POLICIES AND STRATEGIES TO IMPROVE MARKET ACCESS

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This policy brief is the result of an activity entitled "Economic Policymaking in Indonesia' which is jointly conducted by Centre for Strategic and International Studies (CSIS) and Economic Research Institute for ASEAN and East Asia (ERIA). This activity is a contribution from research community that is expected to assist the government in formulating more effective economic policies in the future. In this activity, CSIS and ERIA invited 16 economists with specific fields of expertise from some leading research institutions to conduct in-depth discussions on seven strategic issues facing Indonesian economy (infrastructure development, competitiveness, investment climate, food policy, services sector policy, fiscal policy, and social protection policy), which is then summarized into policy briefs covering each of the topics.

Dissemination of the findings and recommendations produced by this activity is conducted through several channels. First, this activity has made efforts to engage the relevant government officials through some Focus Group Discussions (FGD), the publication of High Level Policy Notes, and hearings with some strategic policymakers with regard to each of the strategic issues mentioned above. Secondly, this activity also conducts widespread public disseminations through Public Seminars on each of the strategic issues, along with publications of the Policy Briefs and supporting multimedia that can be accessed online through www.paradigmaekonomi.org.

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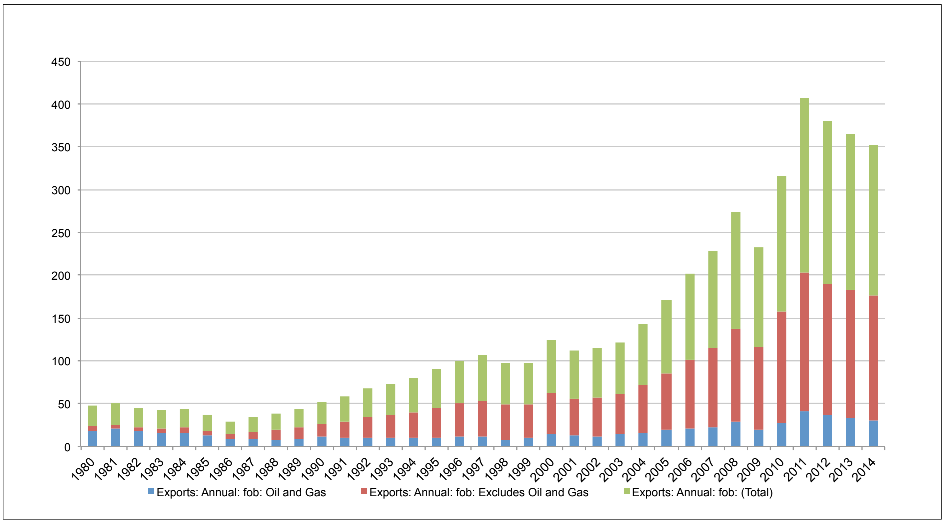
New strategies are needed to improve export performance. Noting that exporting involves sunk-cost, i.e. expenses that cannot be retrieved when exports are not realized., the government's role should be facilitating. ***Government of Indonesia needs to revisit its trade promotion strategies including the role and business model of its National Export Development Agency; allocate more resources for trade and trade promotion; and align its promotion strategies with new development in information and technology.***

EXPORTING IS AN IMPORTANT COMPONENT TO GROWTH

Indonesia's exports declined in the past few years. Currently, exports was about 24 percent of Indonesia's GDP with trade was about 45% of GDP relatively small compared to Vietnam with export share of 86% of GDP and total trade of 169% of GDP (World Bank, 2016). A number of studies show factors behind export decline includes the declining of commodity prices, real appreciation of Rupiah, high real wages and the bottleneck in the supply sides due to poor quality of infrastructure and logistics (Aswicahyono and Hill, 2014, World Bank 2014). However, export will remain an important component of Indonesia's growth. Although Indonesia is a large country with 250 million populations, its GDP was only 1 % of the world GDP in 2014, or if we use GDP at PPP, it s about 2.4% world GDP (IMF, 2015).[1] In additions, exporting is a reflection of the firm's and countries competitiveness as global players are usually the efficient and innovative firms.

Figure 1. Exports Performance, 1980-2014



1 Indonesia's economy size (about 889 billion USD), only 1% of world economy
The largest economy remains the US, China, Japan, Germany, UK etc (the ranking depends on what indicators we are using, conventional GDP or PPP GDP).

LESS DIVERSIFIED EXPORTS

Indonesia's exports was dominated by primary products and less diversified, both product and market wise (Basri and Rahardja, 2011,Presisi Indonesia, 2014, Bank Indonesia 2015) which make Indonesia's export vulnerable to shocks such as the decline in primary commodities' prices and weakening demand for imported goods in major markets.

SUPPLY SIDE CONSTRAINTS REMAIN

Besides, the supply side constraints, which have been the impediments to growth, were not yet addressed comprehensively. The quality of infrastructure in general and the logistic infrastructure in particular had contributed to the weakening of the manufacturing exports (Athukorala, 2006).

THE MOST PRODUCTIVE FIRMS INVEST ABROAD, THE LEAST SERVES DOMESTIC MARKET

Researches in the past showed the most productive firms engaged in investment abroad while the second most productive ones export while the remaining stay domestic (Helpman, et al, 2004 and Girma et al, 2005). Given that the most productive firms invest abroad, large domestic market should be a training ground to be a global player. The government should facilitate the growth of domestic firms by providing competitive environment to allow domestic firms develop as competitive firms which later on can be investors in global markets.

THE WAY FORWARD

With economic growth decelerating since 2009, an overhaul to economic strategy, export strategy in particular is needed. The weakening of the manufacturing sector needs to be addressed. With commodity prices decline and mining is highly politicized, it is important for government to facilitate the growth of the manufacturing and services sectors.

The current government begin to address the supply side constraints, although the significant outcome is yet to be seen. The issue is with the supply constraints been addressed to improve competitiveness (see Zen, Nurizki, Aswicahyono 2015). While the supply side constraints have been addressed, we might expect that cost of production and beyond the factory gate cost significantly lower and on time delivery can be expected.

Constraints in accessing export destination also need to be tackled. The government has been actively engaged in trade agreements (multilateral, regional and bilateral) as discussed in Rizal (2015) to maintain and improve market access in potential export markets. The expectation is that the government's engagement in trade agreements will improve market access (tariff and non tariff reduction).

Do we miss any elements to boost export performance? Presisi Indonesia (2015) shows that lack of information is among the reasons why our exports perform below its potential. Ensuring firms/exporters/potential export can access potential markets need additional elements, which might have received less attention so far but very crucial: policies and strategies to facilitate exports. This note highlights the importance of new policies and strategies to facilitate exporters/potential exporters to access potential markets. This policy notes emphasis on the facilitating role of government. We argue that the government needs to facilitate trade and reduce sunk cost to export.

LOWERING SUNK COST TO EXPORTS

Exporting is a totally different game to selling to domestic market. Supplying export market is totally different game from supplying domestic market. A number of firms, mainly small and medium firms we interviewed in the past, claimed that the firms did not bother to export when the domestic market (local market) is large enough for them to supply, as exporting is **riskier and costly than supplying domestic market.** Apart from tariff, which is relatively transparent, non-tariff such as technical standard, health and sanitary standard as well as import procedures in the destination differ from countries to countries and can be product specific as well. Exporters, particularly potential exporters need to collect all of this information prior to exporting. And this is sunk cost to exporters, once it is spent it cannot be retrieved when export not realized. Roberts and Tybout (1997) and Narjoko and Atje (2007) show that the sunk cost affects firms' decision to export. Sunk cost to export can be large, particularly entering markets with non-transparent regulations.

FROM REGULATING HEAVY TO A MORE FACILITATING ROLE

Can government reduce sunk cost to export? Government of Indonesia tend put too much focus on regulating rather than facilitating. Every year, a large number of new regulations are enacted. During the period 2007-2011, there are 192 new laws enacted.[2] In the next five years, based on on *Prolegnas* 2015-2019 there will be 160 new laws with hundreds of implementing regulations can be expected as results. For example, the trade law, which was enacted in 2014 requires 9 government regulations, 14 presidential regulations and 20 ministerial decrees. During the 2014, the Ministry of Trade had introduced 368 regulations in total. Facilitating is not the core element of Ministries related to trade as indicated in their job descriptions (*tugas dan fungsi*).

To make trade as an important element of economic development, the government needs to change its mindset towards trade and trade management. The government needs to facilitate trade and reduce sunk cost to export. Its role needs to shift away from regulation heavy to a more facilitating, addressing supply side and demand side of exports. The government also needs to change its mindset towards imports. The new production pattern relies on imports with more products produced globally in a chain. This will requires the change in mindset and the way of doing business including institutional reforms.

The leading agency to facilitate exports is the Ministry for Trade. However, the Ministry cannot work solely, coordination with technical ministries is important to address supply side and demand side issues. Within the Ministry, there are least three DGs involved in exports DG for National Export Development,

2 http://www.dpr.go.id/uu/prolegnas-long-list

DG for International Trade and DG for International Trade Cooperation. Apart from DG for Export Development, the role of other DGs involves regulatory making. The budget for the Ministry for Trade is relatively small, about Rp 2.3trillion (about US$191bn) in 2014, with 10% of budget allocated for DG National Export Development.

The Ministry for Trade has 25-trade attaché and 19 Indonesian Trade Promotion Centre (ITPCs) worldwide, mainly in major export destinations.[3] The role of trade attaché can be classified into three main elements: representing Indonesia's government in relation to trade policies, facilitating exporters and managing export promotion. For promotion, the Ministry for Trade establishes Indonesia Trade Promotion Centre (ITPC) in strategic locations. The purpose of the ITPC is to provide information and facilitate interactions between Indonesia's exporters/potential exporters with importers/ potential importers. ITPC usually provides permanent display room for export products, websites, facilitate trade missions and matchmaking. However, our assessments on a number of ITPCs shows that their ways of promotion is conventional (focusing on trade expo and business meetings) and majority of websites exhibit information that is not relevant to exporters to the market and importers. ITPCs are also understaffed. This is related to budget that are being allocated to trade promotion. By way of comparisons, Japan's export promotion organization JETRO has 73 offices in 55 countries with 1500 staffs. The Malaysia's Trade promotion agency has 46 offices in 37 countries. Meanwhile, the Thailand's Department of International Trade Promotion (DITP) of its Ministry of Commerce operates 62 offices in 48 major cities around the world, plus 5 regional offices in Thailand. The 5 regional centers work closely with 62 DITP offices worldwide.

RECOMMENDATIONS

Given the existing condition, not much can be done to leverage the role of government in reducing the sunk cost to export in the short run. Unless, the government consider the importance of its trade agencies overseas and change its way of doing business in trade promotion, the sunk cost will be beared by potential exporters. Some recommendations for improvements worth mentioning, includes:

Short run quick solutions:

1. Review the contents of trade related websites
2. Improve the quality and user-friendliness of trade related websites
3. Establish updated database of markets intelligent findings
4. Make the database available for exporters

Medium to longer-term recommendations:

1. Change its mindset in managing trade and trade policies: from regulation heavy to a more facilitating roles
2. Revisit its trade promotion strategies from a conventional to a more modern and innovative way (networking, evidence collecting and IT based promotion)
3. Revisit the role and business model of National Export Development

3 Sydney Australia, Barcelona Spain, Johannesburg South Africa, Jeddah Saudi Arabia, Lagos Nigeria, Mexico, Busan, South Korea, Osaka Japan, Milan Italy, Chennai India, Budapest Hungary, Hamburg Germany, Lyon France, Santiago Chile, Sao Paulo Brazil, Los Angeles and Chicago United State, Dubai United Arab Emirates and Vancouver Canada

4. Allocate more resources (budget and human resources) for trade and trade promotions
5. Dispatch professionals in market intelligences in its trade attaché offices worldwide
6. Enhanced cooperation between Ministry of Trade, Ministry of Foreign Affairs and the Coordinating Board of Investment (BKPM)

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