# Regionalism vs. Nationalism: Prospect of Indonesia's Involvement in AFTA

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**Abstract**

Indonesia has switched, in its foreign economic policies, to neo-liberal posture especially after the turmoil of Asian financial crisis, and continues to adhere to the course of liberalization, especially during the current regime of President Susilo Bambang Yudhoyono. The benefits from joining the ASEAN Free Trade Agreement (AFTA) have been believed to be a stepping stone for ASEAN countries to compete in the world markets. It is also believed to be better than other multilateral organizations such as WTO. However, many others, especially those of the minimalist camp, claim that pursuit of open regionalism has limited Indonesia's ability to resist the negative forces of globalization while ASEAN's contributions to Indonesian international autonomy and bargaining power have been minimal. This paper aims to examine Indonesia's reluctance for participating actively in AFTA from the political economy perspective. Given Indonesia's commitment to free trade and its accelerated dismantling of trade barriers, sometimes unilaterally, the reservations about AFTA seem paradoxical. Nevertheless, we want to argue that the crucial factor in deciding Indonesia's adherence to AFTA is employment. Despite its huge population, Indonesia's competitiveness is still under threat from other labor abundant ASEAN countries, not to mention China. Therefore, the adoption of a strategy of enhancing employment for Indonesia is critical for raising people's support for further regional integration and the successfulness of its participation in AFTA.

Keywords: AFTA, trade and employment, nationalism, openness

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## Nationalism and Foreign Economic Policy

One of the most prominent features of the Indonesian Economy during the post-independence period is the emergence of economic nationalism. Shortly after independence, for example, the Indonesian government introduced the so-called *Benteng* system in 1950, which was intended to promote native Indonesian businessmen (Mackie, 1971: 47). Subsequently, following the introduction of Guided Democracy in 1957, the expropriation of foreign capital began to take place. During this period, many "Dutch trading and estate enterprises, the core of Dutch colonial capital, were expropriated together with Dutch shipping, banking and industrial enterprises" (Robinson, 1986: 79). The New Order government in 1966 made changes in the way economic nationalism was implemented. The New Order government's main priority in its economic stabilization program was to curb the rate of inflation that it had inherited from the previous government (Thomas and Ponglaykim, 1973: 145). As a result, Indonesia implemented an open-door economic policy, which "aimed at producing maximum economic growth and relying heavily upon investment by international corporate capital" (Robinson, 1986: 131). However, these economic policies lasted only until 1975, when there was a resurgence of economic nationalism (Robinson, 1986: 131). The New Order government began to take a more active role in foreign policy, particularly within the regional context, following the end of the Cold War in the late 1980s and the resurgence of regionalism in both Western Europe and North America. In any case, the New Order government pursued a rather pragmatic approach in its overall conduct of foreign economic policy.

The economic crisis in 1997 marked the fall of the New Order government. Habibie was appointed the third Indonesian President following Suharto's resignation on May 21, 1998. Harbibie faced an immense challenge when he took the presidency, particularly with regard to alleviating the economic crisis and trying to establish the foundation of democracy in Indonesia. The deepening economic crisis and the independence crisis in East Timor triggered nationalist sentiment in the country. Searching for possible scapegoats to take the blame for the economic crisis, the Indonesian authorities and media alike pointed their fingers at currency speculators (Henderson, 1998: 155). The appointment of Adi Sasono, a former Islamic NGO activist, as the Minister of Co-operatives, Small, and Medium Enterprises also raised fears over the possible re-emergence of economic nationalism in Indonesia. In the past, he had developed the concept of the Ekonomi Kerakyatan (People's Economy), which can be defined as a participatory economy, which allows fair and equal access to all members of society in the processes of production, distribution and national consumption without sacrificing human resources and environment to support the people (Sasono, 1999). In principle, the concept of the People's Economy involved activities conducted from the people, by the people, and for the prosperity of the people. However, economic nationalization of foreign and ethnic Chinese capital was not the main aim of Sasono as some suspected. True reform within the framework of the People's Economy, according to Sasono, would include the empowerment of the small and weak in order to create a strong middle class.

Harbibie's foreign economic policy was quite successful overall. Apart from his full commitment to the IMF's prescriptions, the success of Habibie was also due to his ability to promote political democracy in Indonesia, which allowed the country to regain the necessary support from the international community to alleviate the economic crisis. Another major move to secure economic support from foreign donors and international financial institutions was Habibie's intention to hold a fair and open election. Furthermore, at the regional level, during his short tenure, Habibie managed to make close contact with Mahathir Mohammad, the Malaysian Prime Minister. As a result, the future of ASEAN regionalism, and the progress of AFTA in particular, was no longer in jeopardy despite the strained relationship between Indonesia and Singapore (Chandra, 2008: 105).

Abdurrahman Wahid took over the presidency following the 1999 election. Shortly after his appointment as the head of state, President Wahid set out the main themes of his foreign economic policy, which included the promotion of foreign investment and free market reforms (Symonds, 1999). This was President Wahid's nationalist appeal to build a stronger Indonesia in the face of the economic crisis. In addition, Wahid also called for closer ties with Japan, China and the member countries of ASEAN. Another major foreign economic policy in the Wahid administration was a commitment to fully support the IMF rescue loan package, which was linked to the IMF Letter of Intent (LoI). The disbursement from the IMF was important because it could be "taken as a measure of market confidence in the progress of economic reform. Therefore, . . . the credibility of Indonesian economic reform [was] reflected in the successful and consistent implementation of the IMF program" (Feridhanusetyawan, 2003: 238). Although the President was able to gain enormous support from the international community for Indonesia's efforts at national integration, Indonesian foreign policy during the Wahid administration remained quite conventional and its main ideas were similar to the foreign policy conducted by the New Order government (Smith, 2000: 523).

It was decided through a vote in the Parliament that the Wahid should step down and Megawati was sworn in to become the fifth Indonesian president on July

2001. As with her predecessors, the Megawati administration inherited the challenges of maintaining the country's integration, alleviating the economic crisis, and ensuring long-term political stability in the country. As with her father, Sukarno, President Megawati has also been known as a staunch nationalist who was reluctant to jeopardize the current geographical existence of the country by allowing any separatist movements within the country. In terms of improving economic conditions, Megawati appears to have put the appropriate foreign economic policy in place. One key feature of the Megawati administration's overall foreign policy has been a return to the traditional concentric circle formula (see figure 1). This formula has identified ASEAN as the highest priority of Indonesian foreign policy. Indonesia's return to the concentric circle foreign policy formula dismissed speculation that Indonesia would abandon AFTA and other ASEAN regional economic integration initiatives. ASEAN and Western countries remain within the first and the third circles of Indonesian foreign policy overall. Major adjustments, however, have been made to the second circle (Non-Aligned Movement, NAM), which indicates that Indonesia will concentrate its foreign policy on the member countries of the Pacific Island Forums (PIFs), the Southwest Pacific Dialogue, and the Tripartite Consultation between Indonesia, Australia, and Timor Leste, and the three close economic partners of Indonesia, Japan, China and South Korea (Chandra, 2008: 111). The adjustments made to the concentric formula indicate Megawati's realization of the growing need to strengthen regional economic cooperation with the countries of the Southwest Pacific and Northeast Asia. In this way, Indonesian foreign economic policy is decided according to the overall foreign policy of the country.

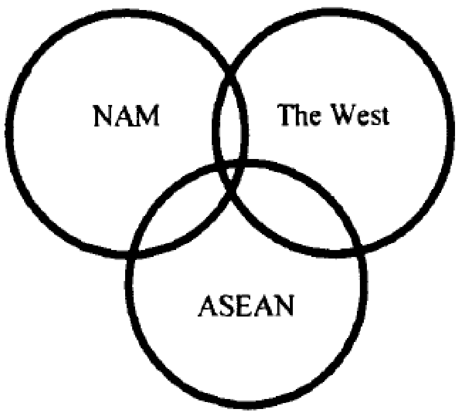


**Figure 1 Three Concentric Circles of Indonesian Foreign Policy**

Source: Smith (2000), p. 18.

Meanwhile, Indonesia experienced major problems with foreign investments.

The main obstacles to investment in Indonesia were international as much as domestic. At the international level, aggressive U.S. foreign policy toward Afghanistan and Iraq has had a damaging effect on the Indonesian economy. These two events stimulated threats and demonstrations against the United States and its allies in Indonesia (Anwar, 2003: 75). At the domestic level, issues such as regional security, law enforcement, labor market problems, the overlapping responsibilities of central and provincial government, regulatory burdens, and distributions in the tax system remain major problems to be confronted by potential investors in Indonesia (Bappenas, 2003).

Dr. Susilo Bambang Yudhoyono (Also referred as SBY) is the first Indonesian president that has been directly elected by the voters throughout Indonesian history. He secured the majority of votes in presidential elections in July 2004. Yudhoyono's conviction toward neo-liberalism has been consistent since he was elected as the representative of the Democratic Party to take part in the presidential election. During his election campaign, for example, Yudhoyono ensured his supporters that the promotion of foreign investment would make a positive contribution toward job creation in the country. One important element to support his neo-liberal policy was the strengthening Indonesia's relationship with the United States, a move which was welcomed by the Indonesian armed forces. Another important element of Yudhoyono's neo-liberal agenda was the active and aggressive participation of Indonesia in bilateralism, regionalism, and multilateralism. Indeed, the Yudhoyono administration was generally supportive toward any forms of regionalism in a complementary to the ideological approach that was subscribed by the Indonesian leader.

In sum, the collapse of the Indonesian economy in 1997 brought significant changes in the way that nationalism and foreign economic policy were integrated by the state. The conventional approach of implementing economic nationalism was no longer applicable. Faced with an ever-increasing dependency on various international financial institutions and other foreign donors, all the post-economic crisis Indonesian governments were forced to follow stringent measures to secure loans from these international institutions. The agreements made between these Indonesian governments and the IMF through the signing of LoI, in particular, have been particularly demanding. However, there have also been debates among the Indonesian political elite as to whether Indonesia should continue its relationship with the IMF, which officially expired at the end of 2003 (Economist Intelligence Unit, 2003: 22). On the one hand, the Indonesian political elite is concerned that the Indonesian government will continue to lose its sovereignty by following IMF measures. On the other hand, the presence of the IMF has, indeed, improved the macroeconomic condition of Indonesia. Although the final outcomes have yet to be seen, the Indonesian public has shown growing dissatisfaction toward the IMF's stringent conditions. As regards Indonesian foreign economic policy in ASEAN, the shift of leadership from Wahid to Megawati allowed Indonesia to return to its more traditional focus on its immediate neighbors. As a result, Indonesia remains committed to the progress of ASEAN economic regionalism, particularly AFTA. After all, it has always been in the interests of Indonesia to put ASEAN at the cornerstone of its overall foreign policy.

**Indonesian Perceptions of AFTA**

The perceptions of Indonesian state and non-state actors of AFTA in recent years have been changing. The emergence of regional economic crisis in 1997, in particular, has played a major role in changing their attitudes toward ASEAN regional integration schemes. This change of attitude was actually stimulated by the economic crisis in that there was a consensus among Indonesian policymakers that enhanced regional economic integration in the Southeast Asian region would provide a fundamental mechanism to alleviate the economic crisis. As a result, the Indonesian government welcomed ASEAN's initiatives to accelerate the AFTA schedule as envisioned in the Statement on Bold Measures (ASEAN 1998). This statement reflected the realization of ASEAN leaders that the economic crisis would have disastrous effects on the business dynamics and the economies of ASEAN member countries. It is for this reason that the member countries of ASEAN agreed to initiate some concrete measures to minimize the negative effects of the economic crisis. Although AFTA in itself was not able "to address the regional upheaval and was certainly not designed to deal with such events" (Narine, 2002: 186), ASEAN leaders were convinced that the acceleration of AFTA would stimulate economic growth and renewed business confidence, which, in turn, would speed up the process of economic recovery in the region. As its stood, Indonesia managed to place as many as 6,346 items (88.43%) on to AFTA's inclusion list in 2000, and 6,461 items (90.04%) in 2001 (Depperindag, 2000: 27; cited in Chandra, 2008: 150), which reflected Indonesia's genuine commitment toward AFTA.[1]

Table 1 AFTA Common Effective Preferential Tariff (CEPT) List for 2001

| | Inclusion List | Temporary Exclusion List | General Exception List | Sensitive List | Total |
|---|---|---|---|---|---|
| Brunei | 6,284 | 0 | 202 | 6 | 6,492 |
| Indonesia | 7,190 | 21 | 68 | 4 | 7,283 |
| Malaysia | 9,654 | 218 | 53 | 83 | 10,008 |
| Philippines | 5,622 | 6 | 16 | 50 | 5,694 |

[1] However, according to ASEAN Secretariat as adapted from Chowdhury (2007), the number of items in 2001 Indonesia's inclusion list is 7,190. See Table 1.

| | | | | | |
|---|---|---|---|---|---|
| Singapore | 5,821 | 0 | 38 | 0 | 5,859 |
| Thailand | 9,104 | 0 | 0 | 7 | 9,111 |
| **ASEAN 6 Total** | **43,675** | **245** | **377** | **150** | **44,447** |

Source: ASEAN Secretariat; adapted from Chowdhury (2007), Table 2.

Apart from a need to alleviate the economic crisis, Indonesia was also inclined to strengthen ASEAN economic regionalism through AFTA for the overall benefits accrued from regional integration strategy. Chandra's field research also reveals that, because of its commitment to AFTA, Indonesian state and non-state actors were convinced that the country could move closer to achieving its objectives of sustained economic development and the maintenance of national unity (Chandra, 2008: 150). With its capacity to promote economic growth and competitiveness, AFTA will have positive knock-on effects on the overall economic development of Indonesia, leading to prosperity. This nationwide prosperity will help the Indonesian government to minimize the threat of national disintegration presently posed by several ethno-nations, i.e., Aceh, Papua, etc., which has become a serious post-crisis phenomenon in Indonesia. Moreover, the Indonesian government will also be able to increase its autonomy and bargaining power in the international arena through its full commitment in the ASEAN regional integration schemes. In the age of an increasing drive toward multilateralism, pressure groups, i.e., the business community, the academic community, NGOs and civil Society organizations (CSOs), in Indonesia are demanding that their government should play an active role in the international arena. Greater prosperity throughout the Southeast Asian region will also increase the prestige and power of other ASEAN member countries. Such conditions, in turn, will give ASEAN member countries greater autonomy and bargaining power in dealing with major powers, such as the United States and the EU, in many multilateral negotiations. In the long run, the regional integration strategy is also hoped to contribute to the promotion of Indonesian culture and identity at both regional and international levels. Therefore, the need to minimize the negative impacts of the economic crisis and other important incentives afore-mentioned has acted as stimulants to promote the speeding up of the AFTA schedule.

However, the Indonesian government's commitment toward the implementation and scheduled acceleration of AFTA drew some criticism from various sources in Indonesia. Indonesian domestic pressure groups such as business associations, NGOs, CSOs, for example, were very skeptical of Indonesia's entrance into the AFTA scheme. A year prior to the implementation of the AFTA scheme in January 2002, for example, the Indonesian Chamber of Commerce and Industry (*Kamar Dagang dan Industri Indonesia*, KADIN) expressed its concern about AFTA and made an official demand that the Indonesian government should delay Indonesia's entry into the scheme until

2005 (*Kompas*, 2001). Almost a year after its implementation, the Indonesian government was still receiving stiff criticism over its commitment to AFTA. In the face of possible increases in fuel, power, and telephone prices in early 2003, for example, various Indonesian labor organizations and members of the Indonesian Entrepreneurs Association (*Asosiasi Pengusaha Indonesia*, APINDO) maintained that the Indonesian government's commitment to AFTA was a proof that the government was more concerned about the country's global position than the welfare of its people (Guerin, 2003). The anti-AFTA sentiment in Indonesia contended that the government should be more concerned about domestic problems rather than giving priority to regional trade liberation issues.

Another important factor in analyzing contemporary Indonesian attitude toward AFTA was the introduction of the Regional Autonomy Laws (*Otonomi Daerah*, OtDa), which challenged the AFTA scheme. In 1999, the Habibie administration issued Act No. 22/1999 (UUPD), which is a regional government law, and Act No. 25/1999 (UUPKPD), which concerned with fiscal balance between central and regional governments. Both regulations were officially implemented in January 2001. These two acts were aimed at decentralizing the heavily centralized system during the New Order period. Specifically, Act No. 22 was used to make a fundamental shift in government functions from the central to regional level, while Act No. 25 was implemented in conjunction with the former to focus on fiscal relations between the central and regional governments (Silver *et al*., 2001: 346). They have generated great concern, particularly over the issue of ethno-nationalism. In KADIN's view, for example, the OtDa will complicate the investment laws that could hinder business transactions (Tempo, 2001). Following the implementation of these regulations, many provincial governments have issued numerous laws which have greatly bureaucratized the relationship between officials and the business sector. The Indonesian government, on the other hand, argues that such changes are a natural result of political transition in Indonesia, and should be considered reform euphoria.

At the time of the formation of AFTA, the ASEAN countries accounted for only 10% of Indonesia's total exports. Indonesia increased its export share to ASEAN to about 18% in 2006. Singapore is Indonesia's major ASEAN export market. However, the share of Indonesia's exports to Singapore has remained stable at around 10% since the early 1990s. On the other hand, the importance of Malaysia as an export destination has increased from around 1% in 1991 to close to 5% by 2004.

ASEAN is more important as a source of Indonesia's imports than as a destination of Indonesia's exports. Around 32% of Indonesia's imports came from the ASEAN countries. Overall, ASEAN still accounts for around 24% of Indonesia's total trade; countries outside ASEAN remain major trading partners. Although Indonesia's intra-ASEAN trade has increased in recent years, it only accounts for 11% of total intra-ASEAN trade, well behind more advanced members, Singapore and Malaysia, and 4 percentage points behind Thailand in 2005(see Table 2). Singapore alone accounts for around 41% of total intra-ASEAN trade, followed by Malaysia with a share of around 22%. Thus, it seems that less developed members are not benefiting much from AFTA.

Table 2 Country Shares in Intra-ASEAN Trade (%), 2005

| | Share (%) |
|---|---|
| Brunei | 0.7 |
| Cambodia | 0.4 |
| Indonesia | 10.9 |
| Laos | 0.2 |
| Malaysia | 21.6 |
| Myanmar | 0.8 |
| Philippines | 5.3 |
| Singapore | 40.7 |
| Thailand | 14.9 |
| Vietnam | 4.6 |

Source: ASEAN Secretariat.

Given Indonesia's very small share in total intra-ASEAN trade, Indonesia is not expected to gain much from AFTA. One study undertaken by the Ministry of Industry and Trade suggests that Singapore and Malaysia benefit most from AFTA, followed by Thailand and Indonesia (reported in Saleh, 2005). This is in line with their respective intra-ASEAN trade shares. Based on CGE modeling, Feridhanusetyawan and Pangestu conclude, "The creation of AFTA . . . is estimated to contribute little additional welfare benefit . . . to Indonesia . . . ." On the other hand, they find significant welfare gains from full implementation of trade liberalization under Uruguay Round and Asia Pacific Economic Cooperation. However, agricultural liberalization in AFTA is likely to benefit Indonesia as we can expect from Indonesia's potential capability to provide agricultural products for the region (Feridhanusetyawan and Pangestu, 2003: 72).

In a more recent study Hartono *et al.* (2007), also using CGE modeling, found similar results to Feridhanusetyawan and Pangestu (2003). Their simulation results show that real GDP of Indonesia increases by only 0.13% and the welfare gain by only 0.61% from AFTA trade liberalization. On the other hand, real GDP and overall welfare gains from global trade liberalization are 1.31% and 2.64% respectively. More interestingly, unskilled labor income increases by only 0.79% from AFTA liberalization as opposed to a staggering 6.46% from global trade liberalization.

Table 3 Indonesia's Gains from Trade Liberalization (percentage change compared to base-line simulation)

| | AFTA Liberalization | Global Liberalization |
|---|---|---|
| Real GDP | 0.13 | 1.31 |
| Imports | 1.92 | 8.86 |
| Exports | 0.68 | 3.89 |
| Unskilled labor Income | 0.79 | 6.46 |
| Capital Income | 0.64 | 4.87 |
| Welfare* | 0.61 | 2.64 |

* Welfare index includes 17 variables, such as inflation, wages, government revenue, GDP, etc.

Source: Adapted from Hartono *et al.* (2007), Table 5.

The estimated gains from ASEAN *plus* and other bilateral trade liberalization (Indonesia-China, Indonesia-Japan, Indonesia-Korea, Indonesia-India) are also quite small compared to global trade liberalization. Only in the cases of East Asian FTA and APEC FTA, the estimated welfare gains are reasonable. A very similar sectoral output effect occurs in the case of ASEAN-China FTA. More damaging impact on labor-intensive sectors such as textiles and leather happens in the case of ASEAN+3 and East Asian FTA.

The expected loss from AFTA and ASEAN *plus* FTAs in the labor-intensive sector has significant political economy implications, especially when Indonesia's competitiveness is being eroded due mainly to other labor surplus countries such as Vietnam and China. Between 2000 and 2002 nearly one million workers lost jobs in the textile, garments and footwear (TGF) industries (Chowdhury, 2007: 10). And if we look at it from a longer run perspective, the TGF lost a total of 7.7 million workers from the period of 1985-95 to the period of 1995-2005 (Aswicahyono *et al.*, 2011: 18). Exports in TGF hardly grew and they declined in the wood-based industries (including furniture) from 1995 to 2005.[2] Nevertheless, employment growth was still significant in both these industries, suggesting that some labor-intensive segments were still able to compete in world markets. For example, even though TGF and wood industries contributed less than 5% of the increase in the value of manufacturing exports in 1995-2005, they provided 40% of all jobs associated with exports in this period.

The share of unskilled labor-intensive manufactured exports has been declining since the early 1990s, about the time when AFTA was initiated. This saw the rise in unemployment rate from 4.4% in 1994 to 4.9% in 1996. The rate rose to a peak at

[2] The value of exports continued to increase slowly in the TGF industries in 2000-2005, while they fell in the wood-based industries. See Aswicahyono *et al*. (2011), Figure 8.

11.24% at the end of 2005 and increasingly declined to less than 6% recently (Trading Economics, 2013). Therefore, it becomes politically difficult to pursue further regional integration when Indonesia is rapidly losing competitiveness in labor intensive manufacturing exports mainly to its ASEAN partners, contributing to rising unemployment and poverty. The persistence of unemployment and poverty may slow down not only regional integration but also multilateral liberalization. There is already a view among academics, officials, business leaders and civil society organizations that liberalization has gone too far (see, *e.g.*, Chandra, 2008). They are demanding that protection should be increased in sensitive sectors such as textiles, chemicals, motor vehicles and steel (Vanzetti *et al.*, 2005).

## Concluding Remarks

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the Role East Asia plays for Indonesian economy

Table 1 Intra-Regional Trade Ratios of Manufacturing

| | East | Emerging East | ASEAN+3 | ASEAN | NAFTA | EU15 |
|---|---|---|---|---|---|---|

| | Asia-10* | Asia-9 | | | | |
|---|---|---|---|---|---|---|
| 1994-95 | 53.2 | 36.5 | 27.0 | 17.8 | 39.9 | 62.6 |
| 2006-07 | 55.1 | 40.0 | 30.4 | 20.2 | 38.3 | 57.4 |

* Intra-regional trade shares have been calculated excluding bilateral flows between the PRC and Hong Kong.

Source: Athukorala and Archanun (2009), Table 4.

Table 2 Intra-Regional Trade Intensity Indices

| | 1980 | 1990 | 2001 |
|---|---|---|---|
| East Asia-10** | 2.13 | 2.08 | 2.22 |
| Emerging East Asia-9*** | 3.02 | 2.66 | 2.44 |
| NIEs-4 | 2.00 | 1.56 | 1.41 |
| ASEAN-4 | 1.58 | 1.45 | 2.17 |
| NAFTA | -- | 2.06 | 2.12 |
| EU15 | 1.39 | 1.45 | 1.67 |

* Intra-regional trade intensity: $(X_{ij}/X_{..})/[(X_{i.}/X_{..})(X_{.j}/X_{..})]$, where $X_{ij}$ represents exports of region i to region j，$X_{i.}$ represents total exports of region i, $X_{.j}$ represents total exports of the world to region j, and $X_{..}$ represents total exports of the world.

** East Asia emerging 9 and Japan.

*** NIE-4 (Korea, Taiwan, Hong Kong and Singapore), ASEAN-4 (Malaysia, Thailand, Indonesia and the Philippines) and China.

Source: Kawai (2004), Table 2b.

Labor market rigidity
Hufbauer (2007), 98

Most objectionable are severance pay rules and layoff procedures
Hufbauer (2007), 99.

Proposed reform entailed revision to Labor Law No. 13/2003, adoption of which significantly raised hiring costs. The proposed revision includes:

- Fixed-term contracts (FTCs)
- Outsourcing
- Minimum wage
- Severance pay

Forced labor

Child labor

Hufbauer (2007), 102-104

Minimum wage applies only to formal sector, which accounts for 35% of the work-force
104

In non-communist countries, semidemocratic and authoritarian states banned unions (Thailand 1957–1972, Burma), controlled unions through exclusionary corporatist institutions in which state-backed unions enjoyed monopoly or near-monopoly status (the Philippines, Taiwan, Indonesia, South Korea, Singapore), or constrained unions through restrictive labor legislation (Malaysia, Thailand since the 1970s)

Caraway (2010), 227-28

Most striking are the plummeting scores of the four countries with the strongest DJLS—Cambodia, Indonesia, Vietnam, and the Philippines. The falling scores on DFLS are in part a function of their high DJLS scores

Caraway (2010), 229-31

Incorporating enforcement had particularly strong effects on labor market flexibility in Cambodia and Indonesia because both had relatively high DJF scores but extremely poor enforcement.

Caraway (2010), 232

In Indonesia, South Korea, and Thailand, evidence is mixed about the effects of the GSP petitions on labor rights. Indonesia was the target of multiple GSP petitions in the late 1980s and early 1990s. All of the petitions were accepted for review, and two underwent continuing reviews. Glasius (1999) documents a number of steps taken by the government, but none ultimately had much effect on collective labor rights, de jure or de facto. For example, although a strike ban in vital industries from the 1960s was revoked, the Suharto regime had long relied on other regulations to suppress strikes. A new ministerial regulation that permitted independent unions to form at the plant level also required them to later affiliate with the state-backed union. The in-

crease of the minimum wage and stronger enforcement of this higher wage was a significant achievement, but gains in wages should not be confused with meaningful improvements in collective labor rights, on which the regime gave little ground. In addition, a massive wave of wildcat strikes swept through Indonesia during this period, and most of these strikes focused on minimum wages, so the interactive effect of international and domestic pressure is evident. Glasius is probably correct that part of the explanation for the limited effect of the GSP petition is that the USA was half-hearted in using its influence to pressure an important ally and trading partner. The memory of the unpleasant glare of the international spotlight during the GSP review, however, played a role in making labor reforms a high priority for the Habibie administration, which was eager to establish its democratic credentials after the fall of Suharto (Caraway 2004).
Caraway (2010), 235

At PT Mulia Knitting in Indonesia, for example, investigators from the Worker Rights Consortium (WRC) uncovered evidence that management had busted a union by firing its leaders.19 When the WRC asked the university licensee to exert pressure on the company, the licensee was in no position to do so because it no longer had any orders with PT Mulia. In another case in Indonesia, the PT Dae Joo Leports factory worked with the WRC to make significant improvements to address numerous violations uncovered by the WRC investigation team, but PT Dae Joo Leports later closed its factory, relocating to China, in part because of the increased costs imposed by complying with the WRC's recommendations.

Caraway (2010), 239

In the remaining four countries—South Korea, Indonesia, the Philippines, and Cambodia—the IMF's strong preference for greater labor market flexibility has been evident, although in all but South Korea, this is a recent development.

Labor market flexibility escaped the IMF's notice in Cambodia, Indonesia, and the Philippines in the immediate aftermath of the Asian financial crisis, even though all had relatively inflexible labor regulations. Since 2004, however, the IMF has recently begun to highlight issues of labor market flexibility in its Article IV consultations with Cambodia, Indonesia, and the Philippines. In Indonesia, the new attention is the result of the passage of the Manpower Act of 2003, which reduced labor market flexibility. In response to both IMF and business pressure, the Indonesian government attempted to push through a reform of the Manpower Act, but labor unions mounted massive protests and thwarted this effort.

Caraway (2010), 242

Indonesia is the second country that revised its laws in the direction of less flexibility. In 2000 the pro-labor Minister of Manpower issued a decree that dramatically increased severance pay. Unions were ecstatic and fought successfully to prevent the revocation of this decree. The Manpower Act of 2003 further increased protection by limiting outsourcing to "non-core" work and raising severance pay for most dismissals. Since 2003, the IMF has voiced its concern about Indonesia's inflexible labor markets, but government efforts to carry out flexibilizing reforms were greeted with massive protests by unions. In spite of the wish of employers to revisit labor reform, thus far the government has proven reluctant to try again.

Caraway (2010), 243-44

Given Indonesia's very small share in total intra-ASEAN trade, Indonesia is not expected to gain much from AFTA. One study undertaken by the Ministry of Industry and Trade suggests that Singapore and Malaysia benefit most from AFTA, followed by Thailand and Indonesia. This is in line with their respective intra-ASEAN trade shares.[9] Based on CGE modeling Feridhanusetyawan and Pangestu (2003, p. 72) conclude, "The creation of AFTA… is estimated to contribute little additional welfare benefit … to Indonesia…" On the other hand, they find significant welfare gains from full implementation of trade liberalization under Uruguay Round and Asia Pacific Economic Cooperation. However, agricultural liberalization in AFTA is likely to benefit Indonesia as it makes Indonesia potentially the major producer of agriculture in ASEAN.

Chowdhury (2007), 9

The estimated gains from AFTA *plus* and other bilateral trade liberalizations (Indonesia-China, Indonesia-Japan, Indonesia-Korea, Indonesia-India) are also quite small compared to global trade liberalization. Only in the cases of East Asian FTA and APEC FTA, the estimated welfare gains are reasonable.

In terms of sectoral impacts, AFTA creates positive output growth in some capital intensive sectors, such as automobile, other transport means, machine, metal and construction, but negative impact on labour intensive sectors such as leather. A very similar sectoral output effect occurs in the case of AFTA-China BFTA. More damaging impact on labour-intensive sectors (e.g. textiles and leather) happens in the case of ASEAN + 3 and East Asian FTA.

Chowdhury (2007), 10

As can be seen from Figure 4, the share of unskilled labour intensive manufactured exports has been declining since the early 1990s, about the time when AFTA was initiated. This saw the rise in unemployment, the rate rising from 4.4% in 1994 to 4.9% in 1996.[10] The unemployment rate now stands at around 6% (according to the old definition) and at around 10% (according to the new definition).

Chowdhury (2007), 11

With the increase in unemployment, the poverty rate remains stubbornly high at around 16%. Since the majority of the poor live in the rural areas, it is important to examine the impact of trade liberalization on rural household income. According to Chandra (2005), unemployment in the Indonesian agricultural sector is likely to rise due to BFTA, and small peasants would be worse-off.

Figure 3: Declining Share of Indonesia's Labour Intensive Exports


Source: Ministry of Trade, Government of Indonesia

Chowdhury (2007), 11

Majority of Indonesian migrant workers are employed in the informal sector, and have little protection against various abuses and exploitation. According to Kaur (2007), Malaysia recruits about 60,000 Indonesian domestic workers annually and more than 90% of the 240,000 domestic workers in Malaysia are Indonesians. Singapore has been the second major destination for Indonesian migrants in the region and Indonesian labour migration to the island has been dominated by women since the late 1980s. Domestic workers are usually paid lower wages than other migrant workers, and wages are often delayed. Few are allowed to have rest days, and their accommodation is sub-standard (some have to sleep on the floors of kitchens). Moreover, these workers are often subjected to sexual harassment by men in employers' households, as documented in several studies conducted in Singapore and Malaysia.

Chowdhury (2007), 12-13

The slowdown of Indonesian exports can be attributed to supply problems, including the cost of doing business (high cost economy), weak industrial relations policy, minimum wage hikes and poor infrastructure conditions. These factors have become a major constraint to rapid growth of exports.

from 1995-2001 the RCA of some of these products, including plywood, textiles, footwear and garments, showed a declining trend (arrow from right to left). These figures reinforce the earlier suggestion that export growth was mainly driven by the supply side (competitiveness) rather than the demand side from 1985 to 1995, but this was no longer the case from 1995 to 2001. This suggests that the main obstacles to Indonesian export growth mainly stem from the supply side.

Soesastro (2005), 4

The continuing signs of increasing protectionism imply that the Indonesian government has resorted to trade policy to overcome inefficiencies in the supply side. The government has not addressed the problem of lagging productivity through measures to increase efficiency. Instead, it tends to preserve the inefficient industries by increasing protectionism.

Soesastro (2005), 7

The rhetoric of agricultural protectionism for example is to protect poor rural farmers, but in reality it protects politically powerful rent-seeking groups. Basri, Maddaremeng and Nuridzki (2004) shows that there is a statistical evidence that trade protection was mostly given to the sector with high capital intensive. This study also finds that there is no statistical evidence that trade protection has been given to protect the sector which has low wages and salaries. In other words there is no evidence that protection protect the poor. Contrary to the argument that protection help the poor or labour, this study shows that the capitalists are the one who are the benefited by trade protection in Indonesia.

Soesastro (2005), 12-13

Indonesia is a newcomer in forming bilateral FTAs. Its agenda has been largely driven by the offers made by other countries to form FTAs with Indonesia. Unlike Singapore or Thailand, Indonesia does not pro-actively select countries as its potential FTA partner. During the Megawati government, Indonesia did not have an overall strategy guiding the formation of bilateral FTAs as a trade policy option. The new government of Indonesia under President Yudhoyono seems to be moving ahead on forming bilateral free trade agreements (FTA). The push for the new government to engage in bilateral FTAs with Indonesia's major trading partners was given by the Indonesian Chamber of Commerce and Industry (KADIN). This was contained in their 12-point recommendations to the new government. The new Coordinating Minister for Economic Affairs was the outgoing chairman of KADIN, and thus it was logical that the new government would adopt it as its policy.

Soesastro (2005), 21-22

The results indicate that LMR has a highly significant impact on trade. In particular, a higher LMR increases c.p. the comparative advantage for capital-intensive pro ducts and decreases c.p. comparative advantage for human capital- and land-intensive products. The Relationship ij as well as the HO p I coefficients are all of the common expected sign and are mostly significant

Huber (2011), 4

The employment elasticity with respect to total GDP or income provides an interesting insight. First of all, the employment elasticity with respect to the total income for the agricultural sector appears to be negative. That means higher total income will lead to lower agricultural employment. This, in essence, is in line with the structural change theory proposed by Chenery and Syrquin (1970). Overall, the above results

suggest that increases in agricultural income will have two counteracting influences on agricultural employment. On one hand, the expansion of the agricultural sector will boost employment in the sector, but on the other hand, the expansion of the economy as a whole decreases employment in the sector as workers reallocate their services to non-agricultural activities.
On the other hand, the coefficients of employment elasticity with respect to total income for industry bears a positive sign. This implies that the net employment creating capacity is higher for industry, since both the sectoral effects and the overall effects are additive. Again, this result agrees with the structural change theory.

Islam (2000), 18

SMEs and employment

Regional autonomy

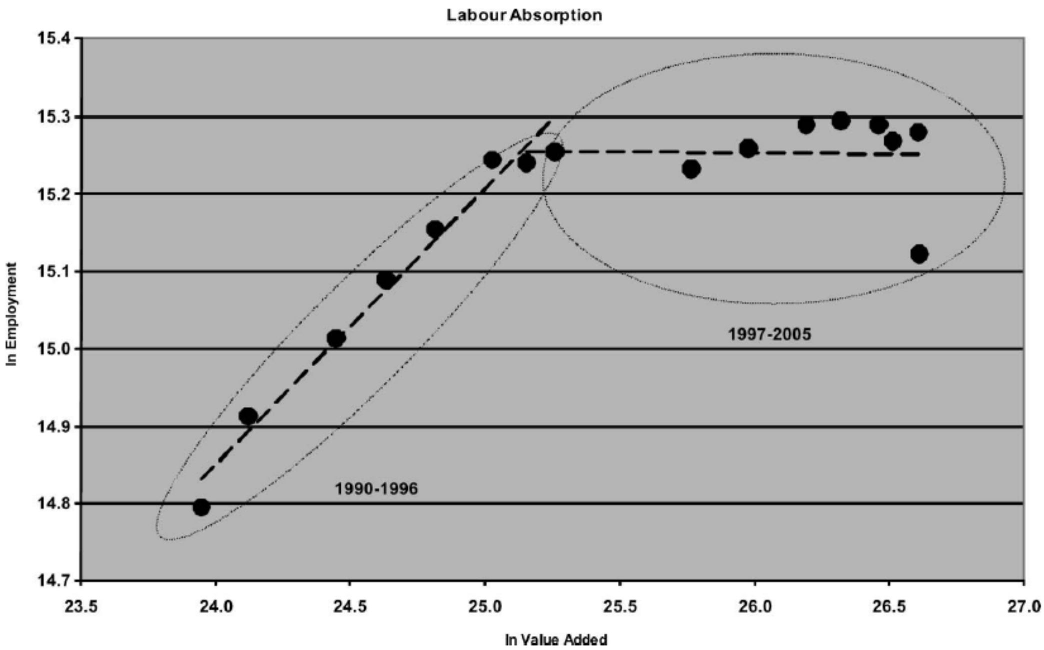
Thus, changes in unit labour costs reflect the net effect of changes in nominal wages and changes in labour productivity. ULCs rise when nominal wages rise faster than labour productivity. To understand this, recall that labour productivity can be measured as the quantity of output produced for a given labour input. If labour productivity increases and nominal wages remain unchanged, then unit labour costs would decline, ceteris paribus. Conversely, if labour productivity remains unchanged but nominal wages rise, then unit labour costs would rise. ULCs are useful as an indicator of competitiveness, both economy-wide and at a sector level, as a supplement to the real effective exchange rate.

The general picture is one of continuous increase. Prior to the crisis, ULCs were growing quite strongly, for the period 1991–1996 by more than 6 per cent per annum, broadly similar to the increase in real value added per worker. However, they rose very sharply during the crisis period, 1997–1999. This was primarily the result of rising nominal wages (though sharply falling real wages), combined with declining labour productivity, the latter principally the result of sharply declining capacity utilisation rates as domestic demand collapsed. Since the crisis, ULCs have continued to increase, albeit at a slower rate, similar to that of the pre-crisis period. By 2005, ULCs on average were about 3.5 times that of 1990. Thus there has been a sharp increase in ULCs, indicating that nominal wages have increased much faster than productivity growth, with the result that Indonesia has lost some of its labour cost competitiveness.

Haryo (2010), 1095

manufacturing employment was highly output responsive over the period 1990–1996. Since 1998, however, there has been virtually no manufacturing employment growth, despite output growing at an average of 5.5 per cent.10 This outcome reflects both the general effects of slow employment growth in aggregate and the specific effects on major labour-intensive activities such as TCF. Since it has persisted for several years after the recovery, beyond the period when any 'labour hoarding' effects would have been felt, the primary explanation for the outcome has to be the labour policy regime. In interpreting the results, recall that the industrial survey data refer only to firms with at least 20 employees. It is possible, indeed likely, that some of the employment growth hitherto occurring in the 'formal' sector has been pushed into the less regulated (and poorly paid) informal sector of manufacturing. Employment trends in the latter are not well documented, and so this possibility remains a hypothesis pending better data.

Haryo (2010), 1095-96.




Haryo (2010), 1097

This was a 'big bang' decentralization, motivated at a time of widespread inter-communal and ethnic violence, by a fear of territorial disintegration and occurring when the central government was at its weakest. They were also driven by a strong push towards democratization at both the central and regional governments. Owing to the scale and rapidity of change, centre-region relations are in state of transition, and are regularly being modified by new laws and regulations. A new modus operandi, widely accepted by all parties, is in the process of being established. Coordination and supervision procedures are thus being refined, especially as the central government is clearly unable to supervise almost 500 sub-national government units.

This reform has had two major implications for the business environment and domestic trade. The first is that there are new and powerful policy actors in Indonesia located outside the capital. Whereas in the past all significant administrative decisions were taken in Jakarta, licensing authority, a range of business-support facilities, and legal sanctions now reside with the regional governments. Given Indonesia's great diversity, and as centre-region relations become more settled, regional governments can be expected to compete for footloose labour and capital through the provision of clean, efficient, business-friendly environments.[22] The second implication is that ambiguity in centre-region relations, combined with the political vacuum at the centre (especially in the immediate post-Soeharto period), has created a significantly more unpredictable business environment. As Brodjonegoro (2004, p. 139) observes, 'decentralization has increased uncertainty in doing business at the local level', principally owing to the emergence of many formal and quasi-legal business charges, with little commensurate improvement in public service provision.

Bird (2007), 26-27.

Indonesian trade policy making broadly occurs in an institutional vacuum. The ad hoc inter-departmental Team Tariff sets tariffs on an informal basis, without reference to clear objectives and rigorous analytical research, and in a largely non-transparent manner. It has no control over other trade barriers, principally non-tariff barriers, and here as noted the more protectionist line ministries seek to by-pass the Team. Such a policy making structure worked well in the 1980s when the technocrats were in control, the main game was to persuade the all-powerful president, and the strategy of Soesastro's (1989) 'low politics' guided policy reform. But it is much less well suited to an era of assertive legislatures and noisy civil society, where vocal elements of both are predisposed to protectionism, and where a constituency has to be won over by argument.

Bird (2007), 32

Moreover, trade policy reform 'works' when it delivers results and thereby wins over a constituency for further reform. This in turn requires competent macroeconomic management (to ensure that the exchange rate does not overshoot), institutions such as a customs service which ensure the speedy and unhindered movement of goods across international borders, and labour markets which translate economic growth into growing employment opportunities. Since the crisis, Indonesian economic policy has been just adequate with respect to the first variable, weak on the second, and notably deficient on the third. Consequently, it is possible for opponents of the continued maintenance of open borders to mount a critique of it on the basis of the country's indifferent export performance (noted above), even though the root causes lie elsewhere.

Bird (2007), 33

A third general conclusion is that trade reform is about much more than barriers to commerce at international boundaries. Perhaps unexpectedly, this is where major problems arose in Indonesia after the crisis. That is, a weakened central government has been able to maintain broadly open international boundaries, but it has been powerless to prevent the proliferation of a range of quasi-legal and blatantly extortionist exactions on domestic trade. Combined with a far-reaching decentralization program and under-investment in infrastructure – both common features of post-crisis countries – Indonesia risks fragmenting into a series of poorly connected regional economies, some of which may be more integrated with neighbouring states than with the rest of the country

Bird (2007), 33