

TRADE REFORM AND EXPORT OPPORTUNITIES

KEY POINTS

- Since the onset of the financial crisis, the Indonesian Government has accelerated trade reform. Indonesia now is moving towards a liberal trade regime, similar to Singapore's or Hong Kong's in the 1960s and 1970s.
- By mid 2000, 60 per cent of tariff lines had duties of 0 to 5 per cent, and over 70 per cent had tariffs of 10 per cent or less. The unweighted average tariff rate now is below 9 per cent.
- Tariff reductions include agricultural products; these reductions lowered the unweighted average tariff rate on agricultural products from 19 per cent in 1995 to 8.6 per cent in 1998.
- The Government has removed many non-tariff barriers on agricultural imports, notably import licensing requirements on commodities the national logistics agency, BULOG, controlled, permitting competitive imports and distribution of wheat, flour, sugar, soy beans and garlic.
- Reductions in tariffs and local content requirements also are boosting prospects for Australian car exporters in Indonesia.

In response to the financial crisis and its participation in multilateral trade reforms, the Indonesian Government has accelerated its trade reform program since 1995. By encouraging labour intensive manufacturing, increased openness to international markets complements other post crisis government reforms to improve efficiency in the Indonesian business sector and promote more equitable development. Lower trade barriers also benefit Australia, as it is a natural trading partner with Indonesia, with complementary resource and human capital endowments.

This chapter briefly reviews the history of trade policy in Indonesia. Although in the past, economic down turns and oil price volatility often forced Indonesia to liberalise trade, its renewed free trade agenda in the mid to late 1990s reflected a growing regional consensus favouring trade liberalisation, as expressed through Asia Pacific Economic Cooperation, APEC, and ASEAN Free Trade Area, AFTA, resolutions.

The chapter also identifies opportunities for Australia, through Indonesia's market opening, and concludes by assessing the risks associated with current liberalisation efforts.

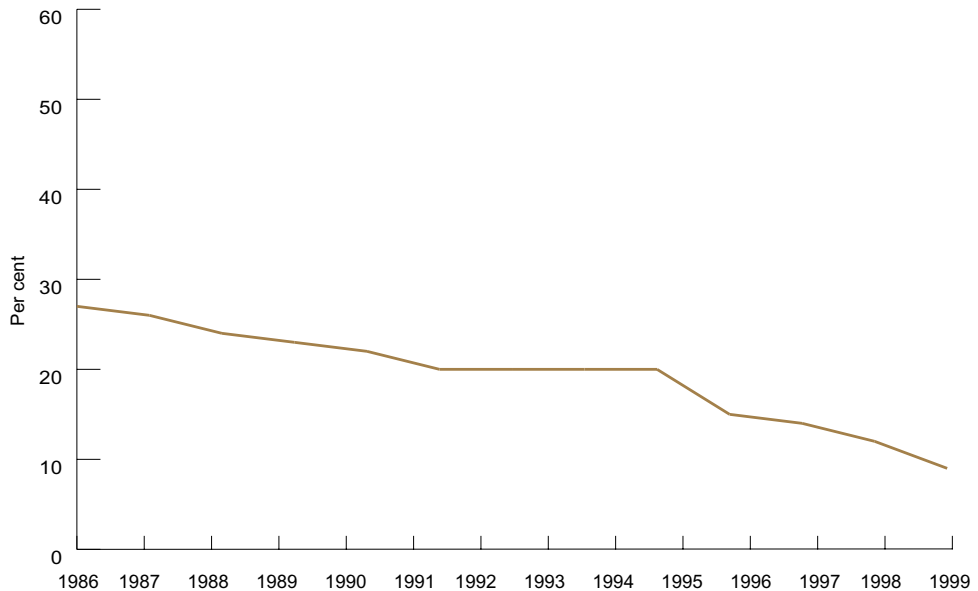
CRISIS AND REFORM

Trade barriers have declined markedly over recent decades due to consecutive reform efforts. The 1997 financial crisis promoted bold trade liberalisation. While other regional governments also are adopting freer trade arrangements, Indonesia currently has one of East Asia's most liberal trade regimes, outside Hong Kong and Singapore.

Crisis-led Reforms

Indonesia's first major trade reforms occurred in 1985 when falling oil prices and concerns about its high cost economy resulted in the Soeharto Government lowering tariff ceilings to 60 per cent and reducing the number of tariff levels from 25 to 11. These reforms also converted several import licences, which at their peak covered 43 per cent of tariff lines, into tariff equivalents (Centre for Strategic and International Studies, 2000). The 1985 recession and 1986 collapse of oil prices prompted more aggressive trade reforms, which reduced the unweighted tariff rate from 27 per cent in 1986 to 20 per cent in 1991 (Figure 4.1). Other reforms abolished import monopolies for plastic, steel and cotton, and introduced a more transparent quota system for textiles. In 1990, the Government also reduced non-tariff barriers to electronics imports, and removed import bans on cold rolled steel, sheets and tin plates. These reforms underpinned Indonesia's rapid economic growth in the late 1980s and 1990s.

Figure 4.1

Major Liberalisation in Late 1980s and Late 1990s^a**Unweighted Average Tariff Rate, 1986-1999**

Note: ^a 1987 and 1998 were interpolated from adjusted years' data.

Source: Centre for Strategic and International Studies 2000.

However, through the early 1990s, trade liberalisation slowed and the unweighted tariff rate remained steady. Propylene and ethylene tariffs increased and the national car, the Timor, was made exempt from the 35 per cent domestic luxury tax and protected by extensive non-tariff and tariff barriers. These developments fuelled doubts about the resolve of the Soeharto Government to continue trade reform.

By the mid 1990s, concerns about Indonesia's deteriorating external trade balance spurred renewed liberalisation, and the unweighted average tariff rate again declined (Figure 4.1). Importantly, in 1995, the Government committed for the first time to a schedule of tariff reductions; this anticipated a maximum tariff rate of 10 per cent by 2003, excluding automotive related products, and tariffs on most items falling to between 0 and 5 per cent (Table 4.1). Successive packages substantially reduced non-tariff barriers; by 1995, tariffs covered 65 per cent of items.

Table 4.1

Major Tariff Reforms Promised in 1995
Tariff Reduction Commitments, 1995-2003

Tariff before	May 1995	1995	1996	1997	1998	1999	2000	2001	2002	2003
5	5	5	5	5	5	5	max 5			
10	5	5	5	5	5	5	max 5			
15	10	10	5	5	5	5	max 5			
20	15	15	10	10	5	max 5				
25	20	15	15	10	10	10	10	10	10	max 10
30	25	20	20	15	15	10	10	10	10	max 10
35	30	25	25	20	20	15	15	10	10	max 10
40	30	25	25	20	20	15	15	10	10	max 10

Source: Indonesian Ministry of Trade and Industry quoted in Centre for Strategic and International Studies, 2000.

In July 1997, in line with previous unilateral announcements and to meet World Trade Organization, WTO, and APEC commitments, the Government again reduced tariffs on 1 600 items, lowering the unweighted tariff rate to 11.7 per cent. Over 50 per cent of Indonesian tariff codes then were within the 0 to 5 per cent range, and over 60 per cent were at 10 per cent or less (Table 4.2). The Government also removed a series of non-tariff barriers, including on new and used shipping imports.

Table 4.2

Trade Reforms Accelerate Post Crisis
Indonesia's Import Tariff Structure, 1997-99

Tariff	0 to 5 per cent	0 to 10 per cent	0 to 20 per cent	25 to 35 per cent	40 per cent or higher	Total tariff lines
July 1997						
Total tariff lines	3 688	4 563	6 151	1 032	80	7 263
Per cent	51	63	85	14	1	100
1998						
Total tariff lines	4 266	5 188	6 973	167	72	7 212
Per cent	59	71	96	2	1	99
1999						
Total tariff lines	4 289	5 226	7 055	135	69	7 259
Per cent	59	72	97	2	1	100

Source: Asia Pacific Economic Cooperation, 1999.

TRADE LIBERALISATION SINCE THE CRISIS

Responding to the financial crisis, the Government further accelerated trade regime reform efforts, especially eliminating non-tariff barriers for agricultural products and measures to protect the national car. The rupiah's dramatic 80 per cent depreciation in the year to mid 1998 made most Indonesian products very competitive at world prices, so many trade barriers became redundant. As the rupiah was unlikely to rebound quickly, the crisis offered an opportunity to remove many remaining trade barriers. Indonesia now is moving towards a liberal trade regime similar to that of Singapore or Hong Kong in the 1960s and 1970s.

These developments clearly benefit Australia as lower tariffs offer Australian exporters better access to the Indonesian market.¹

Tariff Reductions since the Crisis

Building on Indonesia's WTO and APEC commitments, the four-year IMF program recommended a three-tier tariff structure by 2003, with rates of 0, 5 and 10 per cent for all items except cars and alcohol. The Government committed to reducing immediately high tariff rates on some items not previously slated for liberalisation, including reducing tariffs of 15 to 25 per cent on iron and steel by 5 percentage points to reach 10 per cent by 2003. It also committed to reduce tariffs on chemical, metal and fishery products to 5 to 10 per cent by 2003.

By mid 2000, 60 per cent of tariff lines had tariffs of 0 to 5 per cent, and more than 70 per cent had tariffs of 10 per cent or less; this reduced the unweighted average tariff rate to below 9 per cent (Figure 4.1 and Table 4.2).

Post crisis, the Government also extended earlier programs to reduce tariffs on agricultural products; this lowered the unweighted average tariff rate on agricultural products from 19 per cent in 1995 to 8.6 per cent in 1998. Tariffs on food-related agricultural products fell to 0 to 5 per cent and non-food agricultural tariffs fell by 5 percentage points from prevailing levels. By 2002, the maximum tariff on non-food agricultural products will be 10 per cent.

As major exporters of agricultural products and manufactures to Indonesia, Australian producers will benefit from tariff reductions (Table 4.3).

Tariff reductions behind schedule

Despite these successes, actual tariff reductions are behind targets set in the May 1995 trade liberalisation package. Even after the December 1999 trade reform package, which reduced rates on 232 tariff lines, 2 142 lines remain above the 1995 target.

¹ Foreign suppliers should observe newly established anti-dumping measures in Indonesia.

Table 4.3

Few Barriers to Australian Exports
Tariff Rates on Major Indonesian Imports from Australia, 1999-2000

Item	Export value 1999-2000 (A\$ million)	Tariff rate (per cent)
Confidential items (mainly wheat)	560.2	na
Cotton	390.0	0
Aluminium alloys and aluminium ingots and products	139.8	0 to 20 depending on level of processing
Live animals	106.9	0 (5 if over 350 kg)
Iron and steel milling equipment	39.8	5
Frozen bovine meat	37.6	5
Zinc	32.9	5
Woodchips (not conifers)	23.6	0
Passenger motor vehicles	22.4	35 to 80, see box
Milk powder	21.8	5
Petroleum oils and products	39.1	0 (crude), 5 (refined)
Flour	20.9	0
Mining machinery parts	19.7	0
Motor vehicle parts	19.1	15
Copper cathodes	18.0	0

Note: na Means not available.

Source: Department of Foreign Affairs and Trade, 2000.

Non-tariff Barriers

Before the crisis, trade reform somewhat neglected non-tariff barriers. Some barriers prevented or severely limited the importing of certain items. Since the onset of the crisis, the Government has removed many of these barriers, especially exclusive licences for importers of agricultural products. The Government has announced it will remove all remaining non-tariff barriers by 2002, except those relating to health and environmental concerns. Removal of these barriers will significantly enhance local investment and production efficiency, and present Australian producers with significant opportunities.

Licensing requirements

In early 1998, the Government committed to removing all import licences, including agricultural import licences, which fell outside previous WTO commitments. The complexity of these licences impeded exporting to Indonesia, and monopoly import arrangements often raised domestic prices.

IMPROVED ACCESS FOR CAR EXPORTS

Government reforms have improved significantly foreign producers' access to the Indonesian car market, despite an exemption for car imports under the three-tier tariff structure targeted for 2003. The June 1999 automotive deregulation package substantially cut tariffs on completely knocked down, CKD, and completely built up, CBU, vehicles from 5-200 per cent to 0-80 per cent (Table 4.4). In early 1998, the Government also abolished special tax, customs and credit concessions to the national car project, implementing ahead of schedule the WTO panel ruling on this case. In addition, by the end of 2000, the Government agreed to phase out the motor vehicle local content program that gave preferential tariff rates to manufacturers using a high percentage of local parts.² As the economic recovery gathers momentum, Australian manufacturers of vehicles and automotive parts will be well placed to access the opportunities these reforms provide.

Table 4.4

Reforms Drive Vehicle Tariffs Lower

Tariff Reductions on Vehicle Imports since June 1999

	Tariff rates			
	Completely built up, CBU		Completely knocked down, CKD	
	Old	New	Old	New
Sedans less than 1500 cc	200	65	65	35
Sedans 1500 cc-3000 cc	200	70	65	40
Sedans higher than 3000 cc	200	80	65	50
Minibuses	105	45	25	25
Jeeps	105	45	25	45
Buses	70	40	25	25
Trucks with GVW less than 24 tons	70	40	25	25
Trucks with GVW higher than 24 tons	5	5	0	0

Source: Centre for Strategic and International Studies, 2000.

The Government agreed to liberalise the importing of many items, including agricultural commodities that previously only government agencies imported, and industrial inputs, including polystyrene and polyethylene.³

² These policies complemented the June 1999 abolition of the national car program and local content scheme for automotive products.

³ In both cases, only state owned producers could import these.

After November 1997, the Government removed import licensing requirements on commodities the national logistics agency, BULOG, controlled. This liberalisation permitted import competition for wheat, wheat flour, soy beans and garlic, the sale and distribution of flour, and the importing and marketing of sugar. This major reform should reduce prices of these commodities for consumers, and has obvious benefits for Australian exporters.

In late 1998, the Government opened rice imports to competition. However, in January 2000, because of the sharp fall in world rice prices, the Government placed a temporary Rp. 430 per kilogram import tariff on rice to protect local farmers' incomes; this is due for review in 2001 (International Monetary Fund, 2000a). As a regional exporter of rice, Australia is well positioned to take advantage of this liberalisation.

To smooth the transition to a fully open market, tariffs replaced import licences on some products, including for soy beans and dried garlic (which have a 20 per cent tariff) and wheat flour (which has a 10 per cent tariff). These tariffs are slated to fall to 5 per cent or less by 2003. A 25 per cent tariff on sugar also should be phased out by 2003.

In January 1998, the Government dismantled controls on wood panel exports and shipments, and on dairy product imports; these are markets in which Australia is very competitive. The Government also disbanded Badan Penyangga dan Pemasaran Cengkeh, BPPC, and its monopoly over the domestic marketing and distribution of cloves.

As part of the June 1999 automotive deregulation package, the Government permitted general importers to import completely built up vehicles. Given Australia's increasing success in exporting cars, this represents a major opportunity for Australian vehicle manufacturers.

Local content requirements

In addition to reforms in the car market, in February 1998, the Government announced the phasing out of local content requirements for dairy products, well ahead of Indonesia's commitment under the Uruguay Round, again offering opportunities for Australian exporters.

REGIONAL TRADE LIBERALISATION

Indonesia's participation in multilateral trade groupings, including the WTO, AFTA and APEC, also influences the pace of Indonesian trade liberalisation.

WTO COMMITMENTS

Indonesia joined GATT in 1947, but like other developing economies, was not actively involved in GATT negotiations until 1986. In the Uruguay Round, Indonesia offered trade liberalisation commitments including binding new tariffs (Appendix Table 4.1). It bound 6 714 tariffs or 72 per cent of all manufactured import tariff lines, agreed to eliminate quantitative restrictions, opened up trade in services and liberalised foreign direct investment by offering to apply national treatment by 2000.

GOVERNMENT REVIEWING INCENTIVES FOR EXPORTERS

Before the crisis, the Government offered exporters incentives to locate within the Batam Island, Rempang and Galang special economic zones, by exempting all products produced and imported there from value added tax and import duties. These concessions, and the zones' proximity to Singapore, attracted significant foreign direct investment; this rose from US\$684 million in 1990 to US\$2 332 million in 1999. Exports from the region increased from US\$568 million in 1992 to US\$3 152 million in 1998, with non-oil exports increasing through the crisis years. Because of concerns about the fiscal cost of these concessions, in July 1999, the Government indicated it would commission a comprehensive study to review the tax free status of Batam, Rempang and Galang islands.⁴ However, objections by Batam residents and businesses delayed the removal of the tax exemptions to the beginning of 2001, at the earliest.⁵

The Government also has reviewed tariff exemptions for all capital equipment, machinery and raw materials for businesses in export processing zones or export-oriented manufacturing entrepots. This scheme was based on firms' self assessment of imported value, and despite random government audits, was prone to corruption. In January 2000, the Government committed to remove all such import duty exemptions by May 2000. However, this equipment only carries a 5 per cent import duty.

Source: Centre for Strategic and International Studies, 2000.

However, Indonesia was disappointed by relatively limited concessions western economies offered to liberalise the Multi Fibre Agreement, and many of Indonesia's tariffs were bound at well above existing applied levels.⁶ Other concessions Indonesia made were relatively modest compared to previously announced unilateral trade liberalisation.

Indonesia started implementing Uruguay Round tariff commitments to reduce general tariff schedules in June 1996 (World Trade Organization, 1998). By 2000, Uruguay Round commitments had reduced the maximum applied tariff to 15 per cent (Table 4.1). Indonesia also committed to removing 96 non-tariff barrier measures, meeting its remaining Uruguay Round non-tariff barrier commitments by 2004, although post crisis reforms supersede many of these.⁷ These involved simplifying import licensing and gradually eliminating producer-importer and trade-importer licensing.

⁴ These were signed on 22 July 1999 and 20 January 2000.

⁵ In January 2000, the Government also announced it would remove all tax exemptions currently applying to the integrated economic development zones, KAPET, especially income and indirect tax concessions (International Monetary Fund, 2000a). Businesses within KAPET no longer will receive duty exemptions on their import of capital goods, raw materials and other equipment directly related to production activities. Value added tax and luxury sales taxes on domestic purchases also are applied now.

⁶ Australia is not a member of the Multi Fibre Agreement and hence does not use it to restrict clothing and textile imports.

⁷ By April 1996, Indonesia had eliminated 75 non-tariff barriers, 77 per cent of its Uruguay Round commitments, and by June 1996, had abolished 83 non-tariff barriers, over 80 per cent of its commitments. Indonesia will continue to reduce export taxes on logs, sawn timber, rattan and minerals to achieve these goals.

AFTA

At the fourth ASEAN summit in 1992, the six ASEAN economies, Brunei, Indonesia, Malaysia, Philippines, Singapore and Thailand agreed to establish the ASEAN Free Trade Area, AFTA.⁸ Since 1992, Vietnam, Laos, Cambodia and Myanmar have joined ASEAN and AFTA. AFTA aims to achieve free trade among the ASEAN economies, reducing intra ASEAN tariffs to 0 to 5 per cent and removing non-tariff barriers by 2002.⁹ ASEAN members regard AFTA as complementing WTO and APEC trade and investment liberalisation commitments, not substituting for them.

AFTA tariff reductions only apply to tariff items ASEAN members designate as 'included'. Included items carry the common economic preferential tariff; initially, this comprised 41 147 tariff lines, with 3 321 tariff lines placed on a temporary exclusion list and another 523 tariff lines permanently excluded on the general exception list.¹⁰ Since then, the inclusion list has increased to 53 144 tariff lines, covering 83 per cent of tariff lines. Unprocessed agricultural products were included in 1994.

AFTA helped increase regional integration and intra ASEAN trade from 19 per cent of ASEAN trade in 1992 to 25 per cent in 1997. The crisis has not reduced commitment to AFTA, although recently, Malaysia indicated it would exclude its car tariffs from common effective preferential tariff, CEPT, reductions.¹¹

The success of AFTA also inspired ASEAN members to strengthen, streamline and harmonise non-border measures to facilitate intra ASEAN and international trade and investment. For example, the 1995 Bangkok Summit Declaration agreed to enhance cooperation in liberalising trade in services, and synchronise national regulations to improve members' access to markets for financial services, maritime transport, telecommunications, air transport, construction and business services. In 1998, ASEAN members agreed on protocols to implement their 1995 trade in services liberalisation commitment. Indonesia, along with other ASEAN members, submitted details of service sectors it was ready to liberalise. However, little practical progress has occurred on services trade liberalisation; most ASEAN members are reluctant to move quickly in this sector.

⁸ Indonesia joined ASEAN in 1967, and since 1976, has participated actively in its economic cooperation.

⁹ Members agreed at the sixth ASEAN summit in 1998 to accelerate AFTA, achieving free internal ASEAN trade by 1 January 2002. This shortened the initial 2008 target.

¹⁰ Submitting products for liberalisation under AFTA is voluntary. When AFTA was first initiated, all members submitted their lists of products under each category: included, temporarily excluded and general exception lists, based on each member's willingness to liberalise. Items under the temporary exclusion list initially included sensitive products such as paper and paper products, transport equipment, including motor vehicles, iron and steel, certain electrical products and petroleum products. They gradually were phased into the included list between January 1996 and January 2000, in five equal instalments of 20 per cent of the list.

¹¹ In 1999, the AFTA Council agreed to implement AFTA according to schedule.

AFTA Commitments

By January 2000, Indonesia had 7 173 tariff lines in the CEPT inclusion list, leaving 21 tariff lines in the temporary exclusion list, four on the sensitive list (mostly unprocessed agricultural products, such as rice, sugar, tobacco and meat products) and 68 on the general exception list.¹²

Indonesia's original CEPT-AFTA schedule was similar to its Uruguay Round commitments. However, in 1998, ASEAN economies agreed not to apply tariffs over 20 per cent to products on the inclusion list; this was more liberal than Indonesia's Uruguay Round commitment (Table 4.5). By 2000, with the 1998 CEPT package and IMF liberalisation, Indonesia's average CEPT tariff was below 5 per cent, hence falling within AFTA's target band two years ahead of schedule. AFTA included items now represent 98.7 per cent of all Indonesian tariff items.

Table 4.5

Indonesia Ahead of AFTA Liberalisation Schedule CEPT-AFTA Tariff Reduction Schedule, 1995-2003, Per cent

Tariff before 23 May 1995	1995	1998	2000	2003
5	5		max 5	max 5
10	5		max 5	max 5
15	10		max 5	max 5
20	15		max 5	max 5
25	20	max 20		max 10
30	25	max 20		max 10
35	30	max 20		max 10
40	30	max 20		max 10
Average CEP Tariff (2000-03)	2000	2001	2002	2003
Indonesia	4.77	4.36	3.73	2.16

Source: Centre for Strategic and International Studies, 2000.

¹² AFTA has four categories of products. Firstly, Inclusion List products are subject to preferential tariff reductions and should reach 0 to 5 per cent in 2002. Secondly, Temporary Exclusion List products are temporarily excluded from the tariff reductions schedule but items in it should be phased into the Inclusion List in five instalments. Thirdly, Sensitive List products are declared sensitive, mainly unprocessed agriculture products such as rice, sugar, tobacco and meat products, and will take longer to be phased into the Inclusion List. Fourthly, General Exception products excluded mainly to protect human, animal or plant life, or artistic, historical or archaeological values and for national security and public morality reasons; examples include arms, ammunition and narcotics.

APEC TRADE LIBERALISATION

APEC's goals are to achieve free and open trade and investment by 2010 for developed member economies, and by 2020 for developing member economies. In contrast to WTO and AFTA agreements, which are legally binding, APEC agreements are based on consensus and are not legally binding. In its 1999 individual action plan, Indonesia committed itself to further liberalise trade and investment, progressively reducing tariffs to achieve the APEC goal by 2020 (Table 4.6). It also committed to reducing progressively non-tariff barriers, simplifying import licensing, and harmonising customs and other procedures to facilitate trade (Yamazawa, 1997).

Table 4.6

APEC Reforms Reflect Ongoing Liberalisation Summary of Indonesia's APEC Individual Action Plan

Area	Current status	Short term	Medium term	Long term
Tariffs	Indonesia announced a schedule of tariff reductions on a most favoured nation basis for each year between 1995 and 2001 to reduce: <ul style="list-style-type: none"> tariffs of 20 per cent or less in stages to 0 to 5 per cent by 2000 1995 tariffs of more than 20 per cent in stages to 0 to 20 per cent by 1998, and to 0 to 10 per cent by 2001. 	Indonesia will continue to reduce its tariffs on a most favoured nation basis until 2001, in line with its schedule of tariff reductions. Indonesia will actively participate in the APEC tariff database and regularly update its tariff data.	Indonesia will continue its deregulation efforts to further liberalise trade and investment, and progressively reduce tariffs.	Indonesia will progressively reduce tariffs to reach the APEC free trade goal by 2010-2020.
Non-tariff measures	Indonesia has already eliminated 75 non-tariff barriers which are 77 per cent of its Uruguay Round commitments. In June 1996, it eliminated nine non-tariff barriers; eight belonged to the Uruguay Round commitments.	Indonesia will continue to reduce export taxes on logs, sawn timber, rattan and minerals to achieve APEC goals. It will continue to eliminate by 2004, the remaining non-tariff barriers that are part of its Uruguay Round commitments, and will continuously update its non-tariff measures data in the APEC tariff database.	Indonesia will progressively reduce non-tariff measures, and further simplify import licensing. Indonesia gradually will eliminate producer-importer and trade-importer licensing, except where it is justified.	

Source: Asia Pacific Economic Cooperation, 1999.

POLITICAL OBSTACLES TO TRADE LIBERALISATION

Trade reform may threaten significant existing interests in industries like broadacre agriculture, iron and steel, petrochemicals, flour milling, sugar and transport equipment, as Indonesia is less internationally competitive in these sectors. These interests have sought to rally government support and nationalist sentiments to retain trade barriers. While democracy has weakened the influence of some vested interests, import competing constituencies, including farmers and capital intensive manufacturers, still seek to influence trade policy outcomes.

In particular, liberalisation of certain agricultural commodity imports arouses considerable opposition. For example, rice farmers concerned about the market penetration of lower cost, foreign rice called for rice tariffs to jump from 30 per cent to between 90 and 120 per cent. Sugar industry representatives also argued the 20 to 25 per cent tariff on sugar was too low compared with some developed country tariffs of 140 to 240 per cent (*Bisnis Indonesia*, 30 May 2000).¹³

Steel industry representatives, led by state owned Krakatau Steel, argue strongly to maintain indefinitely steel tariffs at 25 per cent, claiming Japanese, Chinese and Korean imports often are dumped (Centre for Strategic and International Studies, 2000). The Indonesian Association of Steel Pipe Producers, GAPIPA, also is calling for an anti-dumping duty on steel pipe imports (*Jakarta Post*, 5 April 2000). The petrochemical industry, led by Chandra Asri, the country's largest ethylene producer, continues to oppose trade liberalisation, seeking to maintain indefinitely its tariff at 25 per cent (*Jakarta Post*, 10 May 2000).

Even labour intensive manufacturers like the Indonesian Footwear Association, APRISINDO, demand import duties on Chinese footwear, again because of suspicions of dumping; despite rupiah depreciation, prices for Chinese footwear are 25 per cent lower than domestic prices. The Indonesian Antidumping Committee, KADI, currently is investigating the issue.¹⁴

RECENT TRADE TRENDS

Trade reforms throughout the 1980s and 1990s drove rapid trade growth; exports grew from 23 per cent of GDP in 1985 to 35 per cent in 1999. In most years, net exports (exports minus imports) significantly contributed to Indonesian GDP growth. The Indonesian Government recognises the importance of net exports to sustaining medium term economic growth. Before the crisis, Indonesia had run trade deficits but by the September quarter of 2000, Indonesia enjoyed a trade surplus equal to around 11 per cent of GDP.

¹³ Four Java based sugar cane farmer associations and members of Asosiasi Petani Tebu Rakyat expressed these concerns in May 2000. However, their proposal to ban raw sugar imports was rejected (*Republika*, 4 May 2000). In April 2000, at the regional multilateral level, the Asian Farmers Group for Cooperation demanded the WTO respond to its demands for greater agricultural protection, especially on key staples including rice (*Suara Karya*, 19 April 2000).

¹⁴ The Minister for Trade, Luhut Pandjaitan announced an investigation into ways to curb Chinese imports, where unfair business practices or smuggling is evident. He emphasised that any measures must not disturb bilateral relations between the two countries (*Jakarta Post*, 29 June 2000).

Export Trends

By late 2000, the low rupiah, improving trade finance for established exporters and recovering oil prices were driving a rapid recovery in Indonesian exports. Export volumes rose 17 per cent in the third quarter of 2000 over a year earlier (Figure 1.3). Exports bottomed at US\$48 billion in the year to July 1999 but rebounded to almost US\$60 billion in the year to September 2000 (Figure 1.4) (CEIC, 2000). This is 17 per cent above pre-crisis export levels of about US\$51 billion. A competitive currency and continuing strong oil prices are expected to boost exports at least a further 7 per cent in 2001 (Consensus Economics, 2000).

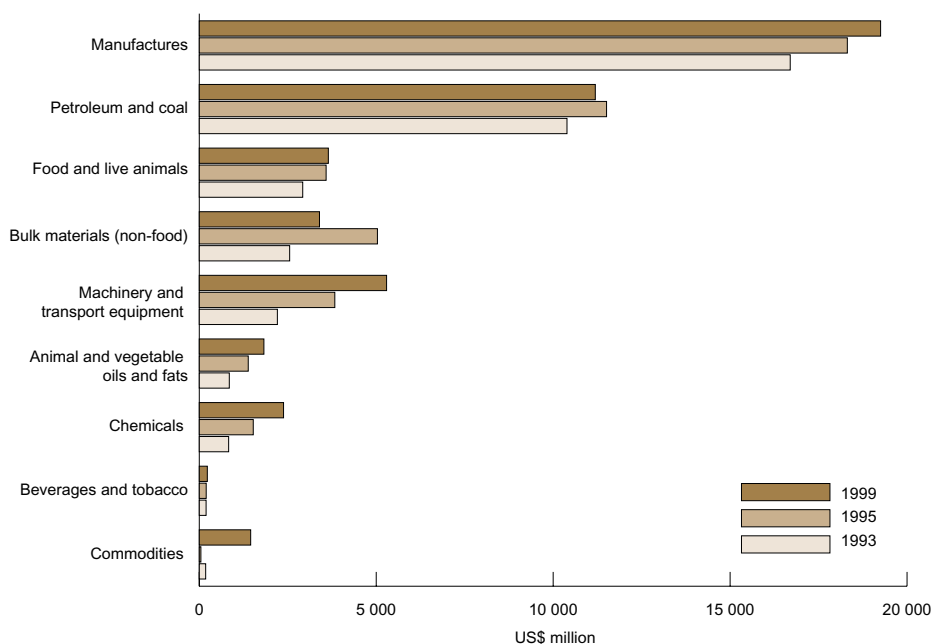
Excluding oil, between 1995 and 1999, the fastest growing major exports were chemicals, up 11.5 per cent to US\$2.3 billion, machinery and transport equipment, up 6 per cent to US\$5.3 billion, and vegetable oils and fats, up 5.3 per cent to US\$1.8 billion (Figure 4.2).

Oil prices over US\$30 per barrel will see oil export revenues increase to US\$7.7 billion in 2000, up from only US\$2.8 billion in 1998, when oil averaged US\$12.18 per barrel.¹⁵

Figure 4.2

Manufactured Exports Growing Strongly Post Crisis

Indonesia's Principal Exports 1993, 1995 and 1999, US\$ million



Source: CEIC, 2000.

¹⁵ This estimate uses the average August 2000 spot price for Minas (Sumatran) crude, compared with the 1998 Dubai average price, which is the marker price for East Asian oil prices. Export volumes are assumed to remain the same; 630 000 barrels per day, although higher prices and demand may induce higher supply (International Energy Agency, 2000; and United States Department of Energy, Energy Information Administration, 2000).

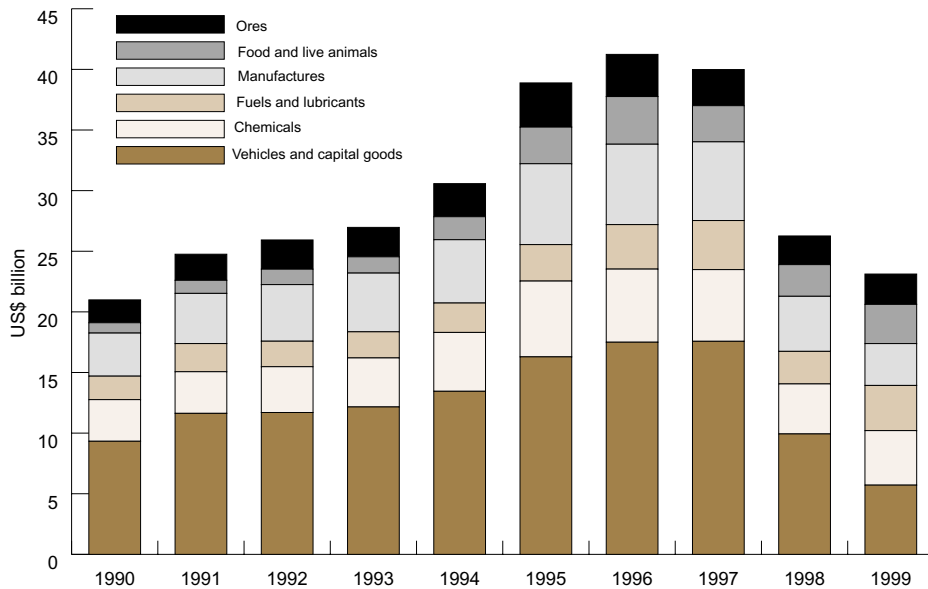
Merchandise Import Trends

By late 2000, imports also were recovering slowly. During the crisis, much of the adjustment in Indonesia's balance of payments came through imports, which bottomed at US\$24 billion in the year to December 1999, down from their peak of almost US\$44 billion in the year to March 1997 (Figure 1.4).¹⁶ Capital goods and cars led the decline (Figure 4.3). However, reflecting the recovery in exports and domestic consumption in the year to September 2000, imports rose almost 16 per cent over a year earlier. Despite this increase, in September 2000, imports were still 34 per cent below pre-crisis peaks at US\$28.8 billion (Figure 1.4).

Figure 4.3

Capital Goods and Cars Dominate Imports but Plunge during Crisis

Indonesia's Principal Imports, 1990-99



Source: CEIC, 2000.

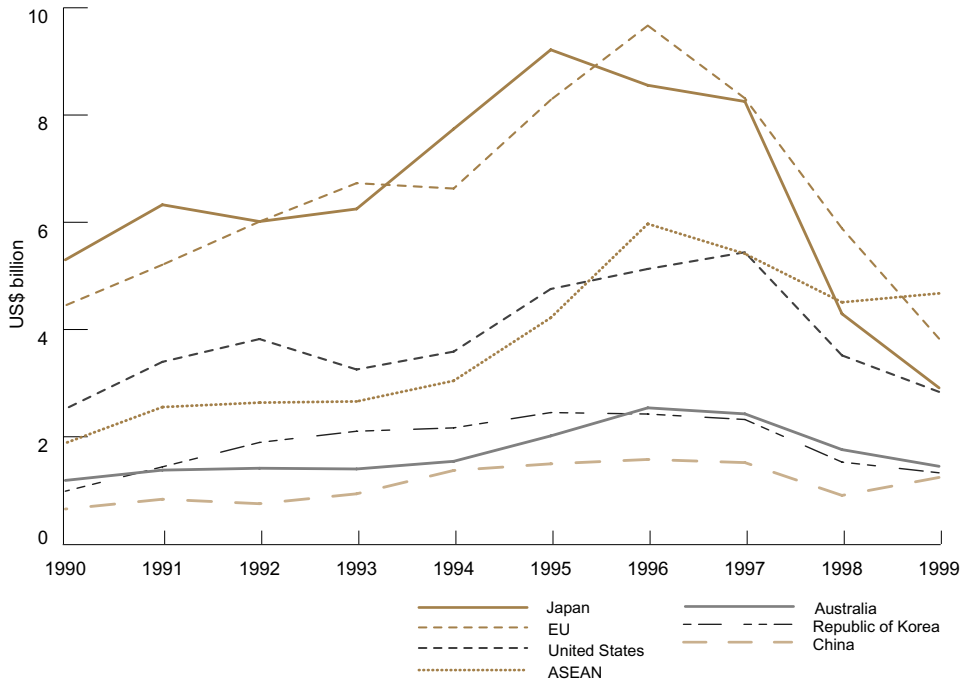
Indonesia's major import suppliers, Japan and the European Union, saw their annual exports to Indonesia fall by 65 and 54 per cent respectively between 1997 and 1999. Partially due to depreciation of several of these currencies, and the composition of their exports, imports from ASEAN, China, the Republic of Korea and Australia experienced more modest declines (Figure 4.4). ASEAN exports to Indonesia fell by just 14 per cent, China's by 19 per cent, Australia's by 41 per cent and the Republic of Korea's by 43 per cent. However, all countries' exports to Indonesia are recovering in 2000. (See Chapter 5 - *Australian Opportunities*.)

¹⁶ Capital goods imports fell by 67 per cent from US\$17.5 billion in 1997 to US\$5.7 billion in 1999. Manufactures also fell 57 per cent over the same period, from US\$6.5 billion to US\$3.5 billion. This decline parallels the fall in investment. Other imports, particularly inputs for the export sector, fell less markedly; chemicals fell by 24 per cent, and ores and other crude materials fell by 14 per cent.

Figure 4.4

Japan and EU Exports Suffered Most

Imports Supplied by Indonesia's Largest Import Suppliers, 1990-99



Source: CEIC, 2000.

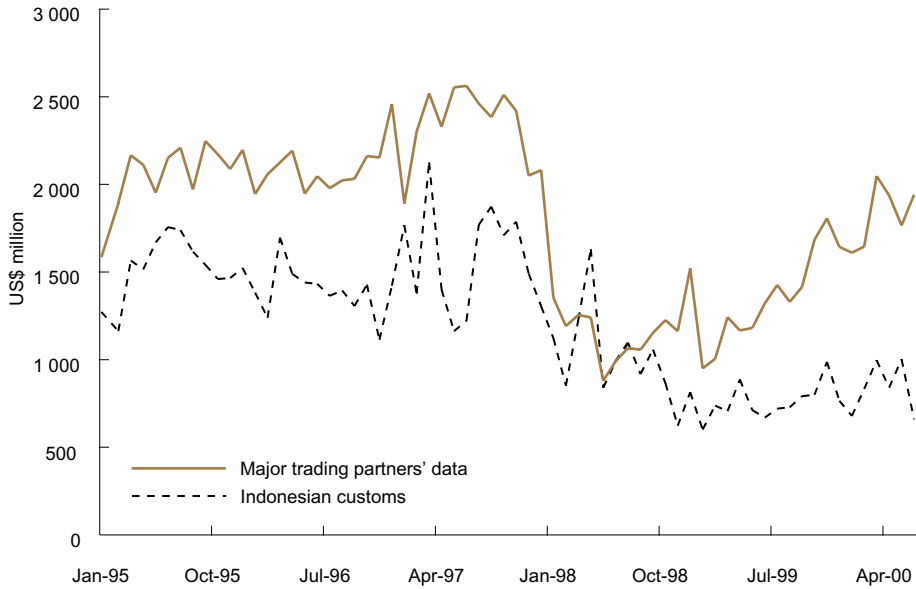
Indonesia's Missing Imports Signal a Free Trade Zone Boom

Although official Indonesian Customs Department data (which, in general, exclude duty free imports by free trade zones) show imports fell from mid 1997 to January 1999, major trading partner data show imports began to increase from April 1998, and have almost doubled since. The significant discrepancy between official and partners' trading data has widened since the crisis (Figure 4.5) (World Bank, 2000). Import categories with the most pronounced difference between official and partners' import data are products used in export processing zones, such as textiles, electronics parts and machinery for specialist industrial applications; bulk commodities, ores and motor vehicles, which typically are not imported to duty free zones, do not exhibit this gap. This supports the hypothesis that the widening import data gap is due to the increasing importance of export processing zones as a destination for Indonesia's imports.

Figure 4.5

Widening Gap between Official and Partners' Import Data

Imports Data from Indonesian Customs and Indonesia's Trading Partners



Source: World Bank, 2000.

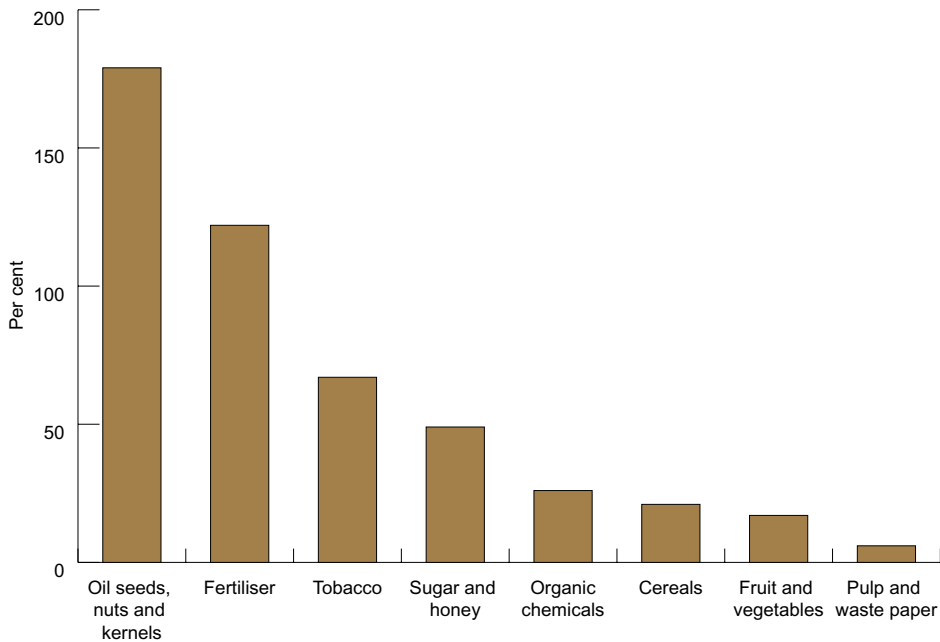
Turning the Corner in 1999 and into 2000

Some of the fastest growing import categories in 1999 included agricultural inputs such as seeds and fertilisers (122 per cent), cereals (21 per cent), metallic ores and scrap (21 per cent), transport equipment excluding cars (16 per cent), and pulp and waste paper (6 per cent) (Figure 4.6). Over 2000, imports of manufactures and crude materials recovered also, in line with the recovery in consumption and exports.

Figure 4.6

Some Imports Surging

Selected Fast Growing Imports, US dollars, 1998-99



Source: International Economic Data Bank, 2000.

Implications

Indonesia has achieved major trade reforms since the crisis, building on liberalisation over the past two decades and moving it rapidly towards its free trade objective. These reforms will assist greatly Indonesia’s growth prospects as it recovers from the crisis, reducing costs for producers and consumers, and encouraging efficient allocation of new investment. Significant tariff and non-tariff liberalisation also will improve market access for Australian exporters supplying the Indonesian market. However, as trade liberalisation focuses on more sensitive and less competitive sectors, resistance to further reform is emerging. Australia’s experience with trade reform indicates failure to explain adequately to the Indonesian public the benefits of free trade could threaten continuing trade liberalisation.

Appendix Table 4.1

Many Tariffs Bound, but at High Levels
Indonesia's Uruguay Round Market Access Offer

Tariff lines	Number	Per cent of tariff lines
A. Tariff binding		
1. Total bound manufactures	7 537	80.3
Existing bindings	823	8.8
New bindings	6 714	71.6
2. Total agriculture (all bound)	1 341	14.3
3. Exceptions	504	5.4
Total	9 382	100
B. Agriculture		
1. Tariffication and binding of all items		
2. Duty reduction of 10 percentage points by tariff line over ten years		
3. Elimination of local content requirement for milk products		
4. Agreed access of 70 000 tons of rice imports annually		
C. Removal of non-tariff barriers on bound tariff items		
Non-tariff barriers on 98 industrial tariff lines affecting A\$358 million of imports to be removed within ten years		
D. Elimination of import surcharges on bound tariff items		
Surcharges ranging from 5 to 25 per cent on 159 tariff lines affecting A\$838 million of imports to be removed within ten years		

Source: Indonesian Ministry of Trade and Industry quoted in Centre for Strategic and International Studies, 2000.

Appendix Table 4.2

Trade Related Policy Actions under the IMF Program

Policy action	Target date
Tariffs	
Reduce tariffs on items currently subject to tariffs of 15 to 25 per cent by 5 percentage points	31 March 1998
Cut tariffs on all food items to a maximum of 5 per cent	1 February 1998
Reduce tariffs on non-food agricultural products by 5 percentage points	1 February 1998
Gradually reduce tariffs on non-food agricultural products to a maximum of 10 percentage points	2003
Reduce tariffs on chemical products by 5 percentage points	1 January 1998
Reduce tariffs on steel/metal products by 5 percentage points	1 January 1998
Reduce tariffs on chemical, steel/metal and fishery products to 5 to 10 per cent	2003
Import restrictions	
Abolish import restrictions on all new and used ships	1 February 1998
Phase out remaining quantitative import restrictions and other non-tariff barriers	End of program
Export restrictions	
Abolish export taxes on leather, cork, ores and waste aluminium products	1 February 1998
Reduce export taxes on logs, sawn timber, rattan and minerals to a maximum of 30 per cent by 15 April 1998, 20 per cent by end of December 1998, 15 per cent by end of December 1999 and 10 per cent by end of December 2000	First step by 22 April 1998
Phase in resource rent taxes on logs, sawn timber and minerals	First step by 22 April 1998
Replace remaining export taxes and levies by resource rent taxes as appropriate	Over program period
Eliminate all other export restrictions	Over program period
Remove ban on palm oil exports and replace with export tax of 40 per cent. Review the level of the export tax based on market prices and exchange rates, and reduce to 10 per cent by end of December 1999	22 April 1998

Appendix Table 4.2 (continued)

Trade Related Policy Actions under the IMF Program

Policy action	Target date
Local content regulations	
Abolish local content regulations on motor vehicles	2000
Abolish local content regulations on dairy products	1 February 1998
Free trade zones^a	
Review the tax free status of Batam, Rempang and Galang Islands, based on a comprehensive feasibility study. Defer plans pending the completion of the study	Based on feasibility study completed by 31 August 1999
Review the effectiveness of policies for the integrated economic development zones, KAPETS, especially the fiscal concessions	Based on study completed by 31 December 1999
Start collecting value added tax from Batam Island	1 April 2000
Review whether to maintain the income tax facilities and abolish the indirect tax facilities for the integrated economic development zones	Complete review by 1 February 2000; implement measures by 1 April 2000
Value added tax	
Limit VAT zero-rating of domestically supplied goods to businesses in proportion to their exports	Upon implementing the new VAT law
Review VAT exemptions on specified capital goods, agricultural inputs and public services, and identify those that should be revoked to avoid cascading	30 September 1999
Prepare draft amendments to the VAT law to provide prompt refunds for all excess credits of exporters and enterprises purchasing large amounts of capital goods	1 March 2000
Eliminate VAT exemptions on capital goods	Upon implementing the new VAT law
Customs administration	
Prepare draft amendments to the customs law and issue implementing regulations to provide for penalties and interest on unpaid duties, and implement short, issue oriented audits	31 October 1999

Note: ^a Several of these target dates have been postponed.

Appendix Table 4.2 (continued)

Trade Related Policy Actions under the IMF Program

Policy action	Target date
Develop and implement a plan to combat valuation fraud by: <ul style="list-style-type: none"> • strengthening physical inspections • establishing special valuation units in the regions • undertaking special valuation audits • developing a valuation database to help detect fraud 	31 October 1999
Reduce exemptions to import tariffs on capital goods; rationalise and make transparent the remaining exemptions	1 April 2000
Dissolve restrictive marketing arrangements for cement, paper and plywood	1 February 1998
Eliminate price controls on cement	3 November 1997
Allow cement producers to export with only a general export licence	1 February 1998
Allow free traders to buy, sell and transfer all commodities, including cloves, cashew nuts and vanilla, across districts and provincial boundaries	1 February 1998
Eliminate the Clove Marketing Board	30 June 1998
Abolish quotas limiting the sale of livestock	30 September 1998
Prohibit provincial governments from restricting trade within and between provinces	1 February 1998
Enforce prohibition of provincial and local export taxes	January 1998
Take effective action to allow free competition in: <ul style="list-style-type: none"> • wheat, wheat flour, soy bean and garlic imports • flour sale or distribution • sugar imports and marketing • rice imports 	30 September 1998 30 September 1998 31 December 1998 Ongoing

Source: International Monetary Fund, 2000b.

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