Improving Services Sectors as a Strategy for Indonesia’s Competitiveness in Regional Comprehensive Economic Partnership

Talking ASEAN: The Business Series
Jakarta, March 6th, 2017

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Services Sector in Indonesia

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

Services Has the Largest Share of GDP

Services Has the Largest Share of Employment

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

a) **Services as an engine of economic growth.**
   - Grew 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.

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

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

d) **Services sector as an enabler for other sectors.**
   - Services act as inputs/enabler for other sectors to be more productive, e.g. IT, logistics, etc.
   - Efficiency in services are crucial for overall productivity in other sectors.
Services Sector in ASEAN and RCEP

a) ASEAN’s share to total world’s trade in services is roughly around 6%, well far below the share of other 6 non-ASEAN countries under RCEP (23%)  

b) However, ASEAN’s annual growth in services sector and investment is relatively high, with 12% and 22% respectively.
Services Sector in ASEAN and RCEP (continued)

c) RCEP aims to advance integration in services and investment among its member countries.
   - Thus, RCEP could help achieve one of the key elements of the AEC, i.e., ASEAN Investment Integration.
   - RCEP could also create momentum for the on-going rapid growth of services sector and FDIs in ASEAN.

d) RCEP could facilitate the three previous investment integration reforms in ASEAN, i.e.:
   - ASEAN Investment Area (AIA) in 1998.
a) One of key elements of TPP is to increase trade in services sector and investment in Asia Pacific.
   - This could boost FDIs on services in ASEAN, which is relatively low compared to FDIs on goods/production.

b) However, the TPP puts a much stronger emphasis on lowering regulation on technological and broadband services. The impacts, for example:
   - ASEAN startups may face greater challenges with the arrival of tech giants from the United States.
   - An increasing competition among telecom giants.
Case Studies:

a) Air transportation services in Indonesia
b) Logistics services in Indonesia
c) Higher education services in Malaysia
d) Financial services in Singapore
Reforms include:
- Aviation policies deregulation in 1990s – from being very restrictive to more market oriented.
- Domestic Aviation Market reforms, e.g.: easier licenses allowance to new companies.
- Initial public offering as part of the state-owned Garuda’s debt restructuring.

Results:
- Indonesia started with 1 state-owned airline company, but now has 17 private domestic airlines and a total of 27 scheduled airlines.
- Competition from private airlines encouraged state-owned airlines’ improvement and competitiveness.
- Rapid growth in domestic market demands, further creates jobs in air transportation services.
- Indonesia air travel has increased five fold in just between 2000 and 2001, and now Indonesia is the 5th largest domestic air market in the world.
On going issues:
- High shipping and inventory costs.
- Further relaxation in custom regulations needed to increase the flow of exported and imported goods.
- Unbalanced distribution of logistic services – currently very concentrated in Java

Reforms include:
- Logistic reforms still considered to be low.
- However, there have been recent efforts in Logistic reforms, especially in border agency area.
- Some relaxation in logistic regulation.

Results so far:
- Indonesia’s Logistic Performance Index increased from 2.76 in 2010 to 3.08 in 2014 (from 75th position in 2010 to 53rd in 2014), but fell back to 63rd position in 2016.
Reforms include:

- Changes in education and immigration policy in the 1990s, e.g.:
  - Allowing private institutions and foreign universities to offer tertiary degrees
  - Encouraging the recognition of degrees internationally
  - Easier migration and visa policies for foreign students

Results:

- Greater revenues from “consumption abroad,” i.e. from foreign students in the country. From 2003 - 2011, the number of International students in the country more than tripled, mostly from Indonesia and China.
- Competition from foreign higher education has led to better domestic education service providers.
- Solved excessive domestic demands for tertiary education problem from the 1990s.
Reforms include:

- Singapore’s Monetary Authority (MAS) adopted policies to protect retail banking in 1970s.
- This includes the introduction of Qualifying Full Bank (QFB) program, i.e., new banking licenses.
- The removal of 40% limit on foreign shareholding of local banks.
- Increasing transparency by strengthening regulatory framework through more demanding disclosure standards, liquidity support, and deposit guarantees.
- Bilateral and multilateral agreements to fasten reforms.

Results:

- A rapid growth in exports and imports of insurance and financial services
- Since the 2000s, finance has become the biggest contributor to trade services surplus.
- Maintained itself as the financial center in the ASEAN region.
Indonesia’s Efforts in AFAS and AEC Commitment

- The creation of the National Committee of AEC.
- On-going reforms in National Logistic Systems.
- Relaxation in Licenses for Indonesia National Single Window (INSW).
- Fewer bureaucracies, e.g., Ministry of Trade as the gateway for International Trade.
- Strengthening the role of National Standards of Indonesia (SNI) to improve the quality of goods and services.
Strategy to Increase Services’ Competitiveness

a) Strengthening infrastructure
   ▪ Spending on infrastructure was US$57.3 billion in 2014, projected to increase to US$138.6 billion by 2025. Moreover, RPJMN (2015-2019) is a good start to improve infrastructure but it also needs support from the private sectors.

b) 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.
c) Intensifying Digitalization.
   - Digital infrastructure sharing has strategic importance for licensed operators trying to extend network while minimizing costs for Indonesia Broadband Plan (Rencana Pita Lebar Nasional). This will lead to higher penetration rates and therefore facilitate many new sectors, i.e. e-commerce, etc.

d) ASEAN Integration on trade in services should be through Mutual Recognition Arrangements (MRAs).
   - RCEP could be the platform for MRAs and a pathway to make AEC’s “free flow of trade in services” a reality.

e) Increase cooperation in services through dialogues and forums among ASEAN members.
   - to increase information of the services market.
   - to diversify production capacity, supply and distribution of services within and beyond ASEAN.
f) Reforms and improvements that provide better delivery of *Modes of Supply* (services in cross-border trade).
   - this includes the elimination of value-added tax (VAT) on services export, which is common in most countries. The current 10% VAT is making Indonesia’s services exports less competitive.

e) Expand RCEP’s membership to TPP’s members for further global trade reforms and a greater engagement of global trade in the Asia Pacific region.
Conclusion

- Services restrictions are holding back growth and reducing competitiveness
- Removing services restrictions is a proven strategy to boost growth
- Case studies show that liberalization and reforms in services sector, when done correctly, can lead to overall growth.
- The RCEP could strengthen ASEAN’s engagement in the global economy.
- Expanding RCEP membership to TPP members could be a pathway to APEC’s Free Trade Area of the Asia-Pacific (FTAAP).
- RCEP and expanding its members could help build momentum for global trade reforms.
- RCEP designed to mutually reinforce and deepen regional economic integration, which will enhance trade and investments flows in ASEAN.