

Indonesia and FTAs in East Asia

By Hadi Soesastro

IN 2004, it is probable that more and more free trade agreements (FTAs) or preferential trading arrangements (PTAs), including East Asian economies, are going to be negotiated. One problem is that these activities may divert attention and energies away from the efforts to form a region-wide East Asian Free Trade Area (EAFTA) and to strengthen the multilateral trading system. Many bilateral and sub-regional FTAs which has been formed in the region are more or less very different in scope and depth, and this could make their future amalgamation a nightmare.

The region may have gained a greater momentum in forming FTAs since Thailand has followed in Singapore's footsteps. It is also notable that Indonesia has finally shown some interest in forming bilateral FTAs. There is a committee on FTAs within the Indonesian government, but its agenda is largely driven by the offers made by other countries to form FTAs with Indonesia. Unlike Singapore or Thailand, Indonesia has not been proactive in choosing countries as potential FTA partners. The Indonesian government does not have an overall strategy guiding the formation of bilateral FTAs as a trade policy option. The Economic Minister is not a promoter of bilateral FTAs. The FTA Committee is under the purview of the Minister of Industry and Trade, whose policies on this matter remain unclear. Indonesia's involvement in forming bilateral FTAs is likely to be an extremely slow process.

It is likely that a political decision to begin official negotiations will not be made in this election year and will have to wait until a new government is in place. Negotiations within the ASEAN framework (e.g. ASEAN-China) will continue but they will not receive sufficient attention from Indonesia's political leaders and the ministers in charge. Much responsibility will be left to the bureaucracy that acts under no clear guidance.

In a sense Indonesia is a newcomer in

forming bilateral FTAs. It is examining this trade policy option more seriously largely in response to offers by a number of countries. It will definitely give priority to FTAs with countries that it regards as politically and economically important, namely Japan and the United States. These two countries have made approaches to Indonesia at the highest level. President George W. Bush launched the Enterprise for the ASEAN Initiative (EAI) at the APEC Summit in Mexico. This was followed up by a visit by U.S. Trade Representative Robert Zoellich to the region, including Indonesia. A Japan-Indonesia FTA was proposed during President Megawati Sukarnoputri's official visit to Japan in 2003.

To a large extent, Indonesia's interest in bilateral FTAs has been aroused by the recent upsurge of FTA negotiations involving its closest neighbors. Indonesia was rather indifferent when Singapore began the process, and later concluded a number of agreements, because it did not see this as threatening. In fact, some Indonesian people thought that Indonesia could benefit from Singapore's FTA as it might use Singapore as a back door to penetrate other markets. Of course Singapore's FTA partners will prevent this from happening, among other things by insisting on rather restrictive rules of origin (ROO) provisions. This certainly appears to be the case with the Singapore-Australia FTA.

When Thailand began to show interest in negotiating a host of FTAs, including agreements with the main markets for Indonesia (such as China and Japan), a sense of unease began to emerge, leading to more serious consideration on the need for Indonesia to do the same, essentially for defensive reasons.

Indonesia has a very modest list of candidates with which it might study the prospects for bilateral FTAs. Most of these candidates (e.g. Pakistan, Bangladesh, Chile and South Africa) are

not significant trade partners. FTAs with any of these countries may be considered mainly as training cases for the bureaucracy to engage in such negotiations. However, this will only be useful if such negotiations could start now. It appears that they no longer are countries with which Indonesia will negotiate first.

The main challenge for Indonesian negotiators is that they will begin this exercise by negotiating with the most important and the most difficult countries – Japan and the United States. If they can do this right, they will obtain substantial pay-offs. But the risks are also very large. It cannot leave the negotiation process to a bureaucracy that lacks expertise and ability. Unfortunately, Indonesia does not have experienced negotiators like Singapore's Tommy Koh to rely on.

Indonesia can draw on the Singapore-Japan or Singapore-U.S. agreements as a model for its negotiations with Japan or the United States, but cannot make use of them. The Singapore-Japan agreement largely dispensed with agriculture, which will be an important component in an agreement between Indonesia and Japan. The Singapore-U.S. agreement largely deals with sectors and areas beyond goods trade that Indonesia is least prepared to address.

The learning process will be the most important aspect of the negotiations. In fact, some kind of facilitation or technical assistance by Japan or the United States should be built into the negotiating process.

It is not immediately clear whether Indonesia should negotiate these bilateral FTAs in some sequence or simultaneously. It is also not clear how its ongoing negotiations with China under the ASEAN-China framework agreement will affect other negotiations. Indonesia-China trade relations are full of contradictions. Some quarters in Indonesia are greatly alarmed by the prospects of a radical opening up of the Indonesian

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A Japan-Indonesia FTA was proposed during President Megawati Sukarnoputri's (left) official visit to Japan in 2003

market to Chinese products. Others see great opportunities being created by an FTA with China for entering the Chinese markets. It remains to be seen which side can exert the stronger pressures on policy makers.

In the domestic arena, immediate efforts need to be made to clearly understand which sectors are likely to gain most from the FTAs and which sectors will be adversely affected by them. The former is necessary so that Indonesia can focus its efforts on those areas. The latter is important so that ways can be devised to lessen the likely negative impact. Domestic adjustments and reforms will have to be made. It is often the case that bilateral or regional FTAs can help to promote domestic reforms. Indeed, an agreement with the United States will have the greatest impact on Indonesia's economic reform agenda. Demands for reforms made by the U.S. side will be substantial. However, this should be done with great care as widespread impressions of bullying by the United States will be counterproductive.

It is unavoidable that each bilateral agreement will be seen as tailor-made. This is exactly why it is difficult to amalgamate the many bilateral FTAs into a region-wide agreement at a later stage. Having this in mind, the Pacific Economic Cooperation Council (PECC) Trade Forum has proposed an "APEC Common Understanding on Regional Trading Arrangements" that lays out a set of guidelines for ensuring that FTAs in the APEC region contribute to the achievements of APEC's objectives. East Asian countries should seriously take these guidelines into consideration when establishing bilateral or sub-regional FTAs. In its negotiations with the United States and Japan, Indonesia can be guided by such "common understanding".

The elements of this "common understanding" include the following:

1. Relation to the "pathfinder" concept: FTAs involving APEC economies

should be fully consistent with APEC objectives and principles, and participation in the network of FTAs within the APEC region should, over time, become open to all the APEC economies;

2. Conformity with APEC liberalization objectives: The liberalization and facilitation provisions of FTAs between economies must be extended to all APEC economies by the Bogor target dates. The timetable for liberalization should be consistent with the Bogor dates. Most favored nation (MFN) liberalization should proceed in parallel with the implementation of FTAs. All MFN barriers should be reduced to moderate levels as soon as possible. Elimination of peak tariffs and tariff escalation must be given priority;

3. Conformity with APEC principles in the Osaka Action Agenda: (a) Concessions provided within FTAs will be made available to all APEC members as soon as circumstances allow, but no later than the Bogor target dates; (b) It should be recognized that consistency with GATT Article XXIV and GATS Article V is a necessary but not a sufficient condition for ensuring that FTAs contribute to the achievement of the APEC objectives; (c) FTAs should cover trade in both goods and services and should cover all sectors, with sensitive sectors being liberalized on a slower timetable; (d) Peer review should be allowed before the FTAs are finally concluded; (e) Peer review should provide an opportunity for discussion of any problems that FTAs being reviewed may be causing for other APEC members and ways of resolving those problems.

4. Consistency with other APEC principles: Where relevant, provisions in FTAs should be linked to the specific sets of principles that APEC members have adopted (such as Non-binding

Investment Principles, Principles on Competition and Regulatory Reform).

5. Promoting convergence and minimizing "spaghetti bowl" problems: (a) The rules of origin should be as straightforward as possible, and should be transparent, clear and consistent, and should not impose unnecessary compliance costs; (b) The adoption of harmonized provisions across FTAs should be encouraged, and this could be achieved by making use, whenever possible, of international standards and APEC-wide agreements and processes;

6. "Best practice" guidelines for PTA liberalization: The liberalization of both goods and services within FTAs should be made progressive and automatic.

7. Development dimension: FTAs should allow for assistance in capacity building to be provided.

To provide greater assurance that FTAs in East Asia could lead to a region-wide arrangement, leaders of the ASEAN Plus Three (China, Japan and South Korea) should agree to immediately launch a systematic effort to develop region-wide guidelines that will eventually be adopted as the basis for creating an EAFTA. It is here where Indonesia, and perhaps also Japan, should focus their attention and make the biggest investment. The formation of bilateral FTAs is, after all, a misguided effort. **JS**

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