/gas sectors (Bank Indonesia, 2003: 82). The rise in imports occurred in almost all product groups, in line with the increase in domestic demand. Increased oil/gas imports were related to higher domestic consumption of fuel in line with growing economic activity in the country as well as the increase in oil prices in the international market. The import value of non-oil/gas consumer goods rose up by 7.6 percent in line with stronger economic growth stimulated by consumption activity; these covered among others food and beverages for households, passenger cars, non-industrial transportation equipment, non durable consumer goods, and military equipment.[7]

The increase of oil price from US$24.4 per barrel in January 2000 to US$30 per barrel at the beginning of May 2000 had impacted both exports and import performances. In line with the sharp increase of export in 2000, imports also increased to US$40.4 billion, but it declined to US$34.7 billion in 2001 and virtually unchanged to US$34.8 billion in 2002. The declining trend in imports in 2001 and 2002 was mainly contributed by declining trend in non-oil-gas imports as investment climate worsened.

In 1985 almost 75 percent of the Indonesian value added that originate from manufactured exports were low technology and resource based. Along with the increasing use of medium and high technology, value added share from low technology and resource based manufactured exports reduced to 60 percent in 1998. The share of value added from medium and high technology in manufactured exports from 1985 to 1998 has increased from 25 to 40 percent respectively **(Annex 3).** These attributes have put Indonesia ranked the last among the ASEAN-6 plus China on the 60th in 1985, although increased to the 42nd in 1998. Meanwhile for the same period China was on 48th rose up to 29th subsequently **(Annex 4)**.

Trade Destination

Indonesia's structure in terms of trading partnership has not changed much since 1996. Indonesia's major trading partner has been East Asian countries, especially Japan, accounting for over quarter of total exports **(Annex 5 and Annex 6)**. In fact, the destination of Indonesia non-oil/gas exports was concentrated to Japan, US and Singapore. Although declining, Indonesia's non oil/gas exports to the US remained high, and the share of Indonesia to China tended to increase. The first biggest trading partner in 2002 remained Japan (21 percent of exports and 14.1 percent of imports), the second largest was the EU, followed by the United States (13.2 percent of exports and 8.4 percent of imports)

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6 Several firms even have relocated their plants to other countries due to such unfavorable business climate as rising manpower cost and others.

7 See Bank Indonesia. 2003. See Table 6.6., 6.7, 6.8 and 6.9

and Singapore (9.4.percent of exports and 13.1 percent of imports). While Indonesia's total exports grew at 2.3 percent during 1996-2002, its exports to China grew at 5.9 percent in the same period and at a high 31.9 percent during 2001-2002 **(Annex 5)**. For imports, the world's share of Indonesian imports declined by an average of 5 percent per annum during 1996-2002, while China's share of Indonesian imports rose on the average by 7.4 percent per annum during the same period.

After the financial crisis, Indonesia's share of exports to ASEAN partners has been fluctuating from 14.8 percent in 1996, to 15.6 percent in 1998, down to 15.0 percent in 2001 and further down to 13.9 percent in 2003. Over the same period, its share of imports from ASEAN partners has been increasing from 6.6 percent to 9.7 percent, to 10.3 percent and further up to 15.1 percent in 1996, 1998, 2001 and 2003 respectively **(Annex 5 and 6)**. However, on the average Indonesia's exports to ASEAN grew by 2.7 percent per year, while the imports from ASEAN declined at the average of -0.32 percent per annum **(Annex 7)**. ASEAN members may be diverting trade between themselves and non-members by providing each other tariff preferences on most imports under AFTA.

Table 2.1. Percentage Distribution of GDP by sector, selected years (at 1983/1993 constant prices)

Economic Sector	1990	1997	2002
Agriculture	20.15	14.88	15.94
Mining	10.11	8.90	9.32
Manufacturing	20.59	24.84	26.64
Electricity, gas and water	0.95	1.26	1.76
Construction	5.78	8.16	5.92
Trade	15.85	16.97	16.24
Transport and communications	7.02	7.34	7.89
Finance	8.16	8.90	7.02
Public administration	7.88	5.45	5.36
Others	3.50	3.30	3.92
Total Percentage	100.00	100.00	100.00
Value at 1983/1993 constant prices (billion rupiah)	263.262	433.246	42.674

Source: Asian Development Bank

Table 2.2. Trend of Foreign Investment Approvals by Sector (million US$), 1997 - April 30, 2004 (Based on ISIC Revision 3)

Economic Sector	1997	1998	1999	2000	2001	2002	2003	2004
Primary Sector	24,059.0	9,239.8	7,859.3	12,054.3	5,823.7	3,663.0	7,474.0	1,887.6
Secondary Sector	23,021.8	8,529.2	6,907.7	10,759.6	5,148.7	3,258.2	6,567.7	1,364.5
Food Industry	676.4	383.7	670.1	759.5	289.1	267.4	507.1	206.4
Textile Industry	178.1	193.4	166.9	205.6	329.9	93.3	123.0	314.9
Leather Goods & Footwear Industry	142.4	35.6	65.6	205.4	32.6	13.8	34.4	1.4
Wood Industry	40.3	97.9	49.0	124.2	23.4	30.3	241.8	0.4
Paper and Printing Industry	5,337.2	44.8	1,387.4	90.4	742.1	10.0	1,300.0	25.9
Chemical and Pharmaceutical Industry	11,944.8	5,972.8	3,193.2	7,288.9	2,309.9	1,872.3	3,034.6	55.4
Rubber and Plastic Industry	316.9	221.0	95.8	166.4	225.9	283.2	76.2	34.1
Non Metallic Mineral Industry	1,469.0	224.8	114.0	8.8	108.1	32.7	711.5	28.0
Metal, Machinery & Electronic Industry	1,325.6	885.9	998.0	1,524.0	653.0	349.1	323.3	683.3
Medical Preci. & Optical Instru, Watches & Clock	27.7	8.9	47.3	67.6	31.0	3.2	4.7	1.3
Motor Vehicles & Other Transport Equip. Ind.	1,220.8	404.7	44.6	241.2	355.1	266.0	146.7	10.9
Other Industry	342.6	55.7	75.8	77.6	48.6	36.9	64.4	2.5
Tertiary Sector	10,140.1	4,106.7	3,323.0	4,721.2	9,395.9	6,029.0	6,819.0	885.4
Total	**33,788.8**	**13,649.6**	**10,884.4**	**16,075.6**	**15,056.3**	**9,795.4**	**13,583.8**	**2,300.5**

Note :

1. Excluding of Oil & Gas, Banking, Non Bank Financial Istitution, Insurance and Leasing, Mining in Terms of Contracts of Work, Coal Mining in Terms of Agreement of Work, Investment which licenses issued by technical/sectoral agency, Portofolio as well as household investment.

2. Number of Project = New Project + Change of Status
3. Value of Investment in Million US$. = New Project + Expansion + Change of Status
4. Tentative data, including approvals issued by regions received by BKPM until April 30, 2004.

Source: BKPM

Table 2.3. Approved Foreign Direct Investment by Country of Origin, Indonesia, 1997-2001 (Per cent)

Country	1997	1998	1999	2000	2001
Europe	34.7	39.2	6.7	38.4	10.2
Netherlands	0.9	3.0	0.4	7.6	1.0
United Kingdom	16.2	35.0	4.7	23.4	8.1
Germany	13.2	0.5	0.8	6.3	0.5
France	1.4	<0.1	0.2	0.4	0.2
America	3.3	5.2	1.3	1.7	0.9
United States	3.3	4.2	1.3	1.6	0.8
Asia	44.8	34.5	59.6	24.9	68.5
Hong Kong, China	0.7	4.0	0.7	0.7	0.4
Japan	16.0	9.8	5.9	12.8	8.5
South Korea	4.2	1.5	2.4	4.5	4.0
Malaysia	6.8	7.8	1.7	1.1	24.8
Singapore	6.8	9.3	6.7	3.5	12.6
Chinese Taipei	10.1	1.2	13.7	0.9	0.8
Australia	0.6	0.6	22.7	0.4	2.9
Africa	0.3	0.5	0.6	3.1	6.2
Joint countries	16.3	20.0	9.1	31.5	11.3
Total	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

Source: Bank Indonesia (2002), Annual Report 2001.

Table 2.4. Export of Non-Oil/Gas by Sector and Commodities, Indonesia, 2001- 2002 (BPS)

No. Sector/Goods	FOB Value (Million US$) 2001	2002	Growth Absolute	Percent
I. Agricultural Products	2 438,5	2 568,3	129,8	5,3
II. Industrial Products	37 671,1	38 729,6	1 058,5	2,8
1 Plywood	1 837,9	1 748,3	-89,6	-4,9
2 Garments	4 476,5	3 887,2	-589,3	-13,2
3 Processed Rubber	1 207,5	1 560,6	353,1	22,6
4 Furniture & Parts	1 414,3	1 501,9	87,6	6,2
5 Tulle and Lace	1 527,6	1 258,4	-242,2	-15,8
6 Base Metal Goods	2 042,8	1 902,5	-140,3	-6,9
7 Electrical Appliance	2 605,1	2 700,0	94,9	3,6
8 Audio Visual	3 259,2	3 291,3	32,1	1,0
9 Fertilizer	130,2	134,6	4,4	3,4
10 Palm Oil	1 080,9	2 092,4	1 011,5	93,6
11 Footwear	1 505,6	1 148,1	-357,5	-23,7
12 Processed Food	1 042,5	1 184,1	141,6	13,6
13 Others	15 541,0	16 293,2	752,2	4,8
III. Mining Products	3 569,6	3 743,7	174,1	4,9
IV. Other Sectors	**5,4**	**4.5**	**-0,9**	**-16,7**

Source: Central Bureau of Statistics

Table 2.5. Rank of Manufacturing Competitiveness of Several SE Asian Countries (Out of 87 countries)

Country	Manufacturing Value Added per Capita Index	Manufacturing Exports per Capita Index	Share of Med-and High Tech Activities in Manufacturing Value Added Index	Share of Med-and High Tech Products in Manufacturing Exports Final Index
Singapore	4	1	1	1
Hongkong	29	26	26	30
Malaysia	32	29	28	22
Thailand	44	42	39	32
China	55	55	53	37
Philippines	60	57	56	25
Indonesia	67	67	64	49

Source: UNIDO. World Industry Report 2003. Geneva.

CHAPTER 3
TRADE, INVESTMENT POLICY AND ECONOMIC INTEGRATION

This chapter discusses the Indonesia's trade and investment policy, as well as its trade liberalisation steps. The participation of Indonesia in multilateral agreements is also briefly discussed.

Introduction

Within the last three decades along with its changing development strategy, Indonesia's trade and investment policies have also undergone significant changes. During the oil boom in the early 1970s, the government embraced an inward looking import-substitution strategy. In the early 1980s Indonesia took up a strategy of limited liberalisation and deregulation. After the oil boom in the mid 1980s the government adopted more extensive deregulation and liberalization.

In 1985 Indonesia began to diversify its economic base away from oil and gas and advocated significant deregulation efforts. During the 1985-1990 period, tariffs were rationalized and reduced across the board. Some non-tariff barriers (NTBs) were removed, especially import licensing and import monopolies (Pangestu, 1996). Such reforms brought positive impacts that were demonstrated in rapid growth of non-oil and gas exports, diversification of Indonesia's export base, and inflows of export-oriented domestic and foreign investments. Unskilled labour-intensive sector in which Indonesia has comparative advantage had also shown some growth.

Along with the change of government and the global situation, the government of Indonesia conducted reforms and deregulations. As stated in the 1999-2004 State Policy Guidelines *(GBHN)*, one of Indonesia's economic development strategies pertaining to industry, trade and investment is geared towards the promotion of global competitiveness by providing access to employment and business opportunities in all regions. The Government is committed to further liberalise trade which is expected will promote further economic development and which in its turn will provide better resources for alleviating poverty. The role envisioned for trade policy is to enhance opportunity, community empowerment, and capacity building focussing on small and medium enterprises.

To promote global competitiveness, five major strategies have been adopted, namely, the development of exports; enhancement industrial competitive advantage; promoting tourism; strengthening market institutions; and improvement of science and technology capabilities (Bank of Indonesia, 2003).

3.1. Investment Policy[8]

As a response to the plummeting foreign direct investment, particularly after the financial crisis, Indonesia promptly introduced measures to liberalize investment. Such liberalization includes allowing foreign firms to operate retail outlets, the distribution and banking sectors, and shortening the negative list of activities closed to foreign investment.[9] Since then, Indonesia has maintained a relatively open investment regime, and has introduced measures to streamline the investment approval procedure and to facilitate foreign investment.[10] The Investment Coordinating Board (*BKPM)* is responsible for promoting and approving both domestic and foreign non-oil and gas investment (apart from banking and insurance).[11]

8 This part is mainly taken from the Indonesian Trade Policy Review (1998 and 2003).

9 WTO (1999).

10 U.S. Embassy Jakarta (2001a).

11 According to the Presidential Decree No. 03/2001) the BKPM is no longer merged with the State Minister for Investment.

A new draft investment law, to replace the 1967 legislation, was released in October 2000, and was to be submitted to Parliament in February 2003.[12]

Impressive reversal of Indonesia's foreign investment policy was reflected in the approval of one hundred percent foreign ownership under the June 1994 investment deregulation package as well as the lifting of the mandatory divestment rule to minority ownership. This made Indonesia's foreign investment policy more liberal than that of the other East Asian countries.

The declining investment, particularly after 1997, has been one of the multidimensional challenges faced by Indonesia. Restoring investor confidence particularly in key sectors is a major challenge for Indonesia. Recently a National Investment Team was established to help improve the investment climate. Apart from that, the government approved a "one-stop one-roof" investment facility in the *BKPM* to simplify the process of investment approval and in implementing plans.

Investment policy in Indonesia is extremely open to foreign investment access. Such openness is manifested in the restriction of limited number of sectors, no limitation on the amount of investment, the availability of fiscal incentives to attract foreign investors, the possibility for foreign investors to wholly own their investment in almost all sectors and simplified investment approval process. The number of sectors closed to FDI has been steadily reduced until at present only confined to a small number of activities.[13] Investment liberalization approach seems to arise from the fact that investment is one of the most important factors in driving economic growth. Therefore, improving investment procedures is critical in order to stimulate a more favourable investment climate.

Although not on the negative list, some sectors remain reserved for small-scale enterprises, and their coverage has been extended (covering activities in the exotic chicken, marine & fishery, forestry, energy & mineral mining, industrial & trading, transportation, telecommunications,[14] and health sectors).[15] Large-scale domestic or foreign investors are permitted only in partnership with a small local business or cooperative.[16] This is due to the fact that small-scale business has a strategic position. Its potential and role are very much acknowledged in national development. Other measures in facilitating foreign investment include giving authority to Indonesia's embassies to approve applications for new FDI in Indonesia.

Indonesia is committed to strengthen trade and business laws and regulations in order to improve the business environment and encourage competition, efficiency, and good corporate governance. Relevant laws and regulations have either been revised or introduced in many key areas. These included the prohibition of monopolistic practices[17], fiscal incentives such as reduction of luxury taxes, income tax, and value-added tax for certain commodities to cut production costs,[18] financial services, especially banking. In addition to these, currently a new investment bill is being drafted and expected to be issued soon, which is intended to attract more investment into the country.[19]

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12 The draft law, inter alia, replaces investor approval with registration, allows for wholly foreign-owned enterprises to invest in most sectors, and full national treatment of foreign investors, whenever possible.

13 See Annex 7 on the limitation of foreign investments access

14 This covers telecommunication outlets, internet outlets and cable installation at houses and buildings.

15 See Attachment 1 of the Presidential Decree No. 127 0f 2001

16 The Presidential Decree No. 99 of 1998 on small-scale enterprises, amended by the Presidential Decree No. 127 of 2001 (issued on 14 December 2001).

17 Act No.5 of 1999.

18 This fiscal stimulus was issued by the Ministry of Finance in January 2003.

19 Key points of the bill are (1). Equal treatment of all investors, domestic and foreign (2). Investment is open to any field/location, except for investors on "negative list" (3). Investors are not required to divest stakes to local partners or nationalize shares (4). Free repatriation of foreign investment capital/returns, and a reasonable portion of salaries/wages of expatriate employees (5). Foreign investment licenses to be given according to economic life of the project (6). Investment system may be simplified to allow foreign investors' access to local financing. (7). Govt to promote beneficial partnership between large foreign and local firms, and small/medium business, and (8). Regional govt to establish, operate a "one-stop" investment service for foreign and domestic investors .

3.2. Multilateral and Regional Cooperation

The increase of regional fora in the late 1980s and early 1990s had at least provided Indonesia with external pressure for liberalization. Such a move became more intense particularly after the financial crisis. Moreover, under the Uruguay Round Agreement and the World Trade Organization (WTO) the government is committed to comply with WTO rules and regulations. In some cases Indonesia has even unilaterally liberalized beyond the multilateral obligations. This is in line with a high trade policy priority to expand and diversify exports.

Indonesia considers that global benefits of trade liberalization would be more equitably distributed if "special and differential" treatment were extended to developing countries, including in agriculture, to accommodate their non-trade concerns, such as rural development, poverty alleviation, and food security. It supports the extension of services negotiations without *a priori* sector exclusions, provided that developing countries are allowed to open fewer sectors and transactions, and the inclusion of emergency safeguard measures.

Uruguay Round and World Trade Organization

Indonesia is an active WTO member. One important characteristic of the WTO agreement that is expected to benefit Indonesia is the elimination of bilateral quotas under the MFA (Multi Fibre Arrangement). Under the Uruguay Round all bilateral import quotas on textiles and garments are to be removed by 2005, and the only trade restrictions in place will be bound to tariffs. Since Indonesia is an important textile and clothing exporter, it could be a major beneficiary of the elimination of the MFA. However, some predict that the elimination of MFA will increase joblessness in Indonesia.[20]

An important characteristic of the Uruguay Round agreement is its progressive agricultural liberalization. Recently the government has announced the July policy package. This package came out after the September 2003 Cancún Ministerial Conference that had ended in a deadlock. WTO members in Geneva began efforts to put the negotiations and the rest of the work programme back on track. Work intensified in the first half of 2004, with the new target date of reaching agreement on a package of framework agreements by the end of July, in effect Friday 30 July. The first draft of the "July package" was circulated on 16 July, and members started negotiating intensively in various formats in the fortnight beginning 19 July.[21] There are different views regarding this package. On the one hand, the Indonesian government considers this package would benefit the nation and other developing countries substantially. On the other hand, this package is seen as a Pandora box with most likely unexpected adverse impacts to the country.[22]

Indonesia's commitments to the WTO can be summarized within six major areas. **The first** is the binding of a majority of tariffs across-the-board at the ceiling rate of 40 percent. These bindings cover 95 percent of all tariff items and 92 percent of all imports. **The second area** is the agriculture sector, with tariffication and binding of all agricultural items, and a reduction in tariffs of at least 10 percent per line item, or about 24 percent overall, over the 10 years from 1994. **The third area** is the commitment to remove non-tariff-barriers (NTBs), such as various import licensing schemes, over the 10 years from 1994. **The fourth area** is the elimination of all import surcharges on items included in Indonesia's market access over the 10 years from 1994. **The fifth area** is the commitment to liberalize, or to the binding of existing market access opportunities, for five services sectors, namely telecommunications, industrial services, tourism, financial services and banking. **The sixth area** is the commitment to remove local content regulations under the TRIMS (Trade Related Investment Measures), with the local content requirements for motor vehicles and agricultural products being notified in 1995 and removed by the end of 2000 (WTO, 2004).

20 Further discussion on this issue is in Chapter 5.

21 See website www.wto.org

22 KOMPAS 26 August 2004. "WTO July Package, Pandora Box for Developing Countries" (Paket Juli WTO, Kotak Pandora bagi Negara Berkembang). Jakarta, page 15

The introduction of a controversial national car policy in 1996 which restored the requirement for certain local content elements along with other policies appeared to violate the clause on the MFN and national treatment under the GATT rules and put the government in a dilemma. In June 1999 the government delivered major trade liberalization with regard to this most protected sector, motor vehicles that comprised removal of local content requirements, reduction of tariffs on imported cars and components, and simplification of licensing procedures. The reforms were aimed at developing an efficient and globally competitive motor vehicle sector.

Indonesia's unilateral investment and trade reforms in 1994 reflected in dramatic liberalization of foreign ownership restrictions and divestment requirements appeared to be more influenced by Indonesia's external commitments. This stemmed from the fact that in 1994 Indonesia was hosting the APEC meeting. In May 1995 a comprehensive program of tariff reductions (64 percent of tariff lines) was announced, and for the first time, contained a schedule for tariff reduction for the 1995-2003 period. By 2003, the government announced that all tariffs, except those on motor vehicle components and products, would be set at a maximum of 10 percent, with most falling in the 0-5 per cent range. This stated schedule was influenced by the AFTA schedule that the government had to prepare, although tariffs for intra ASEAN trade under AFTA were falling to a lower target rate of 0-5 percent. This was followed by another trade liberalization package in 1996, bringing down the average unweighted tariffs to 12 percent, and non-tariff barriers to around 3 percent of tariff lines and 12 percent of imports.

Other international trade agreements, many of which are more progressive than the Uruguay Round in terms of eliminating barriers on non-agricultural products, often exclude commitments for agricultural liberalization. Therefore, the success of the Uruguay Round in including agriculture in its agreement has become the primary source of efficiency gains from this sector. Prior to this agreement, trading economies could impose inefficient and costly barriers since the sector was not regulated under GATT or the WTO rules.

Asia Pacific Economic Cooperation (APEC).

APEC was created in 1989 in order to bring the countries of the Western Pacific closer to the Eastern Pacific region.[23] The objectives of APEC's liberalization are based on the key Bogor General Principles of comprehensiveness, WTO consistency, and non-discrimination (or open regionalism), whereby liberalization should not discriminate between APEC economies, nor between them and non-APEC countries. The main drive for APEC came in 1993, with the first Leaders Meeting in Seattle providing a vision of free trade and investment in the region. Indonesia hosted the APEC meeting in 1994, contributing to the APEC process by setting the long-term goal of free and open trade and investment in the Asia Pacific region by 2010 for developed economies and 2020 for developing members. APEC is supported by the three pillars namely, trade and investment liberalization (TILF), trade and investment facilitation, and economic and technical cooperation (ECOTECH).

The adoption of APEC was a major breakthrough for Indonesia and other APEC members. The APEC process did not employ the preferential regional liberalization path, instead envisaged a process of *'unilateral concerted liberalization'*. This means that members voluntarily undertake unilateral liberalization toward all countries, not just APEC members (i.e on a Most Favoured Nation basis).[24] The APEC process obviously had an influence on the trade and investment liberalization that Indonesia had embarked on in 1994 and again in 1995.

Indonesia plans to implement the APEC's voluntary target, set in the *Bogor Declaration* in 1994, of open and free trade including in services and investment for developing country members by 2020.

23 APEC currently consists of: Australia; Brunei Darussalam; Canada; Chile; China; Chinese Taipei; Hong Kong, China; Indonesia; Japan; South Korea; Malaysia; Mexico; New Zealand; Papua New Guinea; Peru; Philippines; Russia; Singapore; Thailand; the United States; and Viet Nam.

24 APEC contributes to the process through confidence building and peer pressure on all members to act similarly. The process relies on there being 'champions' who voluntarily undertake these unilateral liberalization efforts, and often the economy hosting the APEC meeting will take on the champion role.

APEC economies are to achieve their targets using Individual Action Plans *(IAPs)*. In its IAPs Indonesia indicated that tariff reductions would be continuously implemented in the near future so that rates would range between zero and 10 percent by 2003; export restrictions would be further eliminated and reduced export taxes would be scheduled.[25] However, many APEC economies, including ASEAN members, have either formed or are considering regional trading arrangements that discriminate against other APEC and non-APEC economies. APEC has strengthened its peer review process to examine more rigorously the progress of APEC economies in achieving their free and open trade and investment targets.[26] Indonesia's review is scheduled for 2005.

ASEAN[27] and AFTA

The Association of Southeast Asian Nations (ASEAN) was established in 1967. However, it was not until January 1992 that its members agreed to the formation of an ASEAN Free Trade Area (AFTA). As ASEAN member countries are different with regard to size, historical background, as well as level of industrialization and development (Ariff 1995), on the one hand the expansion of ASEAN will create trade and economic activities, on the other hand new members might have difficulty adjusting and might delay the onset of free flowing resources within ASEAN (Nattapong Thongpakde, 2001).

For the six original members, through AFTA, tariffs are to be reduced on intra-ASEAN trade (with at least 40 percent ASEAN content) under the Common Effective Preferential Tariff (CEPT) to a maximum 5 percent by the end of 2002, or by the end of 2003 on a few products.[28] At the end of 2003, the Inclusion List of tariff items covered by the CEPT represented, on average, 90 percent of the tariff lines of all ASEAN member nations (99 percent for original members).[29] Ninety-six percent of total tariff items covered by the CEPT in 2002 for original members had maximum tariffs of 5 percent **(Table 3.1.)**. The average CEPT tariff on all members was 2.7 percent in 2003 (down from 5.4 percent in 1998).[30]

Products may be excluded from the CEPT scheme as either temporary or general exclusions, or as sensitive products.[31] Products temporarily excluded (i.e. placed on the Temporary Exclusion List/TEL) were to be included in CEPT in equal instalments over five years, since 1 January 1996 so they have more time to adjust to tariff reduction. Under a new Protocol that was agreed in October 2000, the six original founding members may request temporary delay of CEPT tariff liberalization for products that were in the TEL as of 31 December 1999.[32] Members are expected to agree on compensation to other ASEAN partners.[33] At the end of 2003, TEL products accounted for at the average of 0.5 percent of ASEAN tariff lines for original members, namely Brunei, Indonesia, Malaysia, Singapore, and Thailand, although Malaysia was the only one has TEL products **(Table 3.2.).** General exceptions apply to products deemed necessary to protect national security, public morals, human, animal or plant life and health, articles of artistic, historic, or archaeological value; these cover about one percent of ASEAN tariff lines by 2003.

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25 APEC, 2002a.

26 APEC, 2002b.

27 The old members of ASEAN namely Brunei, Indonesia, the Philippines, Malaysia, Thailand, and Singapore is referred to as ASEAN-6. "ASEAN-5" is the same group, excluding Brunei. The term "new members" refers to Vietnam, Lao PDR, Myanmar, and Cambodia. Cambodia attained observer status and is expected to be a member soon. The term "ASEAN-10" is loosely used to include the present members and Cambodia.

28 Originally, CEPT was to achieved by 2008, then it was accelerated for the original members to 2003 and subsequently to 2002 for most products following the financial crisis. Longer periods were provided for new ASEAN members namely 2006 for Viet Nam; 2008 for Laos and Myanmar; and 2010 for Cambodia.

29 The share for the four new members was 72%.

30 Average tariffs ranged from zero for Singapore to 5% for Laos (ASEAN Secretariat).

31 A small number of sensitive agricultural products will be allowed until 2010 to be integrated into the CEPT scheme. In an agreement yet to be fully finalized, tariff reductions on these products will begin between 2000 and 2005, depending on the country and the product.

32 The Protocol covers the delayed transfer of products from TEL into CEPT and suspension of concessions on the last tranche of TEL manufactured products at 31 December 1999 (or other relevant dates for new members), where such liberalization would "cause real problems, by reasons not covered by emergency measures" (Article 1). Delays or suspensions may be reviewed annually by the AFTA Council, Article 8 (see ASEAN, 2000).

33 Compensatory adjustment measures are to "ensure a general level of reciprocal and mutually advantageous concessions not less favourable to trade than that provided for and prevailing" beforehand, and must be applied on an MFN basis to all ASEAN members (Articles 3 and 5).

Indonesia seemed to be progressing to transfer additional products to the CEPT scheme. By the end of 2002, only 0.1 percent of Indonesian tariff lines were not covered, with tariff rates of 5 percent or above. At the end of 2001 Indonesia's CEPT tariffs averaged 4.6 percent, went down from 7.04 percent in 1998, and fell to 3.7 percent in 2003. By the end of 2001, Indonesia had 21 tariff items subject to temporary exclusions and another four items were excluded as sensitive products. By 2003 Indonesia has had no either TEL or Sensitive List products.

Indonesia's regional trade liberalization is mainly to the ASEAN Free-Trade Area (AFTA). Through ASEAN, Indonesia is actively pursuing greater regional trade links. These include the establishment of an ASEAN-China Free Trade Area within ten years[34] and the formation of an East Asia Free-Trade Area between ASEAN members, China, Japan, and Korea (ASEAN +3). Indonesia expects that such an FTA would increase intra-regional trade and investment, lift up economic efficiency and economies of scale, lead to greater business opportunities, and enlarge economic cooperation.

Originally, 15 commodity groups were chosen to be on the fast track for tariff reduction, 8 including sensitive agricultural commodities such as vegetable oils. Under the fast track, products with tariffs greater than 20 percent have their tariffs immediately reduced to 20 percent and to 0–5 percent within 10 years. Fast track products with tariffs at 20 percent or below have their tariffs reduced to 0–5 percent within seven years. The number of tariff posts may be seen in **Table 3.1 and Table 3.2.**

To qualify for the CEPT (Common Effective Preferential Tariff) scheme, one of the criteria is that the goods fulfil a 40 percent ASEAN content requirement. At the beginning of the AFTA agreement, the timetable for tariff reduction was 15 years; it was shortened to 10 years in the Fifth Meeting of the AFTA Council in 1994. The meeting also admitted unprocessed agricultural products into the CEPT scheme. Under the present scheme, fast-track tariff reductions will be completed by the year 2000 and normal-track tariff reductions will be finished in 2003. AFTA allows sensitive items to be excluded from these two tracks. There is also a permanent exclusion list for sensitive products **(ASEAN Secretariat 1995).**

Other agreements intended to promote intra-ASEAN trade and investment as well as greater regional integration include the ASEAN Industrial Cooperation Scheme (AICO) and the ASEAN Investment Area (AIA). Signed in 1996, the AICO encourages technology-based investments in ASEAN, and any ASEAN-based company meeting certain conditions is eligible.[35] AICO-approved products, raw materials, and intermediate inputs are immediately subject to no more than 5 percent tariffs, and eligible for local-content accreditation and non-tariff incentives.[36] The AIA, signed in October 1998, means to increase foreign investment from ASEAN and non-ASEAN regional sources by removing barriers to all ASEAN investors by 2010 and for all investors by 2020.[37]

ASEAN countries are also negotiating intra-regional services liberalization (the 1995 ASEAN Framework Agreement on trade in services/AFAS).[38] ASEAN members are increasingly pursuing bilateral cooperation

34 The Report of the ASEAN–China Expert Group on Economic Co-operation, considered at the ASEAN Leaders Summit (Bandar Seri Begawan, 5-6 November 2001), estimated that an ASEAN-China FTA could increase ASEAN's exports to China by 48 percent and China's exports to ASEAN by 55 percent, and boost GDPs by 0.9 percent and 0.3 percent respectively.

35 It must be incorporated in and operating in an ASEAN country; having a minimum 30 percent ASEAN equity; and being engaged in some type of resource sharing (e.g. sharing of technology, market sharing, or consolidated purchases of raw materials). At least two companies in two ASEAN countries must participate. The conditions, particularly the 30 percent ASEAN equity requirement, may be waived under certain circumstances. At April 2002, there were 90 approved AICO ventures, with an annual transaction value of US$1.09 billion.

36 Non-tariff incentives are to be determined individually by each country, and are yet to be specified.

37 It is based on opening all industries to foreign investment, and phasing out exclusions according to schedules; immediate national treatment for ASEAN investors, with few exceptions; eliminating investment impediments; streamlining investment process and procedures; enhancing transparency; and undertaking investment facilitation measures.

38 Three packages of commitments from two rounds of negotiations have liberalized trade in air transport, business services, construction, financial services, maritime transport, telecommunications, and tourism. A third round of negotiations was launched in September 2001, to begin in 2002 and end in 2004, covering all specified sectors and modes of supply. Members agreed in 2001 to accelerate services liberalization and to negotiate mutual recognition arrangements for professional services.

with non-member states, and other regional inter-governmental organizations.[39] The ASEAN plus 3 members (China, Japan, and the Republic of Korea) agreed in November 2002 to study and formulate options to gradually establish an East Asia Free Trade Area[40]. Indonesia observes an opportunity to increase the level of cooperation and to further expand trade and investment flows among the countries of East Asia. In December 1997 the ASEAN Vision 2020 was issued to commit the region towards closer cohesion and economic integration by, among other measures, fully implementing the ASEAN Free Trade Area and accelerating the liberalization of trade in services. Further in 1998, the implementation of AFTA was accelerated from 2003 to 2002 with some flexibility for the original six members of ASEAN targeting of 100 percent of the tariff lines at 0-5 percent duty rates by 2003.

The result of the Bali Summit of October 2003 was the declaration of ASEAN Economic Community (AEC), as one of the three pillars of a broader ASEAN community. The other two pillars are the ASEAN Security Community and the ASEAN Socio-Cultural Community. This is the realization of the end-goal of economic integration as outlined in the ASEAN Vision 2020. It is characterized as a single market and production base, with free flow of goods, services, investment and skilled labour, and freer flow of capital by 2020 (Reyes, 2004). It also stated the acceleration of regional integration in 11 priority sectors as recommended by a High Level Task Force (HLTF) on ASEAN Economic Integration. At the ASEAN Economic Ministers (AEM) Retreat on April 21 in Singapore, the Ministers set 2010 as the ultimate deadline for economic integration in those sectors.

In September 2004 the 10 economic ministers of ASEAN member nations were expected to strengthen their commitment to push for the liberalization of trade and investment activities in 11 key economic sectors by 2007.[41] Opening up of the 11 sectors is expected to boost trade within the region. As mentioned earlier, ASEAN members have agreed to liberalize the 11 sectors by 2007 for the six founding member countries, and 2012 for the newer members in an attempt to boost trade and investment within the region. Under this liberalization plan, each country has a quota to exclude no more than 641 groups of goods, or 15 percent of the total tariff categories in the 11 priority sectors. This temporary exclusion will expire in 2010. There are a total of 4,273 tariff categories traded in the 11 priority sectors. The tariff groupings are based on the eight digit tariff categories of the ASEAN Harmonized Tariff Nomenclature (AHTN). The Indonesian government has submitted the proposed negative list to the ASEAN Secretariat (Table 3.3.).

Despite the start of a gradual implementation of the ASEAN Free Trade Area in 1992, intraregional trade so far accounts for only about 23 percent of the region's total foreign trade. In comparison, intraregional trade within the European Union was around 75 percent, while the figure for the MERCOSUR region was 35 percent last year.[42] Agreement was reached that roadmaps are to be prepared by countries nominated to coordinate accelerated integration in the designated sectors. Indonesia is designated for Wood-Based Products and Automotives; Malaysia for Rubber-Based Products and Textiles and Apparels; Myanmar for Agro-Based Products and Fisheries; Philippines for Electronics; Singapore for Information and Communications Technology (e-ASEAN) and Health Care; and Thailand for Air Travel and Tourism.

It is interesting to note that based on their study, Feridhanusetyawan and Pangestu (undated) concluded that the full implementation of the Uruguay Round and APEC would greatly benefit Indonesia. The study also showed that the benefit from having unilateral liberalization, in addition to the Uruguay Round commitment, would lead to large welfare gains. On the other hand, the creation of AFTA is expected to contribute only a little additional welfare gain to Indonesia or to the other ASEAN member countries. Therefore, participating in trade agreements whether it is preferential, regional or multilateral, should be taken up with consolidated efforts. This is to ensure that the country could reap the benefits of free trade while preventing the adverse impacts that might go with it.

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39 These include the Andean Council, the Australia–New Zealand Closer Economic Relations (CER), the Economic Cooperation Organization, the Gulf Cooperation Council, MERCOSUR, the Rio Group, the South Asian Association for Regional Cooperation, and the South Pacific Forum. Most ASEAN members are also active participants in the activities of the Asia-Pacific Economic Cooperation (APEC) forum, the Asia-Europe Meeting (ASEM), and the East Asia-Latin America Forum (EALAF).

40 ASEAN, 2002.

41 See the Jakarta Post 01 September 2004 on "ASEAN to open up 11 'priority sectors'

42 Jakarta Post, 1 September 2004

Table 3.1.
Post Tariffs 0-5 and >5 percent within the CEPT-AFTA 2002 by Country

Country	No. of Tariff Post			Percentage		
	0-5%	>5%	Total	0-5%	>5%	Total
Brunei	6,260	16	6,276	99.75	0.25	100.00
Indonesia	7,139	67	7,206	99.07	0.93	100.00
Malaysia	9,127	914	10,041	90.90	9.10	100.00
Philippines	5,371	205	5,576	96.32	3.68	100.00
Singapore	5,859	0	5,859	100.00	0.00	100.00
Thailand	8,747	457	9,204	95.03	4.97	100.00
ASEAN-6	42,503	1,659	44,162	96.24	3.76	100.00
Cambodia	238	2,877	3,115	7.64	92.36	100.00
Lao PDR	1,295	803	2,098	61.73	38.27	100.00
Myanmar	2,850	730	3,580	79.61	20.39	100.00
Vietnam	3,623	1,936	5,559	65.17	34.83	100.00
ASEAN-4	8,006	6,346	14,352	55.78	44.22	100.00
TOTAL ASEAN	50,509	8,005	58,514	86.32	13.68	100.00

Source: Ministry of Industry and Trade.

Table 3.2.
Number of Tariff Posts within CEPT PACKAGE 2003 by Category and Country

Country	No. of Tariff Posts					Percentage				
	IL	TEL	GE	SL	TOTAL	IL	TEL	GE	SL	TOTAL
Brunei	6337	0	155	0	6492	97.61	0.00	2.39	0.00	100.00
Indonesia	7217	0	68	0	7285	99.07	0.00	0.93	0.00	100.00
Malaysia	10124	218	53	0	10395	97.39	2.10	0.51	0.00	100.00
Philippines	5642	0	16	0	5658	99.72	0.00	0.28	0.00	100.00
Singapore	5859	0	0	0	5859	100.00	0.00	0.00	0.00	100.00
Thailand	9211	0	0	0	9211	100.00	0.00	0.00	0.00	100.00
ASEAN 6	**44390**	**218**	**292**	**0**	**44900**	98.86	0.49	0.65	0.00	100.00
Cambodya	3115	3523	134	50	6822	45.66	51.64	1.96	0.73	100.00
Lao PDR	2533	856	74	88	3551	71.33	24.11	2.08	2.48	100.00
Myanmar	4182	1224	48	18	5472	76.43	22.37	0.88	0.33	100.00
Vietnam	6296	0	139	51	6486	97.07	0.00	2.14	0.79	100.00
ASEAN 4	**16126**	**5603**	**395**	**207**	**22331**	72.21	25.09	1.77	0.93	100.00
ASEAN 10	**60516**	**5821**	**687**	**207**	**67231**	90.01	8.66	1.02	0.31	100.00

Note:
IL = Inclusion List ; TEL = Temporary Exclusion List;
GE = General Exclusion; SL = Special List

Source: Ministry of Industry and Trade

Table 3.3.
Indonesia's *"negative list"* in 11 priority sectors

Sectors Negative List	Tariff Posts
Electronics	38
Fisheries	6
Agro-based	18
Healthcare	5
Rubber-based	58
Textiles	11
Automotive	505
Total	641

Source: Ministry of Trade

CHAPTER 4
SOCIAL IMPLICATIONS OF FREE TRADE

There have been a number of debates regarding social impacts of trade liberalization. Yet, Ghose (2000) contends that the feared and apprehended effects of trade liberalization are unfounded. Meanwhile, Feridhanusetyawan (1998) had estimated the impact of international trade liberalisation on changes in welfare, sectoral outputs, and employment patterns in ASEAN by using a global computable general equilibrium model. The results show that countries which participate in regional trade liberalisation, such as APEC and AFTA, will obtain additional benefit from the liberalisation. However, without any participation in the multilateral trade liberalisation, such as the WTO, the gain will be minimal. By participating in the WTO and APEC liberalisation, the total welfare of ASEAN countries will increase by US $3.9 billion. Given that ASEAN countries are participating in the WTO and APEC, the implementation of AFTA will create minimal additional benefit by around US$242 million in total. The opening of AFTA to the MFN basis, however, will increase welfare significantly.

This chapter seeks to draw social implications of free trade on employment and labour. Such effects might be viewed in terms of employment magnitude and structure, labour wage and social security as well as labour mobility. As the traded goods and the sectors selected for the case study are manufactured goods, it is worthwhile to first look at the employment specifically in the manufacturing sector before looking at other issues.

4.1. Employment

Since the 1980s Indonesia has embarked on an industrialisation strategy, aimed at boosting employment in the manufacturing and modern sectors. However, Indonesia's employment structure, until now, suggests that the bulk of the labour force has remained in the agricultural sector. The previous Table 2.2. depicts a shift in the GDP structure, yet up to the present, agriculture is still the largest employer in Indonesia (Chart 4.1.). In 1990 the agricultural sector in Indonesia provided 50 percent of the total employment. Since then, although declining, the percentage of agricultural employment has remained high. After the financial crisis, the percentage of the labour force engaged in agricultural employment seemed to have slightly increased. For example, in 1998 agriculture was the largest employer with a 45 percent share of employment; another 19 percent were employed in trade, hotel and restaurants; 14 percent in public services and 11.3 percent in manufacturing. Since the crisis, the percentage of the labour force working in the non-agricultural sector seemed to have fluctuated. Only agricultural employment demonstrated a steady increase, with its employment share of 46.3 percent in 2003. Such fluctuation reflects that employment in the formal sector has been very tight (Chart 4.1.).

Manufacturing Employment[43,44]

Manufacturing sectors in ASEAN countries including Indonesia are expected to benefit from trade liberalisation. It is likely that the expansion of manufacturing sectors will lead to increased labour demand. Indonesia as a labour abundant country will benefit from the development of labour intensive industries. Other ASEAN countries, especially Malaysia and Thailand, will likely be relying more on capital-intensive industries.

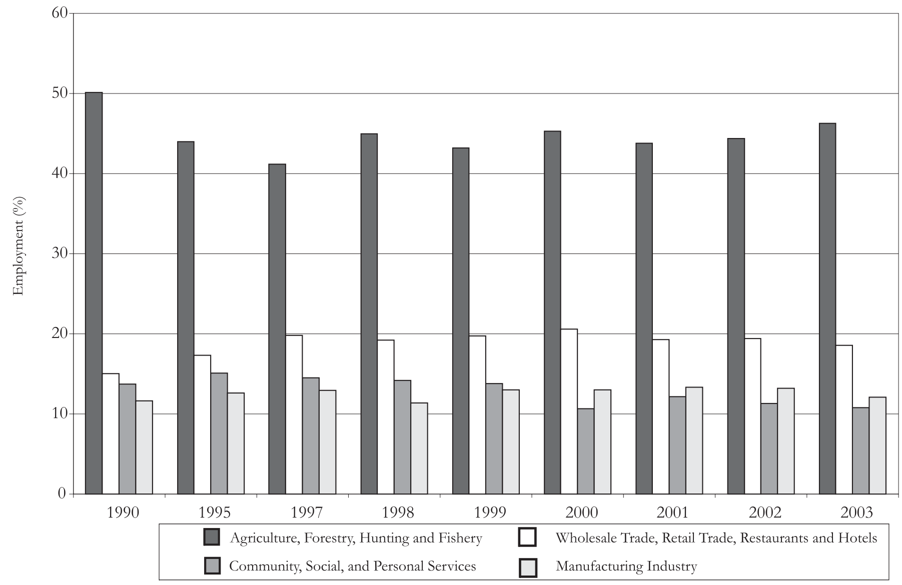
43 This part relies heavily on Shafiq Dhanani (2001)

44 Manufacturing enterprise in Indonesia may be divided into household and small-scale, medium-scale and large-scale industries

In the 1990-2003 period, there had been a fluctuating trend in Indonesian employment, including in the manufacturing sector **(Chart 4.1.)**. For example, in the period of 1997 to 1998, manufacturing employment declined by 1.0 million workers, from 11 million to 9.9 million workers. In 1999 it regained its employment absorption capacity, even surpassed the 1996 level. According to **Dhanani (2001)** practically all the increase in the manufacturing employment in 1998 to 1999 occurred in household and small-scale establishments. During the recovery period of 1999-2000 the employment expansion in the manufacturing sector was very small, 0.14 million. He further showed that although the total manufacturing employment in 2000 did not show a decrease, female employment fell from 5 million to 4.9 million.

The role of household and small industries in employment provision is very significant. It was noted that in the first instance of the crisis the medium- and large scale manufacturing enterprises felt the impact of the crisis almost immediately. Women working in large scale manufacturing enterprises experienced more job losses than those of men.

Chart 4.1. Percentage Distribution f Employment in Selected Sectors, Indonesia 1990-2003



Source: CBS, Statistics of Indonesia, various publications

The decline of manufacturing employment was noted during 2002-2003. Such decline was likely due to the slowing down of some top manufacturing industries, namely the footwear, and furniture as well as other non-mining industries. Unfavourable labour regulations, which have forced companies to rapidly increase the minimum wage at a time when both exports and domestic sales are weak has caused some firms to leave the country or reduce their staff . Some observers notice that the minimum wage increase has been too fast. For example, the capital city of Jakarta was one of the provinces that experienced the large increases of minimum wages in 2002. The Jakarta's minimum wage increased by 38 percent, coming on top of a 49 percent increase in nominal wages in the previous years (Sumhudi, 2002).

Informal Sector

The informal sector plays an important role in the Indonesian economy, in the sense that this sector has created significant employment opportunities. The percentage of people working in the informal sector is relatively high, around 70 per cent. As work status is commonly used as proxy for informal sector in Indonesia, this figure would also include the agricultural sector. The magnitude of the sector usually fluctuates in line with the economic condition, expanding when it gets worse. With the worsening economic condition, particularly noted during the financial crisis, substantial number of people sought employment in the informal sector. It is also a fact that social protection for workers in this sector is still far from the desired level. Therefore, it is thus important that the adoption of trade liberalization policy should take into account social protection of vulnerable workers.

4.2. Real Earnings

As a means of social protection, the Indonesian government has set up the minimum wage policy, that since the implementation of regional autonomy is to be determined by regional governments. The Indonesia minimum wage has been increasing over the years. For instance in Jakarta, the monthly minimum wage was Rp 231,000 in 1999, increased to Rp 591,266 in 2002, and to Rp 631,000 in 2003.[45] Many employers still pay workers below the minimum wage and many workers still work more than the recommended seven hours a day and six days a week.

The minimum wage has been a controversial issue, particularly since the financial crisis. The debate is due to the fact that some findings revealed that the increasing minimum wage has caused declines in formal employment (see studies among others by Rama, 1996; SMERU, 2001). Some observers notice that the minimum wage increase has been too fast. The SMERU study (2003), for example, revealed that every one percent increase in minimum wage causes unemployment to increase by 0.16 percent. The increase of female unemployment is 0.33 percent for every one percent increase of minimum wage. The similar increase of 0.33 percent unemployment rate is also demonstrated by less educated workers.[46] Interestingly, a one percent increase in minimum wage has caused a one percent decline in unemployment of white collar workers.

Minimum wages have been an element in the Indonesian labour policy since the 1970s, but only really began to affect wages in the early to mid 1990s (Manning, 2003). Initially the determination of minimum wage was centralized (with inputs from the provinces). After decentralization, the minimum wage setting was devolved to the regions. Labour-intensive producers such as those in the textile and textile products (TTP) sector fear that local leaders, keen to shore up short run political support, will raise minimum wages with little regard for the competitiveness of local firms, and for the broader regional and national economic interests. Recent increases in minimum wages have been particularly burdensome for the TTP industry.

Observers agree that the important variable missing from the minimum wage setting in Indonesia is productivity. Most TTP producers interviewed said that they would be happy to pay higher salaries if such salary increases could be justified by productivity improvements.

Since decentralization that formally commenced at the beginning of 2001, the obligation of paying local levies and charges has increased substantially. Supported by the enactment of the decentralization laws (Act No. 22 of 1999 and Act No. 25 of 1999), as well as the amendment of the Act No.18 of 1997 on local taxes and charges to become Act No.34 of 2000, local governments throughout the country have been issuing many new regulations designed primarily to raise locally sourced revenues.

The increasing minimum wage was also expressed in real earnings. During the period of 1994 to 1997 real earning for both men and women increased **(Table 4.1.)**. Women's real earnings although getting better, were lower than those of males. Women only received 69 percent of males' earning in 1998, which increased from 64 percent in 1994. In 2003 earning differentials by gender were narrowed, women received 72 percent of those of males' earning. Rural wages were lower than those of urban. In general after the financial crisis, real earnings have slumped. Real earnings recovered in the following two years, but they were still 12 per cent lower than before the crisis, and lower than in 1994.

The majority of people in Indonesia are working in the informal type of employment. Thus this group is not likely to be protected by the minimum wage policy. In addition, this group would likely be implicated

45 The inflation rates in 1999, 2002 and 2003 were 56.20, 11.6 and down to 6.3 percent respectively.

46 Less educated workers are those having junior secondary education or below.

by trade and investment policy. During the crisis, for instance, poverty incidence increased from 18 to 24 percent between 1996 and 1999 although real earnings grew by 10 and 15 per cent in 1996-97 and 1998-99. To shield the vulnerable population from the adverse impact of the financial crisis, the government had implemented a nation-wide social safety net programme, including the provision of subsidized rice targeted at the poorest 10 million out of some 40 million total families across the country, the provision of basic education scholarships and free medical cards in mid-1998. When converted into cash equivalent, the rice subsidy program and the scholarship program represented a significant share of a poor household's income (Dhanani and Islam, 2000).

If we assume that the period of the 1990s was the beginning of free trade, then its social implications have been mixed. There had been improvements but also negative effects. Unfortunately it is very hard to dispel the social impacts of the financial crisis that had very adversely affected Indonesia.

4.3. Labour Migration

International movement of people represents only a small fraction of the world population. There was an estimate that the supply of Asian workers overseas to be around 11 million in the 1990s **(Hugo and Stahl, 1997)**. While possibly small in terms of world population, the increase in labour migration is still phenomenal by regional standards especially in the last decade. Official figures for Indonesia for instance showed that in 1995 there were 120,603 Indonesian working overseas, increased to 339,200 workers in 2001, indicating an increase of 180 percent within 6 years **(Table 4.2.).** Yet, there have been many Indonesian working overseas illegally. For example, according to the Minister of Manpower and Transmigration, Jacob Nuwa Wea, that even though Indonesia had no labour export arrangements with Syria, some 8,000 Indonesians were working illegally in that country.[47]

The most popular destination for Indonesian workers remained the Asia Pacific, which in 2001 took up the bulk of 64 per cent, while another 36 per cent were taken by the Middle Eastern countries **(Table 4.2.)**. In both the Asia Pacific and the Middle Eastern regions, the percentage of women workers was generally higher than those of men. Thus, Indonesian labour mobility has been characterized by increasing international migration of women. Gender has certainly become a significant dimension of international migration in ASEAN, especially for Indonesia.

Overseas workers' remittance has been important revenue to the country, and interestingly, in 2001 the revenue obtained from workers employed in informal type of jobs was greater than those of formal jobs **(Table 4.3.)**. Given the magnitude and characteristics of particularly female workers, the protection of women under some of the existing laws should be grounds for concern. This is particularly crucial as Indonesian women workers unfortunately have been concentrated in the informal type of employment as household servants, employed mainly in the Middle East. Eighty-two percent (2003) of Indonesian workers in the Middle East were women who worked in Saudi Arabia as domestic helpers (MOMT, 2003). Working overseas particularly in informal types in some cases brings adverse consequence. There have been some abuses towards Indonesian workers particularly women.[48]

People moving within ASEAN generally is not meant to become permanent settlers. These movements have often been explained among others in terms of push and pull factors (economic, social and political), increasing integration of ASEAN economies and the emergence of a regional labour market. The concern with socioeconomic and political implications of this phenomenal increase in intra-ASEAN labour movements is

47 See Indonesia: 8,000 Indonesians work illegally in Syria (http://www.asianlabour.org/archives/cat_indonesia.html March 02, 2004), visited on 23 August 2004 May 22, 2004) March 02, 2004

48 Reports on physical abuses including sexual abuses by their employers were noted. For example, the story of Nirmala Bonat, an Indonesian maid whose Malaysian employer repeatedly burnt her with an iron and scalded her with boiling water, has received global attention (see http://www.asianlabour.org/archives/cat_indonesia.html visited on 23 August 2004 May 22, 2004) on "Malaysia: Maid abuse case shocks". The government of Indonesia represented by the Minister of Manpower and Transmigration has made a talk with the Malaysia's government to push for the signing of a bilateral agreement on protection of Indonesians working in the informal sector in that country (see Indonesia: Govt to push Malaysia on worker protection (May 27, 2004) see http://www.asianlabour.org/archives/cat_indonesia.html visited on 23 August 2004).

however recent, more so after the onset of the crisis. If on the one hand, the Indonesian workers going overseas have been on the rise.[49] On the other hand, the number of foreign workers entering Indonesia has been declining. Such decline was most likely due to the slowing down of economic activity in the country in line with the declining foreign investment inflows. The decline of foreign workers in Indonesia occurred across all sectors during the 1997 to 2000, although after that an increase has been observed **(Table 4.4.)**.

The pattern of Indonesian international labour migration reflects labour surplus of mainly unskilled labour force. The Indonesian government has acknowledged that overseas employment is one of the ways of overcoming unemployment problem that has been increasing over time. The employment of workers coming from labour surplus countries has been to fulfil the labour needs due to labour shortages experienced by the more developed high-growth labour importing countries. The need for this particular type of workers has been observed in the case of Japan, Singapore, South Korea, Taiwan and Malaysia. Certain jobs in plantation estates or domestic works are the biggest sources of employment for Indonesian workers. The demand for workers in these countries is generally for such sectors as manufacturing, construction, plantation, services, and domestics helpers. The nature of the majority of work in all these sectors can be described by secondary labour market employment. With trade liberalization it is expected that people mobility including workers would become more intense. However, since receiving countries have their own regulations, the migration of unskilled labour to these countries have frequently been done illegally. The case of substantial number of illegal Indonesian workers in Malaysia, has become a recurrent problem.

4.4. Social Security

Like many other developing countries, Indonesia's labour force is characterized by the substantial portion of informal employment. In fact, those employed in the formal economy in Indonesia represents around 30 percent of the labour force. As the coverage of workers' social security (under the JAMSOSTEK system) is only for those in the formal employment, the group that is eligible for this scheme is very small. Data from JAMSOSTEK reveals that only 25 percent, or 23 million, of almost 90 million workers have been registered as members of social security programs. Although by law firms are supposed to register their workers with the JAMSOSTEK, the number the compliance rate is still very low. Meanwhile, the majority, including the unemployed and those in the informal sector, remain unprotected. Although small, the number of firms registered for JAMSOSTEK has increased during 1981-2002 **(Chart 4.2.)**.

Although most Indonesian workers, both at home and overseas, remain unprotected, but the government is still lack of willingness and capability to provide them with the needed insurance coverage. This is obvious from the weak enforcement of Law No. 3/1992 on national social security (JAMSOSTEK), which requires employers, foundations and other organizations to pay premiums for their employees into the insurance scheme. Another problem that could cause many Indonesian migrant workers overseas have not been provided necessary protection is that because are employed abroad illegally.[50] There is a customary misperception that the social security law applies only to workers employed in industrial enterprises. In reality, the programs are compulsory for all companies, businesses, organizations and institutions employing at least 10 workers, or those firms paying Rp 1 million (US$120) or more in total salaries to their workers. However, several companies and organizations had failed to enrol their employees in social security programs either due to financial constraints or the employees refuse to take part in the schemes. Meanwhile some firms, foundations or organizations had enrolled only a small percentage of their employees in the social security scheme and did not report the true amount of their workers' gross monthly salaries. This move is to avoid paying higher premiums set between 4 to 7 percent of the workers' insurance premiums to be paid by their employers.[51] The ILO under the project on "Restructuring the Social Security System in Indonesia" in 2001 has attempted to come up with some recommendations

49 Such ups and downs was particularly brought about by the social problems arouse in the destination countries, such as Malaysia and Taiwan. Some records on the deportation of Indonesia workers in large scale from Malaysia show that a big portion of them were deported because they entered Malaysia as illegal workers.

50 The Jakarta Post, 18 May 2004: "Most workers still lack insurance"

Chart 4.2. JAMSOSTEK Membership by Number of Firms and Workers, Indonesia, 1981-2002

Source: PT Jamsostek

for extending the coverage of social protection to the excluded groups. The government has recently issued the Bill on *National Social Security System* (SJSN) despite the strong opposition from employers and workers.

4.5. Workers Safety

The influx of foreign investments undeniably has, to a certain extent, come with infringements of labour standards and regulations in the recipient country. Investments in the manufacturing sector, in many cases are represented in factory jobs. It is therefore relevant that the manufacturing industry is frequently associated with work accidents. The number of accidents that has been recorded by JAMSOSTEK has been on the rise. The fatalities, however were slightly declining. It should be kept in mind that this figure does not include all employed people. Data from JAMSOSTEK shows the number of occupational accidents in the country rising slightly to 105,846 in 2003, from 103,804 in 2002. Despite the decline in the number of fatalities at the workplace from 1,903 in 2002 to 1,748 in 2003, the number of workers who were either permanently or temporarily disabled by occupational accidents increased from 101,901 in 2002 to 104,098 in 2003 (**Table 4.5.**). JAMSOSTEK records also reveal that most workers employed on construction projects or chemical factories do not use proper safety equipment.

As a result of the relatively high incidence of Indonesia's occupational accidents, the world economic forum held by the International Labour Organization (ILO) in Switzerland, has ranked Indonesia's safety standards as the second worst in the world after Russia.

Unfortunately the data do not reveal those occupational accidents by scale of establishment or type of ownership, so it is not known which types of firms have higher occupational accidents. It should be noted that of 170,000 companies or industries in the country, SMEs account for 91.53 percent. For this reason, the government will require small and medium enterprises (SMEs) to implement the occupational safety and health program (OSH) in their companies in a bid to curb the number of workplace accidents. Such a regulation is urgent as Indonesia is still ranked among countries with the worst occupational safety records. The government is currently working on a draft of the regulation and preparing guidelines for its implementation.

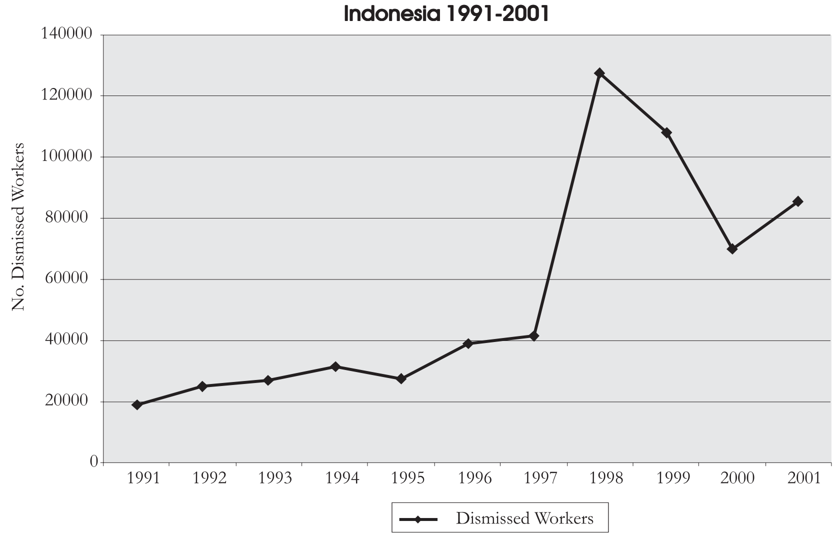
51 The program cover by JAMSOSTEK are occupational accident, health care, bereavement and pension programs. Besides, in cooperation with state and private hospitals, JAMSOSTEK has established 26 trauma centres to minimize the impact of occupational accidents and fatalities in industrial zones across the country.

4.6. Industrial Relation

The globalisation process and Indonesia's openness have to a large extent contributed to the promotion of labour standards in the country. In fact, Indonesia is one of a few countries in Asia that has ratified all the core labour standards.[52] The most significant change was the ratification of the freedom of association. If in the past, during the New Order regime, there was only one labour union that was very much government sponsored, as of May 2004, the number of union federations is 86 at the national level and at least 3 (three) confederations have been formed. The three confederations are, the *KSPSI* (Confederation of All Indonesian Worker's Union), the *KSPI* (Congress of Indonesian Trade Unions) and the *KSBSI* (Confederation of Indonesian Prosperous Worker's Union). If in the past the problem is lack of democratization, with the current5 big number of trade unions, the problem has shifted to the difficulty to select the right representative at the tripartite level. Naturally, the pattern of representative of unions at the tripartite institutions has to be modified and proportionally have to adopt the existing membership of unionism. According to the latest verification of union membership, there are approximately 2.2 million members, around 7.3 percent of the total number of 30 million formal workers in Indonesia.

During the 1990s the number of cases regarding workers' strikes had been on the rise. Consequently the number of workers involved was also mounting causing increasing loss of working hours **(Table 4.6.).** Along with the strikes, dismissals were also noted. The official data recorded that labour dismissal was four times higher in 1998 compared to the previous year **(Chart 4.3.)**. Those strikes occurred in the early 2000s were mainly in the manufacturing sector, and to a small extent in services sector. Manufacturing workers strikes amounted to more than three quarters of the total recorded strikes **(Table 4.7).**

Chart 4.3. Cases on Dismissal and Number of Official Dismissed Workers, Indonesia 1991-2001



Source: Ministry of Manpower and Transmigration

Although Indonesia has already ratified 26 of 165 ILO Conventions, including eight conventions on core labour standards, the worst forms of labour law violations are still occurring in Indonesia. For example, there are 2.5 million child labourers, mostly employed in fishery establishments which are underpaid and work and live in an extremely bad living conditions along the North Sumatra coastline. Therefore, violation of workers' basic rights on salaries, working hours, break times, allowances and social security are still rampant that was mainly as a result of ineffective and weak labour inspections.[53]

52 There are 8 core labor standards covering rights of workers, etc.

53 One of the likely reasons for the ineffective labour inspections is the shortage of labour inspectors. An interview with the MOMT Director General for labour relations reveals that the central government currently has only 650 labour inspectors to check up on more than 176,700 companies, meaning that each inspector, on average, must monitor 220 companies. Ideally, it should have a 1:50 ratio to be effective. Likewise, in 2000 there were 1,500 certified mediators but currently their number is 800, consequently many labour disputes cannot be settled in a tripartite forum because of the shortages of mediators.

Analysing the effects of free trade on labour standards is difficult, the effects may somewhat be reflected in the trends in employment and wages as these may be considered as good indicators for overall labour standards.

The recent trend that has been occurring in Indonesia is that companies, in order to cut costs, are adopting more flexible production methods of employment. These include the use of subcontracting to small workshops, or switching the workforce from permanent to short-term contracts, with a heavy toll in terms of anxiety and insecurity. This outsourcing method, which is permitted according to the new Manpower Act No. 13 of 2003, has distressed labours as their employment tenure become more insecure. Labour activist expressed their opinion that the government should abolish the implementation of worker recruitment through outsourcing system because it has exploited and worsened workers' condition. Trade unions in the country have generally rejected the outsourcing system because it has caused the workers to have no protection for their basic rights at their working places. The rejection of this outsourcing system in recruitment is due to the fact that the employment security of workers that are already employed will be threatened, as the more the companies use outsourcing system, the less number of the permanent workers would be employed. In addition to that, with no permanency in employment it is rather difficult for workers to form workers union. As outsourcing is a way to employ many migrant workers, if it is banned then it would also affect migrant workers employment opportunities.

Adding to this, the poor implementation of regional autonomy has also contributed to widespread labour abuse. With the decentralization of the labour inspection authority to regions, the Ministry of Manpower and Transmigration can no longer monitor inspections, while almost 60 percent or 900 of 1,500 registered labour inspectors have been transferred to other jobs outside their expertise. Making it worse, 89 regencies and municipalities in Indonesia have no labour inspectors at all.

4.7. Gender

There are many problems confronting women as workers, problems their male counterparts do not necessarily face. The fact that women workers have to play a dual role as home maker as well as worker have also brought discriminatory consequences.

As reported, wages levels in the manufacturing industry in Indonesia, especially in the textile, garment and footwear industries are the lowest in South East Asia. They are even lower than in China. Arguably they must be the lowest in the world.[54] Regarding women working in factory jobs in Indonesia the Global Alliance for Workers and Communities reported grim picture.[55]

Women faced considerable discrimination at the workplace, both in terms of obtaining positions and in gaining fair compensation for labour performed. During the year, the International Labour Organisation (ILO) Jakarta office, reported that on average, women in the workforce earned 68 percent of that of male workers. There were reports that female university graduates received an average salary that was 25 percent less than their male colleagues. In 2002, the Government stated that 38 percent of civil servants were women, but that only 14 percent of these women held positions of authority.

Women are more likely to be employed than men on a casual or contract basis. The contract or labour hire systems allow employers to pay workers lower wages than permanent employees, though they perform the same tasks and work the same hours. Contract or daily hire workers enjoy no job security or trade union rights, so the injustice of wage discrimination is compounded by constant fear of retrenchment or reduced hours during periods of 'downsizing'. Although several women trade union

54 From "Women workers in Indonesia: Not mere victims of exploitation but also agents of social change" (Jean Duval,March 5th, 2001). Based on the data from Stratfor, 15/12/2000 in 'Asia's Coming Textile Boom' it showed that the labour costs in the clothing industry in 1998 expressed in dollars per hour, including benefits, the rate in Mexico was 1,51 US$, Guatemala 1,28 US$, China 0,43 US$ and Indonesia is at the bottom with a rate of 0,16 US$

55 From "Women workers in Indonesia: Not mere victims of exploitation but also agents of social change" (Jean Duval,March 5th, 2001).

activists have become rallying points for Indonesian workers, progress on equality for women in the workplace in general and in the trade union movement in has been slow (Sarah Gardner in Inside Indonesia).[56]

Some activists said that in manufacturing, employers relegated women to lower-paying, lower-level jobs. Many female factory workers were hired as day labourers instead of as full-time permanent employees, and companies were not required to provide benefits, such as maternity leave, to day labourers. According to the Government's Central Statistics Bureau, in May 2002, the unemployment rate for men was higher than that for women. If a husband and wife both work for a government agency, the couple's head-of-household allowance is given to the husband. (February 27, 2004 Indonesia: US Department of State's *Country Reports on Human Rights Practices* www.asianlabour.org)

Discrimination in access to employment, training and promotion are also common. The Swiss-based multinational Nestlé stopped hiring women in Indonesia several years ago, to avoid discharging their obligations regarding paid maternity leave. On the other hand, women at hand-rolled cigarette factories, such as PT Gudang Garam in Kediri, are specifically hired for their 'quick, nimble fingers' and neat work, yet they are not considered for positions above cigarette roller. Women are also disadvantaged as a result of definitions contained in Indonesian legislation. The law defines women workers as single; the underlying assumption being that married women do not work and that the husband is the primary income earner. This definition causes women workers and their families financial harm — the tax rates are higher for single workers, and women miss out on access to family health benefits provided by employers. This definition also ensures that women's work continues to be undervalued, both legally and culturally.

Table 4.1. Real Earnings by Sex and Residence, Indonesia 1994–2003
(Rp. 000s per month, 1996 prices)

Sex & Residence	Year							
	1994	1996	1997	1998	2000	2001	2002	2003
Both sexes	185	207	228	147	171	200	214	216
Males	208	231	252	164	190	224	235	236
Females	134	154	173	113	133	152	169	171
Ratio F/M	0.64	0.67	0.69	0.69	0.70	0.68	0.72	0.72
Urban	229	248	273	171	195	228	247	251
Males	258	276	305	191	216	255	n.a	n.a
Females	167	187	207	133	155	175	n.a	n.a
Ratio F/M	0.65	0.68	0.68	0.70	0.72	0.69	n.a	n.a
Rural	142	162	176	119	140	159	165	164
Males	161	182	196	134	157	180	n.a	n.a
Females	96	114	130	85	103	115	n.a	n.a
Ratio F/M	0.60	0.63	0.66	0.63	0.66	0.64	n.a	n.a

Source: CBS

1. Total manufacturing employment: *Labour force Situation in Indonesia* (*SAKERNAS* survey)
2. Medium and large-scale industries: *Large and Medium Industrial Statistics*, CBS, various years
3. Household and small-scale establishments: the difference between *SAKERNAS* and medium and large-scale establishments.

Note:
1. 1996-98 working age was aged 10+, 1999-2000 was aged 15+
2. In absence of data on self-employment and employers, assume all medium and large-scale manufacturing employment (less unpaid family workers) is employees.
3. ' – ' Not available.

56 Indonesia: Women in trade unions, see http://www.asianlabour.org/archives/cat_indonesia.html on December 11, 2003) visited on 23 August 2004)

Table 4.2. Indonesian Overseas Workers by Destination, 1995-2003

Country & Year	Males %	Females %	%	Total
Asia Pacific				
1995	42.53	57.47	100.00	68,436
1996	31.02	68.98	100.00	95,070
1997	57.69	42.31	100.00	375,317
1998	29.34	70.66	100.00	182,574
1999	38.90	61.10	100.00	267,803
2000	38.32	61.68	100.00	325,894
2001	25.75	74.25	100.00	217,555
2002	41.10	58.90	100.00	238,324
2003	58.31	41.69	100.00	106,722
America				
1995	99.66	0.34	100.00	3,483
1996	100.00	0.00	100.00	1,761
1997	100.00	0.00	100.00	736
1998	99.92	0.08	100.00	2,448
1999	99.60	0.40	100.00	3,519
2000	99.93	0.07	100.00	1,509
2001	98.68	1.32	100.00	228
2002	82.50	17.50	100.00	40
2003	84.21	15.79	100.00	171
Middle East & Africa				
1995	11.58	88.42	100.00	47,524
1996	6.08	93.92	100.00	122,564
1997	6.95	93.05	100.00	126,347
1998	7.57	92.43	100.00	193,937
1999	10.06	89.94	100.00	154,636
2000	8.69	91.31	100.00	130,114
2001	8.65	91.35	100.00	121,388
2002	7.76	92.24	100.00	241,961
2003	7.90	92.10	100.00	183,770
Europe				
1995	99.83	0.17	100.00	1,160
1996	96.35	3.65	100.00	767
1997	99.83	0.17	100.00	577
1998	98.93	1.07	100.00	1,214
1999	96.64	3.36	100.00	1,696
2000	89.42	10.58	100.00	359
2001	82.76	17.24	100.00	29
2002	51.47	48.53	100.00	68
2003	48.39	51.61	100.00	31
Total				
1995	32.53	67.47	100.00	120,603
1996	17.91	82.09	100.00	220,162
1997	45.06	54.94	100.00	502,977
1998	18.91	81.09	100.00	380,173
1999	29.20	70.80	100.00	427,654
2000	30.14	69.86	100.00	457,876
2001	19.69	80.31	100.00	339,200
2002	24.31	75.69	100.00	480,393
2003	27.20	72.80	100.00	293,694

Source: MOMT.

Table 4.3.: Revenue of Overseas Workers by Type of Employment, Indonesia 2001

Region/Country	Formal Number	Formal Devisa (US$)	Informal Number	Informal Devisa (US$)
Asia Pacific				
Malaysia	65,867	56,939,783	44,623	4,408,579
Singapore	3,397	4,228,690	30,898	44,349,129
Brunei Daruss.	4,819	8,646,128	954	1,956,163
Hongkong			23,929	77,702,806
Taiwan	1,760	6,479,698	36,359	144,568,795
Middle East				
Saudi Arabia	244	322,364	102,991	155,506,411
Uni Emirat Arab	10	11,444	11,017	14,435,313
Kuwait	7	8,011	3,336	4,350,082
Bahrain			1,558	2,445,253
Qatar	1	1,373	1,028	1,613,428
Oman	-		554	869,493
Jordan	-		379	682,200
Egypt	-		1	3,840
Nigeria	-		8	92,160
Cyprus	-		22	253,440
Turkey	-	221,760	24	23,040
America				
USA	138	927,360	-	
Rep. Palau	90	604,800	-	
Europe				
Netherlands	19	127,680	-	
England	1	6,720	-	
Austria	9	60,480	-	
Total	**81,305**	**84,394,645**	**257,681**	**453,260,132**

Source : Ministry of Manpower and Transmigration, Directorate General of Overseas Employment.

Table 4.4. Foreign Workers in Indonesia by Industry, 1997-2002

Economic Sector	1997	1998	1999	2000	2001	2002
Agriculture	1,431	1,221	871	680	1,014	842
Mining and Mineral Resources	2,997	3,537	2,020	1,765	3,749	4,554
Manufacturing	19,574	17,485	18,758	4,374	4,553	11,331
Electricity, Water and Gas	332	357	95	56	108	116
Construction	3,086	2,878	1,149	1,205	2,089	2,027
Trade	4,049	3,612	3,260	3,444	5,938	0
Transportation	590	518	455	494	882	1,118
Finance	1,045	920	694	548	982	1,045
Services	4,088	2,696	1,706	2,146	5,004	4,680
Total	37,192	33,224	29,008	14,712	24,319	25,713

Table 4.5. Number of Occupational Accidents in Indonesia, 1999-2003

Year	Fatality	Permanent Disability	Temporary Disability	Total	% Fatality
1999	1,476	11,871	78,163	91,510	1.61
2000	1,592	12,025	85,285	98,902	1.61
2001	1,768	12,566	90,440	104,774	1.69
2002	1,903	10,345	91,556	103,804	1.83
2003	1,748	10,395	93,703	105,846	1.65

Source: The Jakarta Post of 08 May 2004 on "SMEs required to apply health and safety program" *originated from PT JAMSOSTEK.*

Table 4.6. Number of Strikes, Involved Workers and Loss of Working Hours, Indonesia 1981-2001

Year	Case	Number of Involved Workers	Loss of Working Hours
1980	100	32,287	328,466
1981	200	54,875	495,144
1982	142	49,525	501,236
1983	96	23,318	295,749
1984	63	10,836	62,906
1985	78	21,148	55,001
1986	75	16,831	117,643
1987	35	8,281	35,664
1988	39	7,544	607,265
1989	19	1,168	29,257
1990	61	27,839	229,959
1991	130	64,474	534,610
1992	251	176,005	1,019,654
1993	185	103,490	966,931
1994	278	136,699	1,226,940
1995	276	128,855	1,300,001
1996	350	209,257	2,796,488
1997	161	100,440	875,512
1998	234	141,495	1,375,654
1999	125	48,232	915,105
2000	273	126,045	1,281,242
2001	174	109,845	1,165,032

Source: Ministry of Manpower and Transmigration

Table 4.7. Labour Strikes by Industrial Sector, Indonesia 2003

Industrial Sector	2001	2002	2003
Plantation	6	3	1
Mining	2	0	2
Manufacturing	118	163	112
Construction	1	2	0
Electricity, Gas and Water	2	0	0
Trade, and Banking	6	0	0
Transportation	2	0	0
Services	28	52	31
Shoes/Sandals	9	0	0
Others	0	0	0
Total	**174**	**220**	**146**

Source : Ministry of Manpower and Transmigration, DG Industrial Relations (Data January to November 2003)

CHAPTER 5

CASE STUDY: GARMENT, TRANSPORT EQUIPMENT AND WOOD FURNITURE

The chapter focuses on three selected industries, namely garments, transport equipment and wood furniture. The discussion will cover its economic value as well as employment aspects. The latter covers working conditions, social security, and other labour issues.

5.1. Garment Industry[57]

The garment industry is one of the branches under the textiles, garments and leather sector (ISIC 32) that has remained as one the most important manufacturing activities in Indonesia, based on its contribution on industry's value added and employment absorption. The Indonesian textile industry is an old industry. It goes back to the late colonial period in the 1920s, when the weaving industry had started to flourish.[58] The favorable investment climate during the New Order government had resulted in the rapid expansion of modern spinning and weaving industries from the early 1970s. The growth of the modern textile industry nevertheless has caused the displacement of the unprotected small-scale, hand loom sub-sector (Hill, 1983). Over the course of industrial development, the share of weaving's value added declined while that of garments grew rapidly.

Table 5.1. , shows that the role of garment in value added contribution had been relatively important over time. Similarly, in employment terms, the garment industry acts as the largest employer in the TTP (Textiles & Textile Products) industry.

Table 5.1. Percentage Share of Value Added and Employment in TTP, 1990-2000

		Value Added (% of total manufacturing)			Employment (% of total manufacturing)		
		1990	1995	2000	1990	1995	2000
35133	Fiber	0,7	0,5	1,1	0,2	0,1	0,1
32111	Yarn	3,3	5,0	3,8	3,5	3,4	4,1
32114	Fabric	3,9	4,1	2,7	6,9	6,5	4,4
32115	Finishing	0,2	0,4	0,5	0,5	0,6	0,9
32121	Finished Textile Goods	0,2	0,2	0,3	0,7	0,6	1,0
32130	Knitting	0,8	0,7	0,5	1,7	2,1	1,4
32210	Garment	3,3	3,2	3,6	9,0	8,4	10,6
	Total	12.40	14.10	12.50	22.50	21.70	22.50

Source: Aswicahyono and Imelda Maidir, 2003.

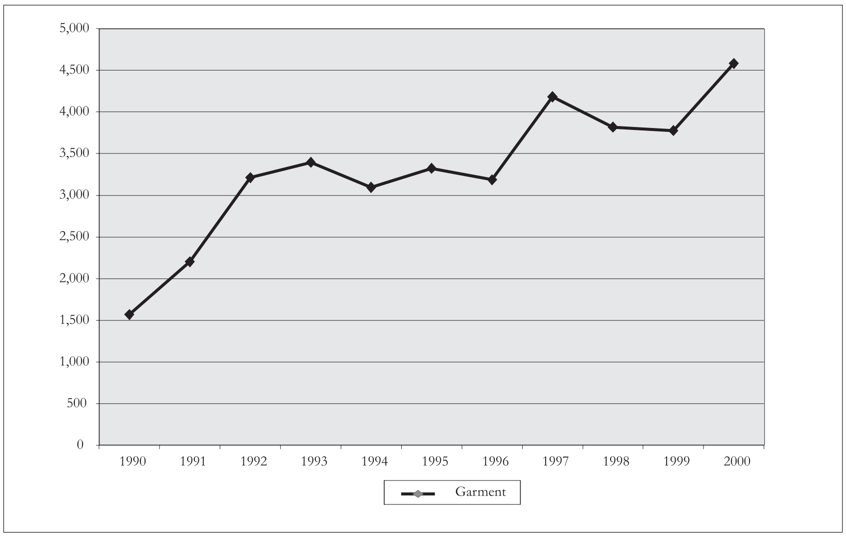
Rapid growth of the garment industry was due to increasing demand in the domestic market in the late 1970s and growing opportunities in the export market in the early 1980s. The change of strategy to export orientation in the early 1980s was caused by slow domestic demand after the end of the oil boom, the comparative advantage of low labor costs, unutilized export quotas, attractive incentives such as the built-in subsidy in the export certificate scheme *(subsidi ekspor)*, subsidized interest rates for

57 This part relies heavily on Aswicahyono and Maidir (2003)

58 During that period, the industry was a local cottage-based handloom weaving industry and was almost entirely dependent on imported yarn.

export credits, and an under-valued real exchange rate (Pangestu, 1996). Despite the fact that textile and garments are Indonesia's leading manufacturing export, the rapid growth of garment industries was halted in 1993.[59] During 1990 up to 1992 there was a rapid increase in garment exports. A sharp increase occurred again just before the financial crisis, restoring its power again after the 1999.**(Chart 5.1.). T**he share of garment products, reached almost 12 percent of total manufacturing exports in 2001 **(Table 2.7. of Chapter 2).**

Chart 5.1. Export of Garments, Indonesia, 1990-2000



Source: CBS, Industrial Statistics.

Employment

In line with the increase in its value added, the garment sector accounted for an increasing share of total employment, overtaking weaving as the larger employer. Even during the crisis, employment in large and medium garment industry remained to increase. The industrial statistics show that large and medium garment firms absorbed around 18.2 thousand workers in 1996 or roughly around one percent of total manufacturing employment in 1996. In 2000 the large and medium manufacturing establishments absorbed around 458 thousand workers but then it declined to 435 thousand in 2002. It was impressive, an increase of almost 25 times within 4 years **(Table 5.2.).** As expected, the garment industry employs more women than men especially in production. In 1996 around 89 percent of those employed in production comprise female workers, that slightly declined after the crisis, to 78 percent in 1998. Then it increased again to 81 percent in 2000 and remained stagnant in 2001. Meanwhile, the number of non-production workers was relatively small, only 3.8 percent of the 1996 total workers, increased to 8.5 percent in 1998, and to 9.5 percent in 2002. The wages of production workers were far less than of other groups of workers, although the discrepancy has been narrowing. In 1996 the wages of non-production workers were almost six times higher than those of production workers. In 2002 they were only twice as much **(Table 5.2.)**.

Home-based subcontracting arrangements in the garment industry, where part of the production process is subcontracted to home workers, appear to be widespread-phenomena in Indonesia. Some studies illustrate the existence of traditional forms of indirect subcontracting, particularly in rural areas where several villages undertake specialized tasks under the direction of an intermediary recruited for this purpose by export firms (Barme, 2000:39). The garment sector is clearly very important for women livelihood.

Based on the latest IO table (1995), which includes small firms, it was estimated that around 2 million people in Indonesia were employed in the textile and garment industry. This amounted to around 2 percent of the total labour force (Aswicahyono and Maidir, 2003).

59 Pangestu (1997) provides explanations for the sluggish growth such as firstly, intense competition emerged from other low wage countries, such as China, India and Bangladesh. Second, there was a reduction in Indonesia's relative competitiveness as a result of the government's minimum wage policy, the increases of which have not been matched by increased labour productivity.

Table 5.2. Employment in Large and Medium Garment Industry, Indonesia, 1996-2002

No. of Production Workers	1996	1998	2000	2002
Males	1,908	65,308	80,893	76,458
Females	15,708	233,505	338,074	317,591
Total	17,616	298,813	418,967	394,049
No. of Other Workers				
Males	364	13,487	18,329	18,301
Females	327	14,337	20,236	22,958
Total	691	27,824	38,565	41,259
Monthly Wages (Rp '000)				
Production Workers	150.98	232.94	386.82	586.41
Other Workers	872.69	500.36	1150.68	1200.67
	5.8	2.1	3.0	2.0

Source: CBS, Industrial Statistics

Competitiveness[60]

The declining trend of textile and garment industries competitiveness partly was justified by lack of new investments that began in 1992. Some possible explanation are offered such as, firstly several large textile and garment industries, instead of investing their windfall profits during textiles and garments boom, expanding horizontally outside their core business and venture into sector not related to textile and garment industries (Aswicahyono and Maidir, 2003). Secondly, in early 1990s Indonesia may already near to the quota limits. Thirdly, competition came from major players in the textile and garment industry, such as China, Pakistan, Sri Lanka, Bangladesh and Vietnam. Empirical studies have shown that the concentration ratio of the textile and garment industry in the world has declined considerably during the period. Fourthly, the textile and garments industry, especially the lower more labor intensive industries, were "squeezed" by increased minimum wage on the one hand, and by declining international price on the other hand.

The textile and garment industry is facing tougher competition. This is particularly true as the global textile quota system as required by the WTO will be terminated in early 2005. Such a quota system in fact has benefited Indonesian textile and apparel producers for years. The reason is with the quota system less efficient producers could still export their products to the US without fear of being sidelined by more efficient competitors as long as they had a quota. Worries now exist that many local firms would face more difficulties in competing with more efficient producers especially from China. This is because local firms are struggling with rising labour costs and has yet to replace old plant and machinery.[61] The Indonesian Ministry of Industry and Trade says that the country's textiles sector requires a minimum of US$505 million in order to improve its production facilities.[62] The textile and garment companies in Indonesia have suffered various problems including aging machinery, huge debt load, and lingering labour conflict. Such problems explain why the utilization of the export quotas at one stage has been low. The average utilization rate of the quota for the US market until the seventh month of 2004 stood at a simply 28 percent.[63]

60 The discussion in this part involves textile in general, which is due to data unavailability and the issue of Multi Fibre Agreement covers textile in general.

61 See the Jakarta Post July 31, 2004 and 16 August 2004 "Textile center exports training skills"

62 A recent survey on the industry carried out by the technical advisory service of PT SUCOFINDO found that almost 20 per cent of 4,109 companies surveyed needed to invest in new technology if they were to stay in business, the remaining 80 per cent of companies surveyed claimed their machinery was up-to-date or less than 10 years old. The survey was carried out in response to the once-thriving industry's decline in the face of increased competition from countries such as China. SUCOFINDO's findings also revealed that of the 774 manufacturers requiring investment, 703 are garment makers, 36 are textile producers, and 35 are connected with finishing, spinning, dyeing weaving, printing, and knitting. See BKPM website on "INDONESIA: Industry Needs US$505m Investment" – Report of 24 August 2004 (visited on 25 august 2004)

63 The Indonesian Garment Producers Association (APGI) has urged the government to redistribute the quota to other companies in a bid to push export.

According to the Indonesia business community (2003) at least 67 textile companies recently have had to stop operations in the West Java capital of *Bandung* due to drastic decreases in orders and rising operational costs; the closures had forced out of work around 10,000 workers.[64] Textile producers have painted a grim picture of the outlook for the country's textile industry for this year, predicting the closure of dozens of factories leading to a reduction of national output by around 20 percent. The gloomy picture of this textile industry may be noted from these excerpt (See following Box)

Box 5.1
Indonesian Textile Industry

- The slump will result in massive job losses, with a senior official of the Indonesian Textile Association (API) predicting 50,000 job losses in West Java alone.
- Apart from West Java, the other major textile center in the country is Central Java.
- Lili Asdjudiredja, chairman of API's West Java chapter, told The Jakarta Post that around 20 percent to 30 percent of the total textile factories in the industry might choose to close down in 2004 due to an inability to face cutthroat competition in local and international markets from producers from other countries.
- According to Lili Asdjudiredja around 121 members of the association had reported closures in the past four years. Taking into account businesses that were non-members or failed to report to API, the actual figure might be higher.
- Local producers have complained that their costs have increased over the past few years due to the increase in minimum wages and the introduction of new regional and national taxes, as well as rising electricity and fuel costs.
- consequently, many foreign operated factories have chosen to relocate production activities to neighbouring countries.

Source: Sandy Darmosumarto, "Textile Industry to Lose More Workers", the Jakarta Post, 03 January 2004.

The chairman of the Indonesia Textile Association, Benny Sutrisno, states that as many as 400,000 workers will lose their jobs, which is bound to occur with the abolition of the quota system. The inability to compete with cheap imports is also experienced by developed countries, such as Australia.[65] The Indonesian government has proposed that the quota system to the US for Textiles and Textile Products be extended for five years (KOMPAS, 19 August 2004). However, such proposal would be difficult to be realized as there might be resistance from other WTO member countries.

Despite the fact that textile and textile product exports value has been declining[66], the Indonesian Textile Association (*Asosiasi Pertekstilan Indonesia/API*) has optimistically targeted a 4 percent share of the world textile and textile product market in the five years of the post quota period (KOMPAS, 26 August 2004). In 2002 the Indonesian TTP only contributed 2 percent of the world TTP output. To achieve their goal of increasing production, some improvements have been made by investing in new machinery. [67]

64 See Indonesia: 67 textile plants close (http://www.asianlabour.org/archives/cat_indonesia.html December 13, 2003) visited on 23 August 2004.

65 See BKPM website from just-style.com of august 20, 2004 visited on 25 August 2004 on "AUSTRALIA: Fletcher Jones to Close Factories", 60 workers will lose their jobs when clothing retailer Fletcher Jones closes its Australian manufacturing division. The company is to shut its Mount Gambier and Warrnambool factories, citing loss of business due to cheap imports as the reason behind the decision, the manufacturing work was likely to move towards Indonesia and China. With the removal of quotas and tariffs, imported garments have become cheaper and cheaper. The Textile, Clothing and Footwear Union has criticised the decision, saying the company didn't work hard enough to prevent closure becoming necessary.

66 According to the Central Board of Statistics, in 2000 it exported US$ 8.2 Billion, it came down to US$ 7.65 billion in 2001, further down to US$ 6.86 billion in 2002 and in 2003 it rose slightly to US$ 7 milyar (KOMPAS, 19 August 2004).

67 KOMPAS 10 September 2004 on « Industri TPT Mulai Investasi Mesin »

The forthcoming termination of the MFA in January 2005 has raised concerns among Indonesian textile producers, who have been struggling to restructure a huge debt burden and aging machinery. They may not be able to compete with Chinese producers that are able to produce much cheaper products. According to the Indonesian Textile Association (API), Indonesia's market share in the U.S. may be reduced to 2 percent from the current 4 percent, while the share of China may triple to 53 percent from 16 percent. Local textile and apparel producers have urged the government to provide incentives and delay the rise in minimum labour wages to help them survive in the main export market.

There have been rising calls for the WTO to delay the termination of the current quota system. The Washington Times reported that the U.S. textile industry, being apprehensive about the flood of cheap Chinese imports when the quota system expires, has been leading an international effort to persuade the WTO to approve a three-year extension of the quota system.[68] The end of worldwide quota is expected to cost 30 million jobs in the United States, Europe and a slew of developing countries, according to industry groups. Some 81 textile and apparel associations from more than 30 countries have also requested for an extension of the quota system until 2007.[69]

Mr. Gusmardi, the present Indonesian Ambassador for WTO, predicted that with the termination of quota system by January 1, 2005, all countries would attempt to protect their industries by applying a variety of measures as long as not violating the WTO regulations. Such attempts for instance may be in the implementation of prohibitive regulation for TTP such as anti dumping claims, environmental issues and safeguard mechanism.

The Way Forward

If the MFA is to end by early 2005, one can anticipate the social implications. Efforts should be made to resolve this forthcoming problem. Clearly boosting the industry's competitiveness is the first priority. The Indonesian government plans to increase the TTP products and exports that are based on natural fibres in order to promote the TTP competitiveness.[70] Such products would be the priority and focus of the government in facing the end of MFA. There are good reasons for this plan. Firstly, the US as the main export destination country for the Indonesia TTP, has imposed lower duty tariff for TTPs that use natural fibres compared to those using synthetic materials. Secondly, natural-fibres are sufficiently available in Indonesia.

The government is aware of the fact that the TPT industry is one of the pillars in the Indonesia's economy. They encourage the industry to use natural-raw materials sourced domestically. The recommendation is also that the Indonesia's TTP industry should focus on higher level segment products as the lower end has been penetrated by products from China, Vietnam and Bangladesh.[71]

68 Some U.S. lawmakers asked President George Bush in June to support an emergency WTO meeting to reconsider the end-of-year expiry on quotas for clothing and fabrics. ".....Chinese domination of the global textile and apparel trade would shake the economic and political stability of dozens of struggling nations, said a letter signed by 13 Senate Republicans and 16 Senate Democrats, including presidential candidate Sen. John Kerry of Massachusetts....". The Bush administration has steadfastly declined to back away from the quota phase out.

69 Source: www.thejakartapost.com Tuesday, 31 August 2004

70 See MEDIA INDONESIA 29 October 2004 Indonesia akan TPT??

71 See Media Indonesia 01 November 2004 on "TPT Industry seems like A Palace of Sands"

5.2. Automotive Industry

Policy Environment

The motor vehicle industry is one of the Indonesia's designated strategic industries.[72] In the last two decades, the government has employed various policy tools including trade instruments to increase national production and to develop the industry structure (WTO, 1998). Not until 1993 that the government remained to bar the imports of completely built up (CBU) vehicles including second-hand cars, but allowing the import of completely knocked-down (CKD) vehicle. These had offered a stimulus to the local assembly industry.[73] Import measures were supplemented by restrictive licensing requirements and deletion plans in order to achieve the desired level of local-content. Nevertheless, while the production of home-produced components and parts increased, local content ratios remained by far below targets, and plans for the construction of a one hundred Indonesia made vehicle had to be postponed several times.

As indicated in the 1998 Trade Policy Review, with the support of high import protection and severe local-content requirements, Indonesia had developed a motor-vehicles industry specializing in assembly operations (sedan cars, light trucks, vans) for the local markets. Exports of automotive products plus other transport equipment were insignificant, less then one percent of production (WTO, 1998). Most assemblers operate in joint venture with multinational companies such as Toyota, Nissan, Daihatsu, Isuzu, BMW, and Peugeot and are highly dependant on imports of components.

The government was very keen of promoting this industry without deserting the goal of developing the industrial capacity for complete vehicle manufacturing. The 1993 deregulatory package had replaced the prohibition of CBU vehicles policy with a system of high tariffs and surcharges and deletion plans with local content system related to tariff incentives. In addition, it adopted differential tax treatment in favour of locally produced passenger vehicles. In 1995, import tariffs on parts and components associated with the local-content levels were reviewed and reduced.[74] Duty-free treatment is still offered for the same local-content level.

In 1996 another measure was introduced, supplementing the 1993 reforms. The main measure in the package was the introduction of the National Car Programme, intended to produce a one hundred percent Indonesian-made car that was consistent with the Government's long-standing industrialization objectives.[75] However such countries as Japan, the United States and the European Union contested the compliance of certain measures of the 1993 package and the 1996 National Car Programme with WTO rules. A panel was established in June 1997 at the request of the European Union and Japan, which was followed by the US. A single panel was then decided to examine all claims. The Panel Report, circulated to WTO members on 2 July 1998, found several aspects of the 1993 and 1996 car programmes to be inconsistent with certain provisions of the WTO Agreements.[76] Responding to these claims the Government committed itself in January 1998 to "discontinue immediately any special tax, customs and credit privileges granted to the National Car".[77] Following it up the government reflected its pledge to be "consistent with its WTO commitments."

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72 The reasons are firstly, it is supplying the needs for transportation means, secondly, it does not only contribute to economic growth and employment opportunity but also expose the economy to high technology, and thirdly, it generates income for government from import duty and taxes (see Aswicahyono, Anas and Damhuri, 1999).

73 Indonesia imposed base duty rates of 200% on all passenger cars, 100% on jeeps, and from 0 to 100% rates on other commercial vehicles. On top of the tariff, a surcharge was imposed on built-up vehicles, not assembled in Indonesia (100% for passenger cars and 40% for most other vehicles). As a result, imported built-up cars and jeeps were dutiable at a total of 300% and jeeps at 140%. Subsequently, the surcharges were incorporated into the tariffs (1996), and, while remaining very high, the resulting tariffs were reduced. The 1998 MFN tariff on imported built-up passenger cars is 200%, while the average tariff for commercial vehicles is 80% (70% for commercial vehicles exceeding 5 tones).

74 For passenger cars and jeeps, the highest tariff for parts (that is, for cars with local content of less than 20%) was reduced from 100% to 65%. For commercial vehicles, the maximum rate was reduced from 40% to 25%.

75 The detail of this national car program is presented in the Annex 9

76 See in particular the conclusions and recommendations of the Panel in WTO document WT/DS54, 55, 59, 64/R of 2 July 1998, p.397 and 398 and discussion on Industrial Policy and the WTO by Bora, B, et al. 1999.

77 Shortly after, two Decrees of the Ministry of Industry and Trade (19/MPP/Kep/1/1998 and 20/MPP/Kep/1/1998) and a Decree of the Ministry of Finance were issued with this aim. In effect, these Decrees nullify all regulations according specific benefits to the National Car (particularly Government Regulation 20/96, Ministerial Decree 142/96, and Presidential Decrees 42/96 and 82/96).

Obviously for revenue purposes and aimed implicitly toward foreign-made vehicles luxury tax rates have remained high (WTO, 2004). In January 2001, such tax rates on sedans and SUVs with engine size above 4,000cc were raised from 50 to 75 percent. Since July 2001, motorcycles, with engine size from 250 cc to 500 cc, have been subject to a luxury tax of 60 percent or 75 percent for engines larger than 500cc. There was no distinction made in CKD or CBU (completely built-up) items.[78] Import restrictions on all CBU cars have been abolished.[79] The import of used cars with minimum GVW of 24 tonnes is prohibited.[80] In the light of these measures, imports of motor vehicles and parts began to pick up as from 1999, to reach around US$1.9 billion (2000 and 2001).[81]

As noted, the Indonesian automotive industry is a significant industry, but generally inefficient owing to highly distorted policy regime in the past. Prior to the crisis, the automotive industry had recorded tremendous growth. During the period of 1994 to 1997, this sector had experienced an average 20 percent growth rate (Aswicahyono, Anas and Damhuri, 1999). Total investment reached 7.1 trillion rupiah and it employed 70,000 workers. Production of the automotive industry in 1997 reached 390,000 units. The development of the industry has also created demand for components. The local content for minibus and pick-up vehicles had already reached 40 percent and for 5-24 ton trucks had reached 30 percent. However, the local content for sedan was limited to 10 percent on average.

Growth

Production and sales of the industry had been extremely cyclical but growing until 1995, falling in 1996, and picking up again in 1997. Since the beginning of 1998 the market has collapsed, with a 69 percent decline in sales in the first quarter, leaving considerable excess of over 70 percent capacity for the industry.[82] Beginning June 1999, an export-oriented automotive development policy has been implemented to comply with WTO commitments and promote the component sectors. Tariff rates in all market segments for motor vehicles were substantially lowered; the maximum tariff was reduced from 200 percent to 80, and tariffs on CKD kits decreased from 65 percent to 25 up to 50 percent depending on the engine size. The tariff schedule for auto components and parts imported for local assembly has been simplified to a flat rate of 15 percent for imported parts for passenger cars and mini-vans. Imports of raw materials have been exempted from import duties and VAT. Likewise, tax incentives for local content have been phased out. The production index of transport equipment in large and medium manufacturing during 2000-2003 had fluctuated **(Table 5.3.).**

Table 5.3. Index of Production of Transport Equipments of Large and Medium Manufacturing Industry (Industrial code 384, 1993=100)

Year	Average of Year
2000	157.78
2001	148.66
2002	131.61
2003	158.21

Source: Central Board of Statistics.

78 USTR (2002).

79 Ministry of Industry and Trade Decree No. 279/1999 and No. 278/2000.

80 APEC (2002a) find in Trade Policy Review

81 Statistics available by UNSO Comtrade for items under HS87.

82 In June 1998 as a result of declining demand and the rupiah devaluation, Indonesia's largest car manufacturer, ASTRA International, temporarily suspended its production. The sharp depreciation of the rupiah had raised the costs of borrowing and of imported parts, causing the price of ASTRA's motor vehicles to become beyond the reach of local customers. ASTRA, like the other car-makers produces most of its cars in joint venture with international companies such as Toyota, Nissan, Daihatsu, Isuzu, BMW and Peugeot, it was highly dependant on imports of components (WTO, 2004).

Exports

Although very low compared to total world exports, ASEAN export of automotive products had been increasing significantly. In 1991, ASEAN export was only 0.33 percent of world export of automotive product. In 1996 its share in world export of automotive products had doubled (Aswicahyono and Anas, 2000). [83]

For Indonesia whose export of automobile was relatively small compared to total ASEAN exports, the main export destination in 1991 was East Asia. However, in the later period exports shifted towards ASEAN and other small countries classified as 'others'. In 1995, Indonesian exports of automobile to East Asia decreased significantly. It reached only about 2 percent of total Indonesia automobile exports in 1995. While exports to ASEAN market were very small in 1991, only 9 percent, it increased to as much as 51 percent of total Indonesia automobile exports in 1995. In the automotive-parts sub-sector, export destinations were more diversified. The main export destinations were East Asia, NAFTA and Europe. In 1991, exports to those markets were about 21 percent (East Asia), 20 percent (NAFTA) and 16 percent (Europe). In 1995, exports to those markets increased slightly. On the other hand, the ASEAN market was still quite small for Indonesian exports of automotive parts. In 1995, export of automotive parts to the ASEAN market comprised only 7 percent of the total of Indonesia's exports of these parts.

According to the Association of Indonesian Auto Industries (GAIKINDO) Indonesia's automotive exports to ASEAN countries fell to US$9.7 million in 2002 from US$10.9 million two years earlier. Over the same period, automotive imports from ASEAN countries also dropped to US$5.7 million from US$6.8 million. In recent years, there have been improvements in the motor vehicle industry. The percentage of volume and value changes for motor vehicles (covering 4 or more wheels and vehicle spare parts have shown positive trend in 2002 **(Table 5.4.)**. Such trend was likely due to the demand in the domestic market. In its further efforts to boost the automotive industry, the government would prefer investments in the production of multi-purpose vans (MPVs), which had a vast market in the country. This stems from the fact that the component industries in Indonesia are more oriented to producing components for MPVs than for other types of cars. In doing so, the government believes that the strong MPV market base would be advantageous for competing in the export market. The data showed that more than 50 per cent of domestic auto sales consisted of MPVs.[84] The only positive change in export volume of the industry in 2001 was shown by the exports of engine spare parts, 11.83 percent. In 2002 the percentage reached 29.99. It seemed that engine and vehicle spare parts both combined were the largest contributor of exporter of the total motor vehicle manufactured exports, reaching 94 percent of the total **(Table 5.4.)**.

Based on their study on the automotive sector covering the 1991-1996 period, Aswicahyono and Anas (2000) have confirmed that there is a certain degree of specialization among the ASEAN countries. For instance, the Philippines and Thailand dominated ASEAN exports of components. The exports of components from Philippines accounted for about 47 percent of total ASEAN exports of component. Meanwhile Thailand exports of component comprised about 34 percent. Malaysia dominated ASEAN exports in accessories; 60 percent of ASEAN exports of accessories came from Malaysia. With regard to engines, it seems that ASEAN had not yet gained significant market share. It was only 6 percent of total ASEAN exports of automotive parts. Thailand had the highest export share (50 percent of total ASEAN exports of engines).

83 ASEAN export of automobile and automotive parts was dominated by Malaysia. In 1995, Malaysia's share in ASEAN exports of automotive products was about 33 %, while Thailand was about 28 %, Indonesia about 15 % and the Philippines 14 % (Table 2.1). In the automobile sub-sector, the share of Malaysia exports in ASEAN automobile exports was about 58 %, while Thailand share was about 32 %, Indonesia share was about 8 % and the Philippines share was only 2 %. In the automotive parts sub-sector, each country's share in total ASEAN exports was relatively comparable. While Malaysia's share in total ASEAN exports of automotive parts was the largest (30 %), other countries were not much below Malaysia's share (Thailand 28 %, Philippines 26 % and Indonesia 15 %).

84 (BKPM website visited on 25 August 2004 on Indonesian Auto Sector Seeks Investment In MPV Production". Business Asia Today, August 24, 2004 - 2004-08-25 13:33:23 in bkpm website visited on 25 aug 2004.

Indonesia exports only a small fraction of ASEAN automotive-parts. Aswicahyono and Anas (2000) have verified that accessories were the main export commodities, accounting for about 60 percent of Indonesia total exports in automotive-parts. Meanwhile, components were about 34 percent of Indonesia total exports of automotive-parts. Obviously, Indonesia's exports of parts did not concentrate in specific products like other ASEAN countries. Indonesia has been exporting various products but in a relatively small quantity. The largest exports of auto-parts were tires (15 percent of total exports of auto-parts), radio-cassettes and loudspeaker (27 percent) and electric accumulators (18 %). During the period of 1991-1995, 91 percent of exported products in automotive-parts sub-sector showed increasing trends (Aswicahyono and Anas, 2000).

Competitiveness

Aswicahyono and Anas (2000) noted that during the period of 1991-1996 although ASEAN countries generally were still far from having comparative advantage in motor vehicle production, the Revealed Comparative Advantages (RCA)[85] index rapid increase in component sub-sector was noted for Indonesia, apart from Thailand. The automotive industries of Indonesia during the same period that showed high and increasing trends of RCA were mainly in accessories industry (Aswicahyono and Anas, 2000). Such accessories industry includes electric accumulators, tyres for bus and car, oil filters for ignition compression engine, and sound system equipment for car. Briefly, Indonesia had been specializing in accessories (tyres, filters, and sound-system) but was aggressively moving to have comparative advantage in exports of components and engines, which seems to be currently confirmed by the development of the Indonesian automotive industry.

According to the Chairman of Association for Automobile and Motor Components Industry *(Gabungan Industri Alat-alat Mobil dan Motor/GIAMM)* the flourishing growth of the market for components and spare parts industries both globally and domestically has created huge market opportunities. Unfortunately, these industries are only able to supply 30 percent of the needs of domestic motor vehicles and spare parts industries. This is a challenge that needs to be considered seriously as it may be a venue for employment creation. Currently the number of manufacturers of motor vehicle components and spare parts in Indonesia is relatively small. There are only 250 firms producing these components in comparison to Malaysia and Thailand that respectively have 600 and 1200 producers.

Employment

In terms of the structure of automotive production, manufacturer of motor vehicle components and parts are the largest employer both for production and non production workers compared to motor vehicle and motor vehicle body manufacturers (**Table 5.5**.). This reflects that manufacturing of components is more labour intensive. Like in all other manufacturing industries during the financial crisis employment declined. After that in 2002, employment in motor vehicle components and parts both for production and non production workers had increased to even higher than pre crisis levels. For example, the number of workers in 1996 was 22.5 thousand, declining to 16.4 thousand, picked up to 21.3 in 2000 and rose to 30.6 thousand in 2002. In motor vehicle and motor vehicle body industry the level were lower than pre crisis level. This trend was due to the increase in its export volume that consequently required more workers **(Table 5.5.)**. As expected, the percentage of women workers in the motor vehicle and related industries was small, yet in the component and parts industry the share of women employment in production was rather significant, more than 10 percent.

85 The Revealed Comparative Advantage (RCA) index of country is measured by the item's share in the country's exports relative to its share in world trade. The measure reveals information regarding a country's competitive position in the world market.

The Way Forward

Indonesia should take advantage of market opportunities for automotive components and engines, yet to maintain the already established focus on automotive accessories. For this there is a need to prepare the workforce through integrated planning and action. Recommendations coming from practitioners are among others, the need to take strategic steps to materialize the plan. The suggestion that banks should provide credits at low interest rates in order to help manufacturers. At the moment the prevailing rates range from 20 to 40 percent, while in Malaysia and Thailand for example, lower rates could be obtained.[86]

In the recent months a meeting was held in Vietnam to discuss the road map in automotive industry in effort to establish the ASEAN Automotive Integration (AAI). In a series of earlier meetings common efforts to boost intra-ASEAN investment and trade, efforts to enhance capacity in auto industry in ASEAN and efforts to improve workers' skill in the sector were also agreed upon. There was also agreement on concrete efforts to eliminate non-tariff barriers, improve customs regulations and materialize industrial cooperation among ASEAN countries. [87]

There is a plan for ASEAN to open up the automotive sector within the next two years. However, the Indonesia government has decided not to liberalize this sector until 2010. Such a decision was made in order to protect the country's automotive industry from competition with automotive players from neighbouring countries. According to the Director General of Trade for International Cooperation Pos M. Hutabarat of the Ministry of Trade, automotive components dominated the country's temporary exclusion list (78.8 percent) from ASEAN's plan to liberalize eleven "priority sectors" including automotive by 2007. The inclusion of certain goods on the negative list was based on the request of local industry players.[88]

Table 5.4.: Export Volume and Value of Motor Vehicle Indonesia 2001 and 2002

Types from previous	% Volume Change from previous year	% Value Change export year	% of Total
2001			
Motor vehicles (2 or 3 wheels)	-26.39	-29.82	0.11
Motor vehicles (4 or more wheels)	-15.04	-5.13	0.05
Engine spare parts	11.83	-5.95	1.69
Vehicle spare parts	-3.16	1.87	0.65
2002			
Motor vehicles (2 or 3 wheels)	-10.06	-4.80	0.10
Motor vehicles (4 or more wheels)	5.48	31.14	0.06
Engine spare parts	29.99	10.49	1.86
Vehicle spare parts	7.51	14.64	0.74

Source: Central Bureau of Statistics, 2002 and 2003 (January-November).

86 MEDIA INDONESIA, Wednesday, 6 October 2004. "Auto Components Manufacturers Are Not Able to Take Advantages of Market Opportunities" (Industri Komponen tidak Mampu Manfaatkan Peluang Pasar). Jakarta.

87 Business News – 14 July 2004 on "Asean Seeks Road Map In Auto Industry" (statement by the Director general of machinery, metal and electronic industries with the Ministry of Industry and Trade)

88 RI delays liberalization of auto sector under ASEAN plan (Source: Ministry of Trade from the Jakarta Post 04 November 2004)

Table 5.5. Employment in Large and Medium Motor Vehicle, Motor Vehicle Body and Motor Vehicle Components and Apparatus Industry, Indonesia, 1996, 1998 and 2000

Motor Vehicle (Industrial Code 34100) No. of Production Workers	1996	1998	2000	2002
Males	10,310	7,685	10,695	8,268
Females	15	76	342	57
Total	10,325	7,761	11,037	8,325
No. of Other Workers				
Males	3,835	4,138	3,283	2,735
Females	429	502	357	265
Total	4,264	4,640	3,640	3,000
Monthly Wages *('000 Rp)***				
Production Workers	462.47	394.56	731.07	1205.02
Other Workers	671.85	634.85	1781.44	2729.06
Ratio of Wages of "Other Workers" to Production Workers	1.5	1.6	2.4	2.3
Motor Vehicle Body Industry (Code Industry 34200) No. of Production Workers	**1996**	**1998**	**2000**	**2002**
Males	15,321	4,045	5,930	9,359
Females	218	85	96	156
Total	15,539	4,130	6,026	9,515
No. of Other Workers				
Males	1,816	674	1,198	1,520
Females	680	254	460	464
Total	2,496	928	1,658	1,984
Monthly Wages *(Rp '000)*				
Production Workers	173.98	250.99	377.25	409.39
Other Workers	320.19	613.75	520.85	697.57
Wage Ratio of "Other workers" to production workers	1.8	2.4	1.4	1.7
Motor Vehicle Components and Apparatus Industry (Code Industry 38433) No. of Production Workers	**1996**	**1998**	**2000**	**2002**
Males	20,107	14,394	18,298	27,187
Females	2,398	2,080	3,034	3,435
Total	22,505	16,474	21,332	30,622
No. of Other Workers				
Males	5,316	3,567	5,018	5,478
Females	997	852	1,015	1,168
Total	6,313	4,419	6,033	6,646
Monthly Wages *(Rupiah '000)*				
Production Workers	238.38	459.03	621.87	818.6
Other Workers	633.98	1,251.89	2,588.81	2,233.27
Wage Ratio of "Other Workers" to Production Workers	2.7	2.7	4.2	2.7

*Note: * not included other allowances. Source: CBS, Industrial Statistics*

5.3. Wood Furniture Industry[89]

The wood furniture in this case is for most parts represented by teak-furniture, which has a long history particularly in Central Java that dates back to pre-colonial times.[90] In the past decades the growth and development of wood based furniture production, as one of forest based manufacturing products, has been driven by several policies such as the policy on micro and SME development and the measure to ban exports of unprocessed forest products.[91]

89 Partly was based on the ILO study (2003) by Anna Posthuman

90 Jepara and Klaten, the cities located in Central Java, are the two traditional clusters in the area. Wood carving in Jepara started in the 15th century that was originally considered an art form. Products were exclusively owned by the nobility and were not for commercial consumption by the common people. The development of the industry was very slow and went unnoticed until the 18th century when Kartini, the first Indonesian woman leader, popularized the art form. Then, wood carvers began producing articles for trade from that time. Since then, the art of carving has been passed down from generation to generation.

91 Forest based manufacturing products might include timber, rattan and other forest products.

The teak wood based furniture industry has become more well-known during the 1980s. Sales boosted due to domestic consumer demand that made quality furniture more accessible to the growing Indonesian middle class. Due to the depreciation of the Indonesian *rupiah* after the financial crisis the industry experienced a boom. Such benefit contributed considerably to the improvement of the competitiveness of the Indonesian teak furniture in the world market. As of 2002 there were more than 30 furniture clusters in the province of Central Java. Timber furniture is the largest export from Central Java, representing about 35 percent (in 2002) of the exports total value[92] and directly employing over 2 million[93] women and men.

It is estimated that 70 percent of all the wood furniture produced in Central Java is directed to global markets. Indonesian wood furniture products have been facing increasing competition from around the world. Although furniture is a resource- and labour-intensive product, many of the major furniture exporting countries are industrially advanced with Italy ranks the top while developing countries provided by China, Mexico, Malaysia, Romania and Indonesia **(Table 5.6.)**. In 1994 Indonesia ranked fourth after Italy, Denmark, and China in the global furniture trade as the top exporting countries (millions of dollars), its position tumbled down to ranking tenth in 1998 **(Table 5.6.).**

Competition for the wood furniture exporters pertain to market access, generally to OECD countries, with the US being the lead in terms of wood furniture importers (Posthuma, 2003). In recent years, the wood furniture industry in Central Java has been suffering although exports in general seemed to have increased. Many businesses have witnessed their sales and exports declining and foreign business owners are leaving to find more profitable opportunities elsewhere in Indonesia or other countries.

Table 5.6. Global furniture trade-top 10 net exporting countries, 1994 and 1998

	Net export value (millions of dollars)	
Country	1994	1998
1. Italy	6,105	7,831
2. China	1,381	2,725
3. Canada	32	1,804
4. Denmark	1,412	1,323
5. Mexico	259	1,190
6. Malaysia	698	1,052
7. Spain	251	741
8. Sweden	254	494
9. Romania	375	382
10. Indonesia	754	339

Source: (UNIDO World Industrial Development 2003)

There are concerns regarding the future of the wood furniture industry particularly for exports purposes. This is due to the fact that this industry has recently been facing challenges, which originate from a number of reasons such as (a) inefficient management practices and technologies (b) increasing global competition and declining demand[94] and (c) declining availability of good quality timber.[95] With this condition the ILO (2003) has made some recommendations for changes. Through these changes it is anticipated that various jobs will disappear and new jobs will be created.

92 Regional Office of the Industry and Trade in Central Java, Semarang (Report on commodities exports for 2001, 2002, 2003).

93 ASMINDO employment figures for 2002 estimate over 2.3 million workers are employed in roughly 664,000 wood furniture units in Central Java, though the Executive Secretary estimates the number of workers in more in the range of 3-3.5 million.

94 While global demand for wood furniture continues to expand, the decline in hand-carved furniture products from Central Java has visibly fallen since its peak in 2000. Global buyers, driven by a range of decision-making factors, are looking to producers of other countries for innovative designs, lower costs, and greater reliability. The type of furniture that Central Java has traditionally produced has lost much of its appeal. That said, the mass-produced, machine-made garden continues to be pumped out at high volumes.

95 It is estimated that the total demand for timber for use in the wood furniture industry in Central Java is about 1.8 million cubic meters a year- of which roughly 80% is currently teak. However, the productive capacity of PERUM PERHUTANI to fulfill the demand with teak is only around one third, with much of the remaining teak coming from private (including illegal) sources. The government has announced further cuts to the annual harvest rates. Thus, in the future, there will be even less teak. This lack of availability has resulted in more discriminating timber allocation practices – with those firms having greater mobility, financing options, and market sway, securing the best quality of wood at the expense of those smaller and medium sized operations that depend wholly on local timber traders for their supplies.

The Indonesian wood industry in general is facing various problems. For example, wood industry in East Kalimantan is currently collapsing because it is more difficult to obtain raw materials as there is decreasing supply from forests areas. Consequently workers dismissal is inevitable.[96] The situation had worsened with the issuance of the Minister of Forestry's decrees (No. 124, 126 and 128 of 2003) to restrict the quota for wood cutting. This of course will impact workers; there are more than 50 thousands people depending on the wood industry in this province. Similarly in South Kalimantan the logging quota has also been substantially reduced.

Employment

In the *kabupaten* (district) of *Jepara* located on the north coast of Central Java, furniture making activity is a very important livelihood of the people. In the mid 1990s the furniture cluster in *Jepara* was estimated to employ around 40,000 workers in more than 2000 small enterprises and 100 larger firms scattered across the district (Schiller and Schiller, 1997). If piece rate workers were also included, total employment in this industry was estimated as high as 80,000 in 1996 (Schiller and Schiller, 1997 and Yuwono, 1997).

According to the employers association (ASMINDO) and supported by the data on large and medium enterprises **(Table 5.7.)**, in the past three years there has been a declining trend of employment opportunities in the wood furniture industry. This partly stems from the fact that the government has reduced the permit for forest utilization rights (HPH) from 400 to less than 300 permits. In addition, the soft lending from the Ministry of Forestry has also been reduced, which had affected production hence also employment. This government decision was mainly based on the diminishing availability of mature teak plantation. Lest that teak will vanish without being able to replenish it any sooner, the government has to put restriction on cutting teak. Some wood furniture entrepreneurs have started to import wood from overseas, for example those in Central Java have imported from Canada to fulfil its exports.[97]

During the crisis wages in this wood furniture industry rose substantially, then declining after 1998. In the past years wages have been fluctuating. The depreciation of *rupiah* has apparently become a windfall for this wood industry. Wages of production workers in medium and large firms in 1998, for example, were four times higher than those of the pre-crisis level; meanwhile for non-production workers wages rates were six times higher in the same period. Sandee et al (1999) confirm such rising wages, were particularly notable for skilled workers.

Women share in the production employment of large and medium wood furniture manufacturing industry was relatively substantial, around 27 percent in 1996. Their share increased to 32 percent in 1998. The percentage slightly declined to 29 percent in 2002 **(Table 5.7.)**. There are diverse types of wood furniture undertakings generally in Indonesia, particularly in Central Java. For instance, as revealed in the ILO's study that 83 percent of firms in the wood furniture clusters in Central Java operated in the informal economy. Their hiring practices reflect that the level of informality was prevalent. Around 67 percent of the labour force is working under informal relations **(Table 5.8.)**. The high rate of informality of these firms raises important implications for government policy toward this sector. In order to avoid taxation these firms continue to remain unregistered and consequently cannot either avail of existing support or services. Such circumstance will also act as a severe constraint on the ability of firms to grow (Tendler, 2002). One thing that is interesting to note, is that serving the export market does not appear to be a significant factor in influencing firms to move into the formal sector.

The informal hiring practices suggest that the forms of employment are insecure. Meanwhile, few reports confirm that working conditions in informal employment are appalling. A significant characteristic of the industry that should be noted is the informality of employment. Such informality would lead to lack of job security and social protection as well as lacking of compliance with labour standards. In addition working condition and labour standards would likely be less.

96 KOMPAS 26 October 2004 "3.500 Buruh Industri Kayu Diminta Terima PHK".

97 KOMPAS daily, 23 July 2004.

It is important to note that, up to now, the research findings have not indicated that wood furniture buyers are interested in encouraging the use of certified sustainable harvested timber in their products. Similarly, global buyers do not seem to encourage suppliers to improve participation in global markets and does not serve as an impetus for formalisation of firms and their hiring practices (Posthuma, 2003). However, this does not mean that a more consistent policy in this regard would not be effective. A more proactive government policy directed toward stronger supply chain management to encourage upgrading of these wood furniture producers would seem very feasible. As noted (UNIDO, 2002) in countries such as Ireland, Malaysia, Mexico, the Philippines, South Africa and Singapore, strengthened linkages between SMEs and their global buyers can be a powerful thrust to modernise and develop local industries. These countries upgraded their local productive capacities and enhanced their industrial performance by integration into global supply chains. However, such changes depend on strong government policy and on good partnerships and coordination among all key stakeholders.

Table 5.7. Employment in Large and Medium Wood Furniture Industry Indonesia, 1996, 1998 and 2000 (Industrial code 36101)

No. of Production Workers	1996	1998	2000	2002
Males	68,917	79,177	82,875	75,307
Females	25,598	36,741	36,855	30,887
Total	94,515	115,918	119,730	106,194
No. of Other Workers				
Males	8,566	10,020	11,059	10,440
Females	3,204	3,822	4,544	4,236
Total	11,770	13,842	15,603	14,676
Monthly Salary				
Production Workers	150.47	708.34	363.72	504.96
Other Workers	324.21	2235.43	684.89	925.8
	2.2	3.2	1.9	1.8

Source: CBS, Industrial Statistics

Table 5.8. Distribution of number of enterprise and number of workers in furniture clusters in Central Java, 2000

Enterprises	Number	Percentage
Informal	6,830	83.5
Formal	1,353	16.5
Total	8,183	100
Workers		
Informal	26,026	67.1
Formal	12,743	32.9
Total	38,769	100
Market Served	32 clusters	13 clusters for exports plus domestic market

Source: CEMSED 2002

If we take the example of wood-based furniture industry, we could say that the development of the industry had benefited from the policy to bar unprocessed log exports. In this way it may improve the availability of high quality wood. The recent policy change however that limits wood logging (in order to preserve wood forests) has to a large extent been hurting the industry. To overcome this problem some alternatives could be done, for example outsourcing raw materials through imports. The involvement of foreign buyers in this industry is partly due to trade liberalization. Foreigners' involvement particularly in marketing and product designs has proven beneficial to the development of wood furniture industry, particularly in Jepara. Apart from that, support that have been provided by the provincial and local governments have of course been very beneficial to the extent that they were aimed at improving the business climate in the area. The ups and downs of the industry, will consequently impact employment and labour.

CHAPTER 6
TRADE LIBERALIZATION: STAKEHOLDERS' PERCEPTION

This chapter presents the perception of stakeholders on trade liberalization. The stakeholders in this study are divided into 3 broad grouping, i.e., the Government, Employers and Trade Unions. The government is represented by senior officials of the Coordinating Ministry of Economic Affairs, National Development Planning Board, and Ministry of Manpower and Transmigration. Indonesian Chamber of Commerce (KADIN) and Indonesian Employer's Association (APINDO) represent employer. 3 Trade Unions are interviewed to represent Trade Unions, i.e., the *Serikat Buruh Sejahtera Indonesia* (SBSI), the *Serikat Pekerja Seluruh Indonesia* (SPSI) and the *Koperasi Buruh Indonesia*[98]. As presented in Chapter 1, to analyze the responses of the respondents for this study, the method of Analytic Hierarchy Process (AHP) was applied. Through this method the benefit, opportunity, cost and risk of trade liberalization are assessed. A synthesis of the result showing the benefit to cost ratio is also presented.

The chapter is organized as follow. The first section presents general perception on free trade based on interviews and secondary documents (media, conference, press release). While the second section presents the results of AHP. The second section will first look at the overall results (a combined perception of the three groups or stakeholders), followed by further analysis, comparing perceptions among individual group and see how these perceptions deviate from the overall perception.

6.1. General Perception[99]

Employers

"The investment and business atmosphere in Indonesia is not encouraging", this is the statement that always be quoted by employers. The grounds lie among others on unfavourable labour regulation as well as investment-related policy particularly since the implementation of regional autonomy.[100] An interview with the Indonesian Employers' Association (APINDO) reveals information that many entrepreneurs had closed their factories in the country as their businesses were uncompetitive because of poor security, a high-cost economy, raw-material shortages and the absence of legal certainty. Labour dismissals; outsourcing and the recruitment of contract-based workers were inevitable phenomena and are expected to increase in the future. Responding to the view on labour standards in Indonesia employers think it is good. Such view is contradictive to that of labours. Employers complained about the existence of many labour unions that lead to rising more problems.[101]

In an interview with the Indonesia Chamber of Commerce (KADIN) concerning the July Package (*Paket Juli*), KADIN considers that this package is not beneficial for the industrial sector, instead it is potential to increase unemployment. A similar view is also shared by Third World Network,[102] whom adds that many companies would leave Indonesia if the government does not take scrupulous approach on the issue of

98 Questionnaires are sent out to 20 trade unions, but only 3 responded, i.e., SBSI, SPSI, and KBI.

99 Unless otherwise noted, this section relies heavily on interviews with trade unions, Indonesia Employers Association and Indonesia Chamber of Commerce, and the government.

100 The wood furniture employers' association (ASMINDO) mentioned that currently there are 8 types of local retribution that in the past was only 3 types of taxes (from the interview). The SMERU's study reveals that the number of regional government taxes range from 18 to 28 types according to the locality. All these new taxes and retributions have put more burdens to employers.

101 Currently there are more than 80 trade unions exist in Indonesia compared to only one during the New Order regime.

102 Director of Third World Network, Malaysia Mr. Matin Khor in MEDIA INDONESIA 25 August 2004 on Increasing Unemployment: WTO Agreement Hurts Industry.

Market Access for Non Agriculture Product (MANA) contained in the July Package. He further says that the MANA framework has harmful impact on the growth of developing countries. This may be explained as the following. The reduction of tariff and non-tariff barriers agreed by the WTO member countries is to be done in non linear manner. With this formula tariff barrier that previously was 40 percent would be cut down to only 4 percent. Such reduction without doubt would increase the imports from the developed countries. This stems from the fact that before proposing for such tariff cuts the advanced countries would might have likely to ensure that their non agriculture products are able to compete.

The wood furniture employers' association (ASMINDO) agrees with the government policy on trade liberalization and considers AFTA will be very beneficial for Indonesia. However, they suggest that the government should take protective measure anticipating the implications; such as imposing Indonesia standards to imported furniture products. The association considers that skill improvement in this sector is seriously required in order to raise the competitiveness.

Trade unions

Indonesian trade unions have mixed responses with regard to trade liberalization. Some unions say that the government should have not taken this step. Some, however, have positive opinion in the sense that trade liberalization would be beneficial as long as the government takes precaution to anticipate the adverse impacts. These suggested measures that should be done by the government among others through workers skill improvement, good investment policy, and good governance. Illegal imported good is mentioned to be one of the causes of less competitiveness of Indonesian products.

Trade unions are aware that the current employment situation since the crisis is in a very bad shape. They suggested that the government should improve the business climate, eradicate *KKN* (corruption, colluding and nepotism), also to conduct law enforcement seriously. Responding to the question on condition of social protection during the 1990 and now, different answers were given. The majority stated that their welfare were better off in the past. Even though the minimum wage shows increasing trend, but the living cost has had also increased substantially. The minimum wage implementation is not considered as a good measure. For one thing, many employers still do not comply with the law. Secondly the minimum wage does not suffice for decent living. In other words what they need is the wage that is based on decent living standard.

In addition many labour union in Indonesia have exclaimed that amid the prolonged economic hardship there is nationwide trend of outsourcing, layoffs and dismissals as employers tried to raise efficiency levels. Many private and state companies had also cut labour costs by changing the status of their permanent workers to contracted workers. Unlike the previous law, the Labour Act No. 13 of 2003 has sparked strong opposition from numerous labour unions, as it allows employers to lock out their companies, lay off workers and even dismiss workers for reasons of efficiency or bankruptcy. The Textile, Garment and Leather Trade Union, for instance considers that the prevalent outsourcing and dismissals of workers were inevitable, since Indonesia could not compete in the era of free trade and globalization. Many labour-intensive companies in the textile and leather industries have closed down operations and dismissed their workers, because their products cannot compete with similar products from other countries such as China, Thailand and Malaysia.

Government

As the decision maker, the government senses that free liberalization approach is very important in order to boost up the export. This in turn will increase economic growth and consequently create more employment. The government should take precaution in taking such forward step. Supply side measure may be conducted through education and training that is demand driven. Human resources development is required to improve competitiveness both in producing goods and services. The later is particularly important as the WTO is covering trade in services. So does the AFTA through the AFAS.

6.2. Analytic Hierarchy Process (AHP)

AHP basically is a method through which perceptions of a pool of expert on specific issues or problem are gathered, and processed statistically such that will result in a ranking of the problems, issues, and way out or policies.[103] This is done in two steps. First, the experts, the respondents of AHP are asked a set of questions about the positive impact of trade liberalization, which is divided into ***benefits and opportunities***, as well as its negative impact, i.e., ***costs and risks.*** The result of the first step is a list of elements of benefits, opportunities, costs, and risks as listed in Tables 6.1 through 6.6. Second, experts are asked about the relative importance of each element to the other, which after a statistical process resulted in ranking of each element as can be seen in Tables 6.1 – 6.6.

To understand the perception of our respondents, analyses were done to get the overall responses as well as separate response of each group of respondents. Overall responses refer to a combined responses of the three groups of respondent, namely, the government, employers' and trade unions. Separate responses of each group are also presented for comparison among the groups' perceptions as well as to analyse how each group's perception deviates from the overall response.

6.2.1. Overall Response

Overall response views that trade liberalization brings some benefits such as rapid advance in technology and employment, and these two benefits are considered as of similar importance (ranked 1 and 2 are identical, see Table 6.1.). The views that free trade will promote foreign direct investment and product market share were also confirmed and ranked 3-4. Economic growth ranked the last among the benefits expected of free trade. The expectations of opportunities that free trade will provide are ranked as: 1) resource re-allocation, 2-3) transfer of knowledge and regional economic integration, and 4-5) enhancement of product quality and increasing living standard. Regarding the negative impact in term of cost associated with free trade, increasing development gap as well as job loss are considered by the respondents as the most importance costs. In this aspect, worker displacement is ranked the last. In addition, risks that are of highest importance are, consecutively, macro economic disequilibrium and environmental destruction.

The next question is: *How are policies to reap the positive impact as well as mitigate the negative impact of free trade be ranked*? It is interesting to note that synthesis of the results shows that the respondents consider that reducing *KKN* (corruption, cronyism, and nepotism) is the first prioritized policy in the agenda (Table 6.2.). The following priorities are given to education, decentralization policy, and investment policy. It is then followed by such measures as easy access to credit, interest rate policy, training and retraining, as well as taxation policy. Surprisingly, industrial policy was stated as the last priority for all stakeholders. It seems that aiming at improving general foundation is critical before working on the specific policy, namely industrial policy.

103 This report does not include a technical explanation about AHP. For a detail technical explanation, please refer to Thomas L Saaty, "Multicriteria Decion Making: Analytic Hierarchy Process", University of Pittsburgh, 1988.

Table 6.1. Overall Results of BCOR regarding Trade Liberalization

	Priority
I. Benefit:	
1. Rapid Advances in technology	0.247935 (1/2)
2. Increase Foreign direct investment	0.231714 (3/4)
3. Advances product market share	0.231714 (3/4)
4. Rapid economic growth	0.040701 (5)
5. Advances employment	0.247935 (1/2)
II. Opportunity	
1. Regional economic consolidation	0.192404 (2/3)
2. Transfer knowledge and information	0.192404 (2/3)
3. Resources re-allocation	0.309887 (1)
4. Enhancement of product quality	0.152653 (4/5)
5. Increasing standard of living	0.152653 (4/5)
III. Cost	
1. Increasing development gap	0.246841 (1/2)
2. Worker displacement	0.061138 (5)
3. Loss of job	0.246841 (1/2)
4. Loss of industry	0.222590 (3/4)
5. Decrease in local product and output	0.222590 (3/4)
IV. Risk	
1. Advances migration of foreign worker	0.118150 (3/4)
2. Increasing Macroeconomic disequilibrium	0.487458 (1)
3. Advances environmental destruction	0.276242 (2)
4. Threat on security	0.118150 (3/4)

6.2.2. Individual Group Response

The findings on the individual group synthesis demonstrate some appealing results.

Breaking down into details on the BCOR of trade liberalization some results are noteworthy (Table 6.3., 6.4. and 6.5.).

Government perceives trade liberalization to be most beneficial in advancing employment, and economic growth. While both employers and trade unions view that free trade will improve product market share, and promote employment.

The biggest cost of free trade that has been anticipated by the government is the decrease in local products and outputs, which in turn will cause job losses. Employers fear that free trade will cost them loss of industry, which consequently will affect decreasing local products and outputs. Such apprehension are also shared by trade unions that mentioned that loss of industry and declining local products and output are the biggest cost to be paid for free trade.

The government detects that free trade will generate some risks such as migration of foreign workers into the country (ranked 1st), and increasing macro economic disequilibrium (ranked 2nd). Meanwhile, according to employers the more important risks are security threats and increasing macro economic disequilibrium that should be anticipated. On the other hand, trade unions are very apprehensive towards migration of foreign workers into the country, and security threat.

Similar insights coming from the three groups (government, employers and trade unions) on prioritized policies/measures are shown (Table 6.6.). These are easy access to credit as the fifth priority, taxation and industrial policies as the eight and the ninth (last) priority. The priority on *reducing KKN* that is the first priority in the overall results, apparently is not so when individual response is assessed. Reducing KKN as the highest priority is only expressed by the government and trade unions, and not by employers that perceive decentralization policy as the most important policy to be improved to gain better in free trade.

Table 6.2. Synthesis of the Overall Results of Benefit to Cost Ratio Regarding Trade Liberalization

Policy	Ratio
1. Training and retaining	0.106659 (7)
2. Education	0.118980 (2)
3. Taxation policy	0.098165 (8)
4. Easiness to get credit	0.108026 (5)
5. Interest rate policy	0.101835 (6)
6. Reduce KKN	0.145277 (1)
7. Investment policy	0.111544 (4)
8. Industrial policy	0.091263 (9)
9. Decentralization policy	0.118252 (3)

Table 6.3. Analysis of BCOR Based on Government's Perception

Government's Perception	Priority
I. Benefit:	
1. Rapid Advances in technology	0.044904 (5)
2. Increase Foreign direct investment	0.159980 (3)
3. Advances product market share	0.143180 (4)
4. Rapid economic growth	0.199613 (2)
5. Advances employment	0.452323 (1)
II. Opportunity	
1. Regional economic consolidation	0.299557 (1)
2. Transfer knowledge and information	0.207914 (2)
3. Resources re-allocation	0.180491 (3)
4. enhancement product quality	0.150682 (5)
5. increase standard of living	0.161356 (4)
III. Cost	
1. Increasing development gap	0.158656 (4)
2. worker displacement	0.106615 (5)
3. Loss of job	0.243195 (2)
4. Loss of industry	0.240189 (3)
5. decrease in local product and output	0.251345 (1)
IV. Risk	
1. Advances migration of foreign worker	0.278136 (1)
2. Increasing Macroeconomic disequilibrium	0.267600 (2)
3. Advances environmental destruction	0.189142 (4)
4. Threat on security	0.265122 (3)

Table 6.4. Analysis of BCOR Based on Employers' Perception

I. Benefit:	
1. Rapid Advances in technology	0.165220 (4)
2. Increase Foreign direct investment	0.117648 (5)
3. Advances product market share	0.270065 (1)
4. Rapid economic growth	0.187247 (3)
5. Advances employment	0.259820 (2)
II. Opportunity	
1. Regional economic consolidation	0.176599 (4)
2. Transfer knowledge and information	0.185937 (3)
3. Resources re-allocation	0.238633 (1)
4. enhancement product quality	0.234741 (2)
5. increase standard of living	0.164090 (5)
III. Cost	
1. Increasing development gap	0.171140 (4)
2. worker displacement	0.189811 (3)
3. Loss of job	0.101529 (5)
4. Loss of industry	0.309173 (1)
5. decrease in local product and output	0.228347 (2)
IV. Risk	
1. Advances migration of foreign worker	0.454147 (1)
2. Increasing Macroeconomic disequilibrium	0.176555 (3)
3. Advances environmental destruction	0.161348 (4)
4. Threat on security	0.207950 (2)

Table 6.5. Analysis of BCOR Based on Trade Unions' Perception

I. Benefit:	
1. Rapid Advances in technology	0.052882 (5)
2. Increase Foreign direct investment	0.109648 (4)
3. Advances product market share	0.412570 (1)
4. Rapid economic growth	0.135933 (3)
5. Advances employment	0.288967 (2)
II. Opportunity	
1. Regional economic consolidation	0.334345 (1)
2. Transfer knowledge and information	0.122346 (5)
3. Resources re-allocation	0.185364 (3)
4. enhancement product quality	0.132968 (4)
5. increase standard of living	0.224978 (2)
III. Cost	
1. Increasing development gap	0.172094 (3)
2. worker displacement	0.067765 (5)
3. Loss of job	0.117505 (4)
4. Loss of industry	0.381115 (1)
5. decrease in local product and output	0.261521 (2)
IV. Risk	
1. Advances migration of foreign worker	0.091010 (3)
2. Increasing Macroeconomic disequilibrium	0.183541 (2)
3. Advances environmental destruction	0.048917 (4)
4. Threat on security	0.676532 (1)

Table 6.6. Synthesis of the Individual Results of Benefit to Cost Ratio Regarding Trade Liberalization

	Ratio of Benefits to Costs					
Policy/Measure	Government		Employer		Trade Unions	
Training and retaining	0.107626	(6)	0.113731	(4)	0.098270	(7)
Education	0.117997	(3)	0.118944	(3)	0.117582	(2)
Taxation policy	0.099729	(8)	0.100841	(8)	0.097913	(8)
Easiness to get credit	0.108290	(5)	0.112269	(5)	0.105800	(5)
Interest rate policy	0.103156	(7)	0.104034	(6)	0.099466	(6)
Reduce KKN	0.141887	(1)	0.127931	(2)	0.170507	(1)
Investment policy	0.109196	(4)	0.103643	(7)	0.117248	(3)
Industrial policy	0.088712	(9)	0.089218	(9)	0.082803	(9)
Decentralization policy	0.123407	(2)	0.129389	(1)	0.110410	(4)

CHAPTER 7
CONCLUSION AND POLICY RECOMMENDATION

One of the main objective of this study is to assess the effects of AFTA and other trade liberalisation on employment and labour. Most of the earlier chapters give the background as well as try to analyse these effects. However, it has to be admitted at the onset that such effort is not a clear cut analysis to do in an economy such as Indonesia. The reason is that within the period of the 1990s there were a number of significant big events, or mega events, occurring in Indonesia at the same time. First, during the period, Indonesia made commitment to join AFTA and other ASEAN related cooperation, the GATT and WTO, and APEC. Second, within the same period Indonesia was also hit hard by financial crisis, that expanded to be a wide economic, social and political crises. Third, a wide economic and political reformation has taken place in Indonesia as result of political crisis. Therefore it is impossible to isolate the effect of AFTA and other trade liberalisation to those resulted from the other big events. So it is important to bear in mind this limitation in reading this report especially regarding the social implications drawn and concluded in this study. The decision to use AHP (Analytic Hierarchy Process) is expected to overcome the limitation since AHP draw heavily on experts perception, and not so much on statistical data that reflect result of a combination of effects of various mega events mentioned above.

7.1. Conclusion

Free trade is believed leads to greater efficiency and cheaper products. The idea to remove barriers to trade would bring huge benefits to the people of ASEAN, to lead to greater specialization and division of labour as each country will concentrate on producing goods and services in which they have a competitive advantage. With these in mind, AFTA expectedly will have a major impact on the lives of ASEAN people including Indonesians. On the downside, however, the greater levels of competition AFTA unleashes will lead to collapse for inefficient companies that have been operating behind protectionist barriers. Therefore, for a specific country, the key to take advantage of trade liberalisation such as AFTA is very much determined by the competitiveness, cum, the quality of its labour force.

Unfortunately, a low quality of labour force is still a big problem for Indonesia. This is reflected by a the lower level of education of Indonesia's worker compared to other Asian countries. Currently, around 60 percent of Indonesian labour force are in the category of never attend schooling, do not finish primary schools, or complete primary school. The lack of education would hinder the process of industrial transformation that could take place with a faster pace due to trade liberalisation, because people are not flexible to change jobs to more modern sectors. Furthermore, Indonesia has also been experiencing relatively high underemployment problem. For this reason, the government should prevent the decline of labour-intensive employment. Such employment is needed for Indonesia to resolve the pressing unemployment problem. These employment problems would certainly be a serious handicapped for Indonesia to reap greater benefit of trade liberalisation. As the economy opens up wider, the lower quality of labour would not certainly able to compete with the higher quality of labour of the neighbouring countries.

The negative impact of trade liberalisation is also brought about by the stagnant, if not negative, foreign investment coming into the country. The data show, however, that employment has been increasing in absolute terms. It is thus, this mainly reflects the poor quality of employment has amplify employment problem in Indonesia.

In the past Indonesia relied mainly on export of oil and gas. During the era of oil boom, the development of alternative commodities which rely on more value added manufacturing sectors have lagged behind. After experiencing the recession and oil price drop in the mid 80s Indonesia started to realize and changed its economic development strategy and to rely more on labour intensive manufacturing sectors for exports, which is still mainly based on resource and low technology.

With regard to regional cooperation. Indonesia's trade with ASEAN is still a small proportion compared to its world trade. It seems there is still a tremendous scope for increase. Consequently, there is necessity to make an adjustment to labour market. Apart from AFTA, Indonesia is also involved in regional agreement that involves several neighbouring countries like in the case of BIMP-EAGA (Brunei Indonesia, Malaysia, Philippines – Eastern Asia Growth Area) and IMT-GT (Indonesia Malaysia Growth Triangle).

Reductions in Indonesia's tariff rates associated with AFTA, have closely followed reductions in MFN rates. Therefore, the margin of preference for Indonesia's ASEAN trading partners has remained fairly small at about 2.5 percent. The margin is probably even smaller for agricultural commodities because of the sharp reduction in tariffs required by Indonesia's LOI (Letter of Intent) with the IMF.

An important question relating to AFTA is whether it has a big impact to the region and to each and every ASEAN countries. Analysis in Chapter 3 suggests that since most ASEAN trade is with non-ASEAN countries, the impact of AFTA on ASEAN countries including Indonesia has probably been small.

The issues relating to labour mobility is also an important issue associated with trade liberalisation, and has a significant international dimension. The issue can no longer be seen as a national concern. Increasing economic integration demands that attention be given to a comprehensive regional macro development strategy, migration laws and regulations, protection and rights of local and migrant workers and the need for a more effective mechanism to protect female migrant workers who were subjected to exploitation at work and sexual abuse. The government should take this issue diplomatically and seriously in order to protect migrant workers.

Currently, a big issue in Indonesia's migrant workers is very much related to their legal status and to the fact that the majority of them work in the informal sector. Therefore, an effective way to protect migrant worker would only be feasible by transforming the type of workers to be employed overseas to more formal workers which at the same time also solves the problem of their legal status.

Case study

Garments. The industry is labour intensive, employing more women than men. Working relation in the industry, to a large extent, is based on sub contracting. Sub-contracted employment is usually done on the workers' own home, thus informal working relation is prevalent. As such, the labour standards and working condition are usually neglected. A low wage characterised the workers, but the low wage still constitutes an important source of income to the families involved. The sector is an important source of Indonesia's non oil/gas exports. Apart for export market, garments also aims at domestic markets. However, the invasion of second hand garments from overseas has threatened this industry, and more even so as the domestic market is opened wider with trade liberalisation. Even though the government has banned this second hand garment imports, such practice is still continued illegally. At the moment, the industry as well as Indonesia's textile has to compete fiercely with China. As China enters the low end segment (mass production) the government has encouraged the industry to attempt entering the upper segment, better quality garment products.

Wood furniture. This industry is labour intensive. Working relation in the industry is mainly informal as a considerable number of workers are contracted to do certain parts of the production. This is almost similar to garment industry. The industry is also facing tough situation as its competitiveness has been declining. The competition with China as a new comer is also a problem. To increase product competitiveness is also one of the agenda, apart from seeking other sources of raw materials for production and improving product quality.

Automotive. Indonesia is still relying on producing components and spare parts for automotive. The government has decided not to liberalize automotive industry until 2010 in order to protect the industry. Focusing on component and spare parts is likely the feasible way for Indonesia to boost the industry. Similar to the other two sectors improvement in quality needs to be done.

The cases study reveal that at least the first two, garment and wood furniture, are not in favourable condition with trade liberalisation, mainly due to the very low quality of labour, cum, a low ability to compete with the region's and worldwide products.

Protective Measures

The government of Indonesia, as an effort to provide protective measures particularly to cope with employment problems which has been amplified by trade liberalisation and especially by the economic, social, and political crises, has revised some manpower regulation and law. Most important effort is the issuance of the Manpower Act No. 13 of 2003. The act seems to have anticipated the social impacts of globalization. The law covers important aspects of the working life including on *child labour*.

Regarding child labour the government has set up a body for monitoring the worst forms of child labour and issued a government regulation that prohibits the employment of children. However, considering the fact that some children have to work to help the family income, some clauses have been drawn to protect these child labours.

Transfer of knowledge from expatriates to national workers has been anticipated through the investment and manpower policies. For example, the Ministry of Manpower and Transmigration requires that training levy is imposed to expatriate workers. Such levy would be used for training purposes.

Regarding social protection, the government has just issued an Act on National Social Security System in which social security for informal sector would also be covered.

Apart from that, such aspects as training and manpower training, minimum wage, labour Standards, Occupational Safety and Health (OSH) and others are also regulated in the Act. Currently the government is preparing the regulations to implement the aforementioned Manpower Act.

Stakeholders' Response

There is only a few opposition from labour groups regarding free trade. Similarly, the employers in general and the government are looking at free trade in a positive way. A convincing reason why AFTA is important now is the rise of China's economic hegemony. It is therefore ASEAN collectively stands a better chance of competing against China than if its members were to try to compete individually. The launching of AFTA may be considered modest, for it involves only six of ASEAN's 10 members, and does not cover all products and services.

AHP or Analytic Hierarchy Process is used in this study to reveal stakeholders' response to AFTA and other trade liberalisation. As such, AHP analysis constitutes an important part of the report. Respondents response reveal that the positive impacts of trade liberalisation consist of benefits and opportunities, while the negative impacts are costs and risks. A summary of the analysis is given in section 7.1.1. and 7.1.2. (Please refer to Chapter 6 for a detail analysis).

7.1.1. Overall Response

Overall response views that trade liberalization brings some benefits such as rapid advance in technology and employment, and these two benefits are considered as of similar importance (ranked 1 and 2 are identical, see Table 6.1.). The views that free trade will promote foreign direct investment and product market share were also confirmed and ranked 3-4. Economic growth ranked the last among the benefits expected of free trade. The expectations of opportunities that free trade will provide are ranked as: 1) resource re-allocation, 2-3) transfer of knowledge and regional economic integration, and 4-5) enhancement of product quality and increasing living standard. Regarding the negative impact in term of cost associated with free trade, increasing development gap as well as job loss are considered by the respondents as the most importance costs. In this aspect, worker displacement is ranked the last. In addition, risks that are of highest importance are, consecutively, macro economic disequilibrium and environmental destruction.

The next question is: *How are policies to reap the positive impact as well as mitigate the negative impact of free trade be ranked*? It is interesting to note that synthesis of the results shows that the respondents consider that reducing *KKN* (corruption, cronyism, and nepotism) is the first prioritized policy in the agenda (see Table 6.2.). The following priorities are given to education, decentralization policy, and investment policy. It is then followed by such measures as easy access to credit, interest rate policy, training and retraining, as well as taxation policy. Surprisingly, industrial policy was stated as the last priority for all stakeholders. It seems that aiming at improving general foundation is critical before working on the specific policy, namely industrial policy.

7.1.2. Individual Group Response

The findings on the individual group synthesis demonstrate some appealing results.

Breaking down into details on the BCOR of trade liberalization some results are noteworthy (see Tables 6.3. – 6.6.).

Government perceives trade liberalization to be most beneficial in advancing employment, and economic growth. While both employers and trade unions view that free trade will improve product market share, and promote employment.

What are the opportunities expected from free trade? The government as well as employers expects that free trade will be best for regional economic consolidation. It is not the case for trade unions, they view that free trade is the opportunity for resource re-allocation.

The biggest cost of free trade that has been anticipated by the government is the decrease in local products and outputs, which in turn will cause job losses. Employers fear that free trade will cost them loss of industry, which consequently will affect decreasing local products and outputs. Such apprehension are also shared by trade unions that mentioned that loss of industry and declining local products and output are the biggest cost to be paid for free trade.

The government detects that free trade will generate some risks such as migration of foreign workers into the country (ranked 1st), and increasing macro economic disequilibrium (ranked 2nd). Meanwhile, according to employers the more important risks are security threats and increasing macro economic disequilibrium that should be anticipated. On the other hand, trade unions are very apprehensive towards migration of foreign workers into the country, and security threat.

Similar insights coming from the three groups (government, employers and trade unions) on prioritized policies/measures are shown. These are easy access to credit as the fifth priority, taxation and industrial policies as the eight and the ninth (last) priority. The priority on *reducing KKN* that is the first priority in the overall results, apparently is not so when individual response is assessed. Reducing KKN as the highest priority is only expressed by the government and trade unions, and not by employers that perceive decentralization policy as the most important policy to be improved to gain better in free trade.

7.2. Recommendation

Finally some recommendations can be put forward as inputs for the stakeholders to be considered to speed up economic development and stand in a better position in the wave of trade liberalisation. The recommendations are outcomes of the analysis in this study as well as results of discussions and interviews with the satkegolders conducted in this study;

To identify industries that have opportunities for expansion such as manufacturing of motor vehicles components and spare parts. Such expansion will be expected to create more employment. However, there is a need to prepare the workforce that are skilful in that way the industry may achieve its goals to provide employment and to achieve high productivity as well.

Skilled labour is required in order to reap the benefits of trade liberalization. As the majority of the Indonesia labour force have a relatively low educational background as well as mainly unskilled labour, it is imperative that the government put emphasis on promoting its human resources. Labour and employers' organization have the same opinion towards the importance of having skilled labour to take advantage of trade liberalization.

To achieve higher economic advantages the government's policy should be directed towards further liberalization. However, thorough studies and participatory discussion with all stakeholders including workers and employers representative should be deliberated before such policy is to be taken up.

Indonesia should ensure that the five major strategies that have been formulated to promote global competitiveness are to be carried out in sustainable manner.

Good governance and favourable climate for business activity should be promoted. As noted foreign direct investment into Indonesia has been declining, even until now it is still stagnant with various reasons. It is necessary to attract FDI back into the country as required by international community.

Consistent, clear and transparent regulations are important. Consistent and relevant regulatory framework is important in that way that business feel secure and protected from unclear, inconsistent and excessive regulations. Labour market regulation should be in balance in the sense that it is neither too pro labour nor too pro employer. The role of social dialogue is very important to achieve mutual agreements between employers and workers.

The government should ease the existing labour regulations. Some of the labour regulations have discouraged potential investors to enter the country particularly those that intend to invest in labour-intensive projects as such regulations make company pay more expensive. This is also worsened by the practices of regional government's autonomy.

Easement of people's mobility within ASEAN at least should be promoted. The plan of the government to banish departure tax for those leaving for abroad is one way to boost favourable climate for business activity. The magnitude of Indonesian working overseas is increasing, however they are mainly unskilled labour. The attempts of sending more skilled labour should be realized. Overseas employment may serve two folds, firstly to reduce unemployment problem in the country and secondly to increase the government revenue. Because there is such a wide disparity in development levels among ASEAN countries, the incentive for labour mobility in ASEAN is large. There is a need of careful monitoring in labour movement within ASEAN.

Attempts should be made to identify different stages of production of a product in ASEAN countries, with each stage of production being produced in the country with the most comparative advantage for it. In this way fragmentation of works could be distributed to member countries and sourcing of parts should be done without tax penalty.

Prevention of de-industrialization It was noted that many of the workers who lost their jobs in the manufacturing sector moved to the agriculture, forestry and fishery sectors. This was reflected by the increasing number of people working in agriculture in recent years after the crisis. It is also likely that "deindustrialization" of the economy was taking place, wherein people from the formal manufacturing sector were moving back to pre-industrial jobs like farming and fishing. Observer suggests that instead of continuing to increase the minimum wage, the government should work together with companies to provide affordable accommodation near factories.

Capacity building for trade unions is necessary. Trade unions need assistance in under-standing international development, they should understand the rights and obligations and the consequence of free trade. They have to improve their skills and abilities in that way that labour may have wider perspective that in turn will provide career choices. Capacity building of trade unions should be maintained in sustainable manner.

Capacity building on minimum wage mechanism and setting. As minimum wage issue seems to be a highly debatable topic between employers and employee, capacity building for both employers and employees is necessary in order to reach a common understanding.

Social security is imperative. To protect workers from disadvantaged condition they should be protected by social security scheme. The social security act needs to be reviewed thoroughly and carefully before it is spelled out in regulations. Employers and workers should be involved in the discussion as they are the critical stakeholders in the scheme.

It has been the case that the positive impact of social protection on the economy has often been neglected. This good impact can be enhanced by better coordination between social protection, labour market and anti-poverty policies. Top priority must be given to finding the most effective means to bring social protection to the majority who still go without.

Last but not the least, are general recommendations stemming from AHP analysis which is very strighforward, i.e., to focus in the nine prioritized policies reveal by the stakeholders: reduce KKN, education, decentralization policy, investment policy, easiness to get credit, interest rate policy, training and retaining, taxation policy, industrial policy.

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ANNEXES

Annex 1
Selected Macroeconomic Indicators, Indonesia 1997-2002

	1997	1998	1999	2000	2001[a]	2002[b]
National accounts (1993 constant prices)			*(Percentage change)*			
Real GDP, market prices	4.7	-13.1	0.8	4.9	3.4	3.7
Private consumption	7.8	-6.2	4.6	1.6	4.4	4.7
Total consumption	7.0	-7.1	4.3	2.0	4.8	5.5
Gross fixed capital formation	8.6	-33.0	-18.2	16.7	7.7	-0.2
Gross investment	28.3	25.4	20.1	21.8	21.8	20.2
Private consumption	61.7	67.8	73.9	67.3	67.3	70.7
Prices and interest rates						
Consumer price inflation (period average)	6.1	58.5	20.5	3.7	11.5	11.9
Bank rate (December, per cent)[c]	15.3	25.6	25.2	12.9	15.3	15.8
	(17.4)	(26.9)	(24.6)	(12.5)	(14.8)	(15.5)
Central bank certificates (SBI) (period average)	14.5	49.3	23.1	12.5	16.6	14.9
Public finance			*(Per cent of GDP)*			
Budget deficit	-0.7	-2.9	-1.5	-1.6	-2.7	-1.7
Expenditure	17.8	17.6	21.1	21.7	24.5	19.7
Revenue	17.2	15.4	18.6	20.3	20.7	18.0
Total outstanding public debt	..	..	105.4	138.4	100.1	89.2
Domestic debt	..	..	45.5	66.8	46.9	42.7
Monetary sector (period average)			*(Percentage change)*			
M0 (base money)	..	..	..	18.6	17.9	9.1
M1	23.2	22.6	18.8	22.7	19.8	9.9
M2	22.2	62.3	11.9	9.9	14.7	8.1
External sector			*(Per cent of GDP, unless otherwise specified)*			
Trade balance	4.6	18.9	14.8	16.6	16.0	13.5
Services (net)	-6.9	-14.7	-10.7	-11.3	-11.2	-9.2
Current account balance	-2.3	4.2	4.1	5.0	4.7	4.0
Capital and financial account balance	1.2	-4.0	-3.3	-4.5	-4.8	-2.1
Official flows	1.3	10.2	3.8	2.1	-0.5	0
Private flows	-0.1	-14.2	-7.1	-6.6	-5.9	-1.7
Foreign direct investment, net	2.1	-0.4	-2.0	-3.0	-4.2	-4.1
Portfolio investment, net	-2.2	-13.8	-5.1	-3.6	-1.7	2.4
Total external debt (end-period)[d]	62.1	154.8	106.2	94.0	94.0	76.4
Short-term external debt	15.0	16.9	12.9	15.4	..	9.3
Debt-service ratio[e]	30.0	31.7	30.4	41.0	39.7	32.2
Gross official reserves, US$ billion[f]	17.5	23.6	27.3	29.4	28.0	31.6
Reserve cover (months of GS imports)[g]	4.5	8.7	10.9	8.6	9.0	10.9
Exchange rate (percentage change, period average)						
Real effective exchange rate (CPI-based)[h]	-5.6	-51.7	45.2	-1.9	-4.7	26.1
Nominal effective exchange rate	-9.1	-69.0	22.6	-5.3	-13.9	..
Merchandise trade (average of imports and exports)	23.4	42.2	29.3	35.1	32.5	27.0
			(Twelve-month growth rate in US$, end period, per cent)			
Merchandise export growth	12.2	-10.5	1.7	26.5	1.9	-1.2
Merchandise import growth	4.5	-30.9	-4.2	21.1	8.1	-8.3
Memorandum items:						
Nominal GDP (US$ billion)	219.0	97.5	139.5	150.7	141.6	171.9
Gross national savings (per cent of GDP)	31,5	26.5	19.5	25.6	24.9	21.1
Gross domestic investment (per cent of GDP)	31.8	16.8	11.4	16.1	17.4	14.3
Exchange rate (Rupiah per US$, period average)	2,866	9,804	7,882	8,394	10,238	9,367
Unemployment rate (per cent)	4.7	5.4	6.3	6.1	8.0	9.1

.. Not available.
a Provisional.
b Preliminary.
c On rupiah six-month time deposits at state banks. The rates in brackets are for foreign and joint banks.
d Includes both public and private debt.
e Debt service as a share of exports of goods and non-factor services in convertible currencies.
f Total reserves, including gold, end-of-period.

g GS = goods and services.
h Increase equals rupiah appreciation.

Source: WTO, 2004 (taken from Bank Indonesia (2002), Annual Report 2001; World Bank (2003), Indonesia Maintaining Stability, Deepening Reforms, *Report No. 25330-IND, January; IMF (2002),* Indonesia: Selected Issues, *Country Report No. 02/154, July; IMF (2002),* International Financial Statistics, *CR-ROM, October; World Bank (2002),* World Development Indicators 2002, *CD-ROM; and various publications from Indonesian government).*

Annex 2
Ranking by Share of Medium & High Technology in Manufacturing Value Added for Selected Countries, 1985 and 1998

Country	Year		Share of Medium & High Tech Industry		Share of Low tech & Resource-based Industry	
	1985	1998	1985	1998	1985	1998
Singapore	1	1	67	80	33	20
Korea	25	9	47	60	53	40
Malaysia	24	11	47	60	53	40
Taiwan, China	31	14	43	57	57	43
China	19	22	49	51	51	49
Indonesia	55	36	25	40	75	60

Source: UNIDO, World Industrial Report, 2003

Annex 3
Ranking by Share of Medium and High Technology In Manufactured Exports for Selected Countries, 1985 and 1998

Country	1985	1998
Singapore	13	3
Malaysia	26	6
Korea	7	10
Taiwan, China	17	11
China	48	29
Indonesia	60	42

Source: UNIDO, World Industrial Report, 2003

Annex 4
Value of Exports by Principal Country of Destination, 1996-2003(US$Million)

	1996	1997	1998	1999	2000	2001	2002	2003
ASEAN	7,397	8,019	7,596	7,402	9,625	8,446	8,439	4,952
Malaysia	1,110	1,357	1,358	1,336	1,972	1,779	2,030	1,307
Thailand	823	848	943	813	1,026	1,064	1,227	836
Philippines	688	794	707	695	843	815	778	535
Singapore	4,565	5,468	5,718	4,901	6,523	5,364	5,349	3,077
Brunei	27	39	35	27	25	23	32	17
Vietnam	337	390	351	332	361	322	393	257
Cambodia	80	70	65	69	52	72	69	49
Laos	1	1	2	2	1	1	1	0
Myanmar	78	150	167	74	65	69	54	30
China	2,057	2,229	1,832	2,009	2,768	2,201	2,903	2,011
ongKong	1,625	1,785	1,865	1,330	1,555	1,290	1,242	699
pan	12,885	12,485	9,116	10,397	14,415	13,010	12,045	7,923
rica	619	777	904	995	1,114	1,081	1,092	708
A	6,795	7,148	7,03	16,897	8,475	7,749	7,559	4,450
nada	369	400	412	353	404	390	378	241
stral/Oceania	589	783	910	1,020	1,040	993	1,318	713

Europe	7,482	9,112	8,273	7,369	9,165	8,379	8,403	5,219
EU	6,795	8,408	7,474	6,744	8,451	7,449	7,306	4,556
United King	1,193	1,238	1,143	1,176	1,508	1,383	1,252	670
Netherlands	1,667	1,842	1,512	1,543	1,837	1,498	1,618	810
Germany	1,415	1,502	1,458	1,217	1,367	1,232	465	0
Belgi&Luxem	780	796	876	697	857	782	794	570
France	589	499	547	503	718	663	649	372
Denmark	141	146	143	142	135	109	103	64
Ireland	38	55	48	42	68	67	55	34
Italy	744	826	859	656	718	622	720	514
Greece	86	89	108	78	99	94	88	51
Portugal	46	42	37	40	50	76	52	29
Spain	813	888	869	742	932	904	996	698
Total	**49,815**	**53,444**	**48,848**	**48,665**	**62,124**	**56,321**	**57,159**	**35,724**

Source: Central Bureau of Statistics taken from Table 19 in the World Bank "Beyond Macro Economics"

Annex 5
Value of Imports by Principal Country of Origin, 1996-2003(US$ Million)

	1996	1997	1998	1999	2000	2001	2002 Jan-Jul	2003
ASEAN	2,814	3,743	2,646	2,977	3,563	3,199	3,804	2,812
Malaysia	816	865	627	589	1,129	1,005	1,037	573
Thailand	1,081	867	842	933	1,109	986	1,191	914
Phi1ippines	90	127	65	55	115	94	114	99
Singapore	2,856	3,411	2,543	2,448	3,789	3,147	4,100	2,411
Brunei	238	7	0	38	16	37	34	75
Vietnam	204	117	421	590	303	171	259	327
Cambodia	650	0	2	1	1	0	1	1
Laos	0	1	0	0	1	0	0	0
Myanmar	34	19	9	19	22	21	31	9
China	1,577	1,518	906	1,242	2,043	1,843	2,427	1,697
HongKong	266	325	264	227	342	257	241	128
Japan	8,555	8,252	4,293	2,912	5,397	4,689	4,409	2,450
Other Asia	3,572	4,839	3,93	13,068	3,391	2,083	2,783	2,628
Africa	406	468	399	339	348	369	300	190
USA	5,130	5,441	3,517	2,837	3,390	3,208	2,640	1,621
Canada	804	682	504	417	638	357	412	184
Australia And Oceania	2,539	2,427	1,750	2,219	2,359	1,785	1,526	1,796
Europe	7,237	9,744	6,520	4,061	4,878	3,961	4,197	2,635
UK	1,140	1,084	920	511	557	641	656	265
Netherls	505	566	338	347	434	344	352	219
Germany	3,010	2,629	2,366	1,398	1,245	1,301	1,224	696
Belgium& Luxemburg	398	340	275	178	278	215	191	113
France	1,037	1,017	568	371	400	397	406	270
Denmark	187	159	50	38	44	58	45	23
Ireland	40	35	25	31	66	42	42	27
Italy	1,169	918	480	276	345	407	402	196
Greece	83	52	19	25	15	18	16	9
Portugal	217	22	2	2	2	2	2	1
Spain	342	370	160	206	185	178	130	66
Total	**42.929**	**41.680**	**27,337**	**24,003**	**33,515**	**30,962**	**31,289**	**18,629**

Source: Central Bureauof Statistics taken from Table 20 in the World Bank's Beyond Macro Economics"

Annex 6
Indonesian Trade to and From ASEAN 1996-2001 (US$ Million)

Export To	1996	1997	1998	1999	2000	2001	Market Share in 2001 2001	Growth 1996-2001 Rate
Brunei	29,02	3814	3566	2763	2551	2161	0.35	-5.73
Laos	0,72	85	181	169	88	144	0.01	14.87
Malaysia	1196,39	147335	135847	133594	197184	177863	14.40	8.25
Myanmar	86,78	13778	16734	7433	6475	6898	1.04	-4.49
Philippines	725,03	74440	70738	69469	81953	81478	8.72	2.36
Singapore	4952,79	523085	571828	493051	656238	536383	59.60	1.61
Thailand	889,46	79497	94250	81270	102646	106362	10.70	3.64
Vietnam	358,03	36526	35061	33160	36064	32205	4.31	-2.09
Cambodia	71,93	6536	6469	6919	5168	7213	0.87	0.05
Total ASEAN	**8310,15**	**885096**	**934674**	**827828**	**1088367**	**950707**	**100.00**	**2.73**
Import From								
Brunei	80	660	18	3766	1647	3714	0.68	115.45
Laos	30	70	40	11	116	20	0.00	-7.79
Malaysia	88030	86480	62663	60564	112877	100546	18.41	2.69
Myanmar	3510	1900	914	1933	2198	2083	0.38	-9.91
Philippines	11150	12700	6500	5550	11473	9385	1.72	-3.39
Singapore	308700	341090	254282	252595	378869	314705	57.62	0.39
Thailand	121740	86670	84195	93339	110906	98605	18.05	-4.13
Vietnam	21400	11730	42053	60455	30331	17130	3.14	-4.35
Cambodia	280	10	9	143	66	13	0.00	-45.88
Total ASEAN	**554920**	**541310**	**450674**	**478356**	**648483**	**546201**	**100.00**	**-0.32**

Source: Center of Data and Information, Ministry of Industry and Trade (website visited in June, 2004)

Annex 7
Investment Negative List (as from 2000)

Business activity

I. **Absolutely Closed for Investment (Domestic and Foreign)**

Agriculture
1. Cultivation and processing of marijuana and the like

Marine and fishery
2. Collection/utilization of sponge

Industrial and trading
3. Chemicals harmful to the environment, e.g. penta chlorophenol, dichloro dipenhul trichloro ethane (DDT), dieldrin, chlordane, carbon tetra chloride, chloro fluoro carbon (CFC), methyl bromide, methyl chloroform, halon, etc.
4. Chemicals stipulated in schedule 1 of the Chemical Weapon Convention – sarin, soman, tabun, mustard, levisite, ricine, saxitoxin
5. Weapons and related components
6. Cyclamate and saccharine
7. Alcoholic drinks e.g. liquor, wine and beer (drinks containing malt)
8. Casino and gambling facilities

Communication
9. Air traffic system providers (ATS providers), ship certification and classification inspections
10. Management and operation of radio frequency spectrum and satellite orbit monitoring stations

Mining and energy
11. Mining of radioactive minerals

II. **Closed to Any Foreign Investment (Closed to Investment in Which a Share is Owned by Foreign Citizen and/or Foreign Business Entities)**

Forestry and plantation

12. Germ-plasm cultivation
13. Concession for natural forests
14. Contractors in the field of lumbering

Communication

15. Taxi/bus transportation services
16. Small-scale sailing

Trading

17. Trading and trading support services, except large-scale retailers (malls, supermarkets, department stores, shopping centres), wholesale trading (distributors/wholesalers, exporters, and importers), exhibition/convention service providers, quality certification service providers, market research service providers, warehousing services outside seaports, and after-sale service

Information

18. Radio and television broadcasting, services providers, radio and closed-circuit television broadcasting services, and multimedia and printed media
19. Motion picture production (film production, film technical services, export and import film business, film distributors and operation of motion picture theatres

III. **Open to Investment Under The Condition of A Joint Venture Between Foregin and Domestic Investors**

'20. Building and operation of seaports
21. Electricity production, transmission and distribution
22. Shipping
23. Processing and provision of potable water for public use
24. Medical services, including the building and operation of hospitals, medical check-ups, clinical laboratories, mental rehabilitation, public health maintenance security, rent of medical equipment, assistance services for health aid and evacuation of patients under emergency conditions, hospital management services and services for testing, maintenance and repair of medical equipment
25. Telecommunications
26. Regular/non-regular commercial airliners

IV. **Open to Investment Under Certain Conditions**

Marine and fishery sector

27. Cultivation of freshwater fish (a) open to foreign investment for freshwater turtles, nila gift, sidat, kodok lembu, freshwater giant shrimps and thillapya sp (b) in cooperation with small-scale fishery business
28. Fishing of demersal fish (big fish, grouper and other sea fish, except ZEEI areas of the Malacca Strait and Arafura Sea

Industrial

29. Wood pulp (a) raw material obtained from imported chips or quarantine of raw material supplied from industrial timber estates (HTI) (b) other than sulphonating and/or chlorination (C 12)
30. Pulp made from cellulose fibres or other materials, except sulphonating and/or chlorination (C 12)
31. Chloro alkali, except using mercury
32. Finished/semi-finished goods made from mangrove wood – raw material coming from mangrove cultivation
33. Money printing – operational licences from BOTASUPAL-BAKIN and approval from Bank Indonesia required
34. Special printing – postal stamps, duty stamps, Bank Indonesia negotiable papers, passports and stamped postal matter; operational licences needed from BOTASUPAL-BAKIN
35. Milk processing (powder and condensed sweetened condensed milk (processing not repackaging)
36. Plywood and rotary veneer (only for the Irian Jaya Province (Papua)
37. Sawn timber (a) only for the Irian Jaya province (Papua) (b) or outside, only using logs from non-natural forests
38. Ethyl alcohol – technical grade, being only used as raw materials and auxiliary materials of other industries
39. Raw materials for explosives (ammonium nitrate) – only in cooperation with business entities, which have security devices and recommended by the Ministry of Defence
40. Explosives and components for industrial (commercial) use (a) only in cooperation with business entities recommended by the Ministry of Defence, (b) only manufacturing; storage and distribution are provided by companies appointed by the Government
41. Electricity planning and supervision consulting services, open to foreign investment provided capacities above (a) 50MW for hydro power plant (PLTA), (b) 55MW for steam power plants (PLTU), (c) 55MW for geothermal power plants (PLTP), (d) main electrical relay stations and transmission networks with voltage above 500 KV
42. Electricity equipment construction, maintenance, installation services, development of technology supporting the supply of electricity and testing of electricity installations – open to foreign investment providing that main electrical relay stations and transmission networks have capacity above 500 KV
43. Petroleum and natural gas drilling services – open to foreign investment provided (a) only for offshore drilling, (b) especially outside the eastern Indonesian region in cooperation with national partners of business field
44. Power plants in locations outside Java, Bali, and Madura

Trading

45. Restaurants – open to foreign investment if located in tourism areas/zones and/or integrated with hotels
46. Game services – open to foreign investment if located in tourism areas/zones and/or integrated with hotels

Source: *BKPM, based on Presidential Decree No. 96/2000, jo.118/2000.*