



Indonesia and Europe: Entering a New Stage

Indonesia and the European Union have entered a new stage in their relationship. On 4 November, President Susilo Bambang Yudhoyono met with EU Commission President José Manuel Barroso and European Council President Herman Van Rompuy.

The Leaders applauded the rapid advance in Indonesia - European Union (EU) bilateral commercial and political relations, with two-way trade now exceeding €20 billion (of which almost 20% is conducted with the Netherlands) and the EU as the 2nd largest investment and export partner of Indonesia. Leaders also welcomed the recommendations of the EU-Indonesia Vision Group. One of these recommendations was to start talks on an ambitious Comprehensive Economic Partnership Agreement (CEPA). Leaders agreed that Ministers and officials should continue their work to improve the bilateral trade relationship, including the launch of talks in 2012 building on the work of the Vision Group.

Kadin and Apindo have both expressed their support to a CEPA. Europe and Indonesia do generally not compete with each other because they are strong in different sectors, so a free trade agreement would benefit both sides. By covering more topics than only trade, the CEPA could also support additional European investment in Indonesia.

The economic relationship between Indonesia and Europe is strong in numbers. Indonesian exports to Europe increased seven-fold in the last two decades. The EU however is losing market share in Indonesia to its competitors, notably China and Japan, but also the US. The share of the European Union in Indonesia's external trade has fallen from 16% ten years ago, to just over 10% now. Another interesting aspect of the relationship is investments. The EU is the second largest investor in Indonesia with an estimated total of 700 European companies established in Indonesia generating 500,000 jobs. This however only represents 1.6% of overall EU investments to Asia. Indonesia is also a production base for some large European manufacturers. Airbus has parts of its aircraft produced in Indonesia, pharmaceutical companies are exporting from Indonesia to the EU, and several European companies are having information technology products developed in Indonesia. European investment in Indonesia is however way behind European investment in some of Indonesia's neighboring countries such as Malaysia.

Some Sensitive Issues

There are a number of sensitive issues in the European-Indonesian economic relationship.

One example is palm oil. It is the most important export product from Indonesia to the EU and it goes to an amazingly wide range of food products and cosmetics. In much publicized decisions, a number of large international companies have suspended buying palm oil from PT Smart, one of Indonesia's largest palm oil producers. These decisions were taken after a report by Greenpeace found several environmental problems in their plantations, especially the planting of palm oil on soil with a too thick layer of peat, which contributes significantly to greenhouse gas emissions, and clearing forests without proper permits. PT Smart has since then taken steps to improve the situation and some buyers have resumed buying. Nevertheless, most large buyers in Europe have stated that by 2015 they want to buy only sustainable palm oil. However, much bigger damage is already done, as the negative publicity has created an anti palm oil sentiment in Europe. In France, some products have been labeled as "palm oil free", a label which Indonesia is now challenging in the WTO.

Activist groups in Europe sometimes seem more interested in scoring political points rather than in providing balanced information or contributing to a good solution.

Another issue is timber. Recently, the EU adopted the FLEGT legislation. With this legislation, all sellers of timber and related products have to prove, from 2013 onwards, that their timber is legal. This is not always easy in Indonesia to provide all the necessary documents. The EU has however recognized Indonesia's SVLK-system in a 'Voluntary Partnership Agreement'.



Coffee, fisheries and cosmetics are products in which the

European Union is the world's largest importer, but where Indonesian companies have difficulties in complying with European quality and food and personal care safety standards. These standards are however subject to some debate. In fisheries, for instance, the Indonesian Food and Beverages Association GAPMMI argues that the zero tolerance for antibiotics in shrimps which the EU applies is unrealistic. The EU is providing technical support to Indonesia to strengthen its export quality infrastructure, for instance providing laboratory capacity for food testing. Since some years the number of 'notifications' of food safety issues stemming from Indonesia has fallen sharply. This is evidence that Indonesia is able to comply with European standards.

In traditional natural medicines, a European Union Directive came into force on 1 May this year requiring that only traditional medicines which have been on the market safely for at least 30 years, of which 15 years in the EU, are allowed. This of course makes it impossible for new traditional natural medicines, of which Indonesia has a rich variety and which are high value products, to enter the European market.

Indonesia at times also takes decisions that hamper EU traders and investments. Often these come at a surprise as there is no process of stakeholders consultation or discussion until regulations are adopted. One example is the Horticulture Law issued last year, and which requires foreign investors to sell 70% of their ownership to Indonesian owners in the next four years. Requirements forcing foreign investors to sell the majority stake in their investment in Indonesia are also being considered in express and logistic services. Not only the investment regulations, but equally important, the bureaucratic approval procedures are frustrating foreign investors. In spite of improvements made in recent years, the attitude in the institutions involved in the approval process is still focused on exercising control rather than servicing investors.

From Multilateral to Bilateral Trade Policy

Multilateral trade negotiations in the World Trade Organization are still ongoing but seem not to deliver the results parties had hoped for. Another attempt will be made during a Ministerial meeting in Geneva next month, where the EU says it will try to save the package that was offered to the developing countries. However, during those last ten years the rest of the world has continued negotiating bilateral deals and the EU has decided that – in addition

to the multilateral discussions – bilateral negotiations will support liberalizing overall trade. Negotiations with Singapore, Malaysia and India are ongoing and other countries, such as Vietnam, Thailand and Brunei are interested. Similarly, Indonesia is currently talking with countries such as Australia, India and South-Korea.

Still, the concept of free trade agreements has become rather unpopular, after the China ASEAN Free Trade Agreement (CAFTA), which came into effect gradually but notably in 2010, led to a perceived influx of Chinese products. Indonesia was ill-prepared for this CAFTA and has started to doubt the benefit of any free trade agreement. One lesson learnt was that future agreements should be ‘socialised’ widely – so that local industry and other stakeholders can inform themselves and give feedback to the Government officials negotiating the deal. Indonesia and the EU worked closely together to ensure such socialization is taking place.

In addition, Indonesia – like the EU – aims for ambitious agreements which do not only cover trade but also investment and co-operation in areas like technology and infrastructure.

Towards a Comprehensive Economic Partnership Agreement

In June this year, the EU Indonesia Vision Group, a think tank of Europeans and Indonesians, presented its vision on how to strengthen the economic relationship. The most important recommendation was to start negotiating a Comprehensive Economic Partnership Agreement (CEPA) between the EU and Indonesia. The most important part of the CEPA, would be a reduction to zero of import tariffs on goods for 95% of tariff lines with at least 95% of the trade value, a substantial reduction of tariffs. Such a CEPA is expected to give a boost to Indonesia’s exports to Europe and to its economy.

The CEPA is estimated to generate US\$ 9.8 billion additional Indonesian exports to Europe and would add US\$ 6.3 billion to Indonesia’s GDP. However, the CEPA would not only liberalize trade, but would also have to cover investment and public procurement and as such provide much wider benefits, notably in employment and poverty reduction.

An agreement could include investment protection, as it is one of the new competences of the EU following the Lisbon Treaty.

Finally, the CEPA would also cover technical assistance to Indonesian companies that have difficulties in dealing with

the EU market access standards. This would mean that the EU would, for instance, provide funding for building and expanding quality control centres in Indonesia.

Time for Business to Raise its Voice

In the coming months, input will be collected from the business community in Indonesia and in Europe on what should be included in the CEPA. What are the product categories for which tariffs should be reduced, what are the technical barriers faced by companies exporting from Indonesia to Europe or from Europe to Indonesia, what agreements should be made on investment, public procurement, intellectual property rights protection and taxation, competition policy and customs ?

On 7 November, INA signed an important contract with the European Commission. With this contract, the European Commission provides funding to the European Chambers of Commerce in Indonesia and Kadin to work much more intensively on solving some of the major bottlenecks in the trade and investment relations between Indonesia and Europe. The European Chambers, which are the four bilateral Chambers BritCham, Ekonid, IFCCI and INA, and EuroCham, have already organized two Indonesian-European Business Dialogue conferences, one in Brussels in 2009 and one in Jakarta in 2010. A number of recommendations have been formulated for sectors like food products, textile, infrastructure and pharmaceuticals.

In this new co-operation program, the European Chambers will work more closely with Kadin and Apindo on solving the many complications that still exist in these and other sectors and which are having an impact on trade and investment between Indonesia and Europe. The Chambers will reach out to their members to get their input for the negotiations between Indonesia and Europe. INA members can submit their input on the INA website www.ina.or.id, under Indonesia-Europe.

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