Optimizing Services Sector’s Roles in Local Economy to Drive National Economic Growth
Case of Surabaya

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Services Sector in Indonesia

- Indonesia’s economy has already evolved into a service-driven economy.
- Services sector has surpassed agriculture as the biggest contributor to jobs since 2008.

**Figure 1. Services has the Largest Share of GDP**

**Figure 2. Services has the Largest Share of Employment**

Source: BPS 2017 (2016 statistics calculated only until the 3rd quarter)

1. **Services as an engine of economic growth.**
   - Services grows at a higher rate than national growth and other sectors.
   - Services’ share to GDP is on the rise, while agriculture and industry’s in decline.

2. **Services as the main driver of Indonesia’s job creation.**
   - Services makes up 45% of total employment.
   - Services currently employs 60 million people, a 20-million increase in the last decade.

3. **Services as an instrument for poverty alleviation.**
   - 8 out of 10 people who move out of poverty are employed in services.

4. **Services sector as an enabler for other sectors.**
   - Services acts as inputs/enabler for other sectors to be more productive, e.g. IT, logistics, etc.
   - Efficiency in services is crucial for overall productivity in other sectors.
Services Sector in Surabaya
Services Sector has the Largest Share of Surabaya’s GDP

- Services sector has the largest economic sector, contributing to **77% of total Surabaya’s GDP**, while processing industry and agriculture sector only make up 20% and 1% respectively.

- Three major services sectors are **distribution services** (29%), **tourism services** (14%) and **construction services** (7%).
Figure 4. Index of Various Sectors’ Development in Surabaya (2009 – 2013)

- Three services sectors with major development (in nominal value) in 2013 are transportation & communication, trade, hotels & restaurants, and finance & other business services.

Source: BPS Surabaya
Three of the fastest growing services sectors in 2013 are transportation & communication (9.2%), trade, hotels & restaurants (8.5%), and construction (9.1%).

In general, the services sector has a much larger growth (8.5% in average) than agriculture, mining, and industry (each less than 5%) in the 2009 to 2013 period.

**Figure 5. Economic Growth of Surabaya City based on Sectors (2009 – 2013) (%)**

- **Transportation & Communication**: 9.2% in 2013
- **Trade, Hotels & Restaurants**: 8.5% in 2013
- **Construction**: 9.1% in 2013

Source: BPS Surabaya
Services Sectors’ Growth over the Years

- **Transportation and Communication services** experienced the largest growth over the years, even with some fluctuations.

- **Construction services’ growth has more than doubled** in the 4-year period, while most of other services grew in the same rate over the years.

- Services sectors’ average yearly growth of 8.5% is exceeding Surabaya’s 6% economic growth.

![Figure 6. Surabaya Services Sectors’ Growth (2009-2013) (%)](source.png)

Source: BPS Surabaya
Contribution of Surabaya’s GDP to East Java

- As of 2013, Surabaya’s GDP made up of 18% of total East Java Regency’s GDP.

- Meanwhile, Surabaya’s population only makes up 7% of total population in East Java.

- The services sector makes up of 77% of Surabaya’s GDP.

- Thus, Surabaya’s services sector is contributing the 13.86% to the East Java’s total economy.

Source: BPS Surabaya 2017
Tourism and Transportation Services in Surabaya

- Total number of **foreign visitors** reached **350 thousand tourists** in 2013, a slightly 20 thousand tourists increase from 2012.

- Total number of **domestic visitors** reached **11.1 million tourists** in 2013, about 1.4 million tourists increase from 2012.

- Surabaya plays an important transport hub in Indonesia:
  - Juanda Airport is the second busiest airport in the country, close 18 million passengers in 2013.
  - Purabaya bus station remains the busiest bus station in Indonesia and in Southeast Asia, carrying up to 120 thousand passengers per day.
  - Tanjong Perak is the second busiest port in the country and a crucial hub to connect the Eastern Region of Indonesia with Java and the Western Region.
Most of investment in Surabaya is from the services sector.

Wholesale trade except vehicle and motorcycle has the highest total foreign investment, with USD5.3 million in 2015, or about 36% of total foreign investment in 2015, with total of Foreign Investment is USD14.6 million.

Warehousing services has the highest domestic investment, reaching IDR348 billion, or about 42% of total domestic investment in 2015, with total of domestic investment is IDR828 billion.
Surabaya Smart City

• Digitization in Surabaya’s government services through its SMART City Plan as follows:
  o Command Center 112 for emergency situations such as traffic accidents, fire, flood, natural disasters, etc.
  o e-Procurement (LPSE)
  o Parking meter system
  o SSW (Surabaya Single Window) for multiple online licenses and registrations on KTP, investment, land use, medical practices, etc.
  o Online education services such as online tryout, online academic report, etc.
  o Online information network and other administration services.

• Surabaya’s Smart City is accelerating urban development and a solution for rapid urbanization by integrating technology to efficiently manage city’s services and assets.
Surabaya’s Digital Creative Industry

• The digital creative industry has a great potential for exports, especially with the emergence of the so-called “desainer kampung” across Indonesia.

• “Desainer kampung” refers to designers (in graphic, website, etc.) who do not attend formal education to learn about design work. They are usually freelance workers and often times form their own community particularly in a less urban environment, such as the well known kampung design, Kaliabu Village, Magelang. Many freelancer digital designers have exported their services - with clients from countries such as Australia, the United States, etc.

• There is relatively a strong presence of communities and agencies in the digital creative industry such as Animotion Design School from PT. Telkom, universities groups, Suwec (Surabaya Web Community), FDGI Surabaya (Forum Desain Grafis Indonesia), Pikodia agency, FreSh Surabaya, etc.

• Digital creative industry in general relies on a good interconnectivity infrastructure, especially in rural areas for desainer kampung to bloom.
1. Strengthening infrastructure
   - National spending on infrastructure was US$57.3 billion in 2014, projected to increase to US$138.6 billion by 2025.
   - National spending on infrastructure needs support from local government and the private sectors.
   - Infrastructure development is necessary for greater efficiency in Surabaya’s key economic sectors such as ports (Tanjung Perak), and so on.

2. Streamlining regulation to increase market access
   - Reduce barriers to entry and incentivize companies to develop innovations and offer quality services.
   - Reforms in the systems of licensing, registration, and permit issuance to lower the cost of doing business and promote investment.

3. Intensifying Digitalization
   - Digital infrastructure has strategic importance for businesses especially with the current rise of fintech and the e-commerce market. Surabaya Smart City is step in the right direction.
   - This will lead to higher penetration rates and therefore facilitate many new sectors, i.e. e-commerce, etc.
4. Zeroing VAT of Export in Services

- 0% VAT rate in services is common in international practices, including in many neighboring countries such as Singapore, Malaysia, The Philippines, Thailand, Vietnam, China and Australia.

- In Indonesia, 0% VAT rate only applies to 3 services sectors, which are manufacturing services, construction services, maintenance & repair services.

- VAT taxation hurts the competitiveness of domestic services sectors, especially when other countries already eliminated VAT on financial, consultancy, accounting, call center and many other crucial services that provide big employment.

- Benefit of Eliminating VAT:
  - Increasing trade and making investment in services look more attractive to potential investors.
  - Boosting economic growth as trade in services increases & lead to new jobs
  - Increasing in tax revenue in the long term
  - Increasing Indonesia’s participation in Global Value Chain
Conclusion: Services in Local Economy as a Driver of National Economic Growth

- Services sector **plays major roles in the local economy** such as restaurants, hotels, SMEs, tourism, etc., which helps cities and provinces to be economically less dependent with the central government.

- Thus, services sector helps **increases local government revenue** (PAD – Pendapatan Asli Daerah), which further strengthens the provincial government’s ability to implement its autonomy.

- Services sector generally has **higher economic growth and job creation**, which is crucial in building local economies in the times of declining agricultural sector and commodity prices.

- The case of Surabaya shows that the services sector **contributes to fifth of the East Java Regency’s economy**, which means that a greater efficiency and growth in services sector is crucial for overall economic growth.

- Services sectors such as IT infrastructure, financial, logistics, etc. are **key enablers** to greater efficiency and productivity and competitiveness of manufacturing and agriculture sectors. Thus, improving services’ performance means an overall improvement of economic sectors, i.e. increasing national economic growth.