barriers and to facilitate the resolution of differences. The EU applies control standards for food and food product hygiene, animal health and welfare, and plant health. It also provides rules on appropriate labelling for foodstuffs and food products. This policy follows a so-called 'From the Farm to the Fork' approach that ensures a high level of safety for foodstuffs and food products at all stages of the production and distribution chains. This policy is based on international standards and in line with WTO SPS Agreements.

In order to improve understanding on the SPS measures used by both parties, the EU and Indonesia should intensify cooperation aspects in the area of SPS and animal welfare. Common EQI issues for Indonesian industries marketing their products in the EU are related to testing and accreditation as in the case of fish and agri-foods, food safety and SPS requirements. The Indonesian National Agency for Food and Drugs (BPOM) is cooperating with the EU to establish a National Rapid Alert System for Food products in Indonesia. Through this program, the EU is providing technical assistance to strengthen national capacities in the risk management for food safety through establishing a national Rapid Alert System for Food in Indonesia. The mechanism gathers and analyzes food safety information coming from border inspections and domestic market surveillance.

5.4. Rules of Origin

Rules of Origin (RoO) should be facilitating, not hampering trade. The Vision Group encourages the future negotiators to take a liberal view on this with a view to maximizing beneficial impacts. The CEPA should adhere to a RoO regime which is trade and investment friendly, also taking into account the ongoing reform of current EU RoO and planned negotiations with other ASEAN member states.

5.5. Safeguards measures

Safeguards should be used as emergency measure only when imports surge in a manner disruptive to the economy. Indonesia and the EU are advised to build a joint mechanism to decide on future safeguards, based on objective criteria and short exit periods. This should be seen also in light of the dialogue/governance structure discussed in chapter 13.

6

Market access in Services

Services are of increasing importance to EU and Indonesia trade (representing in 2010 over 16% of overall trade). They are also an important component supporting the efficiencies of trade in goods. A strong part of the value-added in goods, once reaching consumers or business-to-business customers, originates from services. In many manufactured goods, services may account for one-third or more of value-added: the export of so-called "business services" are indeed now the major part now of the international trade in services. **Modern FTAs therefore incorporate significant market access obligations in both goods and services.**

In order to be competitive in any location, one needs to take both goods and services conditions into account. In addition, there are solid economic arguments for services best practise and external opening under a CEPA for the performance of services sectors as such, given their increasingly prominent role in the economy – in Indonesia and the EU. This is for example the case of information and communication technology services which contribute to spreading digital technology and allow SMEs to do business worldwide through e-commerce. This is even more so in the case of financial services, which contribute to the financing of trade and the development of the local economy through lending. Insurance services are a back-bone of trade in goods, but also to the social security and pension systems and the financing of long term infrastructure projects. **For the CEPA to be meaningful in this respect, it should therefore be significantly above initial offers presented in the context of DDA services negotiations.** Both parties should commit to bind under the CEPA the existing current level of practice in the various services sectors, i.e. agree to consolidate their current level of opening to foreign economic actors. Moreover, both partners should commit to certain levels of new openings in key services, differentiated by mode and by sectors, in such a legal form that they effectively create new business opportunities and legal certainty for providers from the partners and for investors in services sectors. The principle of 'asymmetry over time" (the EU opening immediately or rapidly, and Indonesia on schedules with a longer time horizon), differentiated by sectors and/or mode, could also be applied here.

Whereas consumption abroad (mode 2) might not represent a major problem between the two partners, selected (and perhaps conditional) opening under cross border services (mode 1) and especially further commitments under commercial presence abroad (mode 3) would need to be negotiated. The Vision Group is not proposing a detailed negotiation agenda in this area as contacts between negotiators could explore in greater detail the options and their feasibility. Still, strategic vision matters and the Vision Group suggest a few areas and aspects of services which might deserve attention (see annex 1 for details). These include investment restrictions in some Indonesian services sectors, which have to be in accordance with best practise of a modern economy. Their reform and opening could greatly contribute to the long term improvement of infrastructure in the Indonesian economy.

7

Investment

The EU is the leading FDI originator in the world, but Indonesia is only a moderate recipient: only 1.6% of tEU's FDI to Asia over the last ten years went to Indonesia and the EU's FDI remains heavily concentrated in China and Hong Kong. Nevertheless, Indonesia hosts around 700 companies of EU origin with an investment of EUR 50 billion and direct employment of 500,000 people; the multiplication factor to indirect employment is also very high.

EU companies have a greater tendency to invest in Indonesia, rather than simply trade. This is favourable for Indonesia's trade balance with the EU (€7 billion in surplus in 2010). Investment also provides employment, technology transfers and mutual prosperity. As Indonesia tries to dampen short term capital inflows ("hot money") in favour of long term capital investment, removing equity limitations would be a positive factor.

The Vision Group has come to the conclusion that investment between the EU and Indonesia can significantly expand. Easy gains could be made, if issues such as FDI limits, protection, IPR enforcement, regulatory consistency, infrastructure, tax policy & local content requirements are effectively tackled.

In 2009 Indonesia introduced a *one-stop service* for foreign investors in many districts. While there are still some problems with its implementation, it has helped to speed up the licensing process to establish foreign-owned companies in Indonesia. It is necessary to conduct capacity building for government officials in charge of licensing procedures and avoid a too high a turnover of trained officials. Indonesia should carefully consider the deterrent effects of equity restrictions in a world of many choices of locations. While an immediate change in the Negative List appears unrealistic, an incremental relaxation during a transitional period would be favoured by the Vision Group.

In respect of Indonesia's investment in the EU, major concerns include compliance with various technical, sanitary and, environmental requirements, marketing standards, product safety, packaging and labelling and some other industry-specific requirements. It will perhaps take a relatively long while before direct investment overseas rises in importance in the agenda of Indonesian companies.

The EU's potential priority sectors for investment in Indonesia includes infrastructure, chemicals, food, metal, manufacturing and services (banking, express delivery, and logistics and construction).

7.1. Attract further EU FDI to Indonesia: Pre-Establishment/facilitation

Limitation of foreign ownership: all equity caps and joint-ventures requirements are considered by investors as an impediment to do business. The preference of foreign investors is to have control over their investment. If a foreign company cannot have majority ownership, it means that it cannot run the investment as they would wish. Hence, it will not invest in the same way as in countries where this would be possible. It will not transfer technology, know-how and other in-house company expertise, since it would run the risk of losing these essential assets of the company. In fact, joint-venture obligation and equity caps – measures often used by countries as tools aiming at sharing the expertise with the local partner – are most of the time missing their goals and prompt investors to look for alternatives solutions in other more welcoming countries. These limitations still exist in some sectors on the current Negative List of Investment. However, this List will be reviewed regularly and for some sectors may become less restrictive.

Local content requirements: Global companies have often global product strategies that are established before entering one specific market. If the local content requirements fixed by a country are too stringent to a point that it would require the company to modify its production or supply chain, this is perceived as a disincentive to invest in such a market. See also Chapter 9 on Infrastructure.

Transparency and clarity in the regulatory framework: Since the early 1990s Indonesia has made significant progress in respect of decentralization and regionalization, which in some instances has created additional layers of decision making and competencies. The Vision Group advises to continue to ensure that all levels of government, central, provincial and district decide and implement decisions about FDI in a coordinated and simplified manner.

Independence of regulatory bodies: Since the introduction in Indonesia of the fair competition law in the 1990s, significant progress has been made to eliminate unfair competition. The Commission overseeing this law is an independent body. The Vision Group advises to review regulatory authorities to ensure they can operate independently.

Taxation climate: From the Vision Group perspective, Indonesia and EU investors would benefit from a transparent and predictable treaty with all EU countries. In fact, Indonesia has ratified Double Taxation Avoidance Agreements with as many as 19 out of 27 EU Member States.

7.2. Investment protection post-establishment

As of April 2011, Indonesia has signed 66 Bilateral Investment treaties (BITs) with its counterparts, 16 among them with EU Member States (Belgium - Luxembourg, Bulgaria, Czech Republic, Denmark, Finland, France, Germany, Hungary, Italy, Netherlands, Poland, Romania, the Slovak Republic, Spain, Sweden and the United Kingdom).

These BITs give legal protection for post-establishment phase of investment. The elements of this agreement cover legal guarantees for:

» Non-discriminatory treatment
» Nationalization / expropriation
» Compensation for losses
» Subrogation
» Transfer
» Dispute settlement

These elements have been accommodated by Indonesia Law Number 25 of 2007 concerning investment and are in line with internationally accepted principles. **The Vision Group recommends that the EU and Indonesia would conclude an ambitious investment protection agreement covering all EU member states**[4]

7.3. Investment Promotion

Investment promotion efforts need to be enhanced in order to attract potential investment sources from EU countries into Indonesia. In fact, while the EU overall is the second largest investor in Indonesia, this is mainly thanks to some of the Member States. Promotion in the other EU countries could lead to further investments in Indonesia. Similarly, the EU could promote Indonesian investments to the EU as well.

4 According to new EU competence on investment provided for in the Lisbon Treaty.

Cooperation and capacity building

Thanks to the opportunities opened up by the **Partnership and Cooperation Agreement**, the EU and Indonesia have started cooperating in new areas such as on security issues, research and technology, human rights, cooperation on culture and education.

For the Vision Group, three pillars should underpin the successful industrial cooperation between the two economies: *liberalisation*, *facilitation* and *capacity building*. Based on experience, capacity building is becoming a critical tool to any successful bilateral economic agreement, especially in implementing economic agreements between an industrialised country and a developing country. Therefore, the conventional approach of liberalising an economy through reduction and elimination tariffs, in order to facilitate and boost the trade, is now complemented with targeted cooperation activities.

Based on analyses conducted it has been indicated that some Indonesian products, mainly primary products and selected manufactured products are competitive vis-à-vis European products. **It has also been shown that full trade liberalisation between the two sides is expected to create economic welfare and stimulate economic growth**. However, it is important to note that, since the size and strength of the economies is different and the relevant infrastructure of the EU is more developed compared to Indonesia, it seems unavoidable that liberalisation of trade will bring to bear considerable competitive pressure on some of Indonesia's industrial sectors. Therefore, it is proposed to support the adjustment of weaker Indonesian sectors via targeted cooperation.

Support for liberalisation is greatest when obtaining mutual benefits for both parties in a win-win situation. Ideally, both partners should define common interests in order to face future world economic development together. An important aspect of capacity building is that it can be undertaken immediately, even before CEPA finalisation, through existing programmes, such as the Trade Cooperation Facility and Trade Support Programme II. The Vision group has underlined that the CEPA concept is already working for the benefit of Indonesia through these existing programmes.

Tariff rates of both partners are already relatively low. Yet it is not easy for Indonesian products to enter the European market due to high standards and technical requirements. Similarly, Indonesian SPS rules do not recognise EU food safety standards, nor are EU technical laboratories recognised to test for Indonesian technical standards. **The Vision Group concludes that a key to the success of the CEPA that it must provide concrete means to bring industrial requirements, testing recognition and accreditation of certification, onto an equal footing and, if possible, to harmonise all of them around one set of international standards. This will facilitate the flow of goods between Indonesia and EU.**

Where the key to industrial cooperation is moving towards harmonisation of standards, CEPA will include specific actions to align to a common set of standards, based on international rules, and recognition of conformity assessment and certification systems. An example of an activity that would enhance cooperation, harmonise standards and hence improve market access of the EU and Indonesia is the accession of Indonesia to the UN/ECE agreement for Indonesia's automotive components. The UN/ECE deals with the standardisation of products, including automotive products for international trade. These international standards have already been adopted by 55 countries while Indonesia is now preparing its adhesion. Activities leading to the accession of Indonesia to this international agreement could be linked to dissemination programmes for the Indonesian automotive industry.

Providing information on standards and their technical substance from both sides is crucial to ensure that companies from both partners , especially SMEs, can comply with each other's requirements and realise the opportunities offered under the CEPA. One concrete example is to establish an EU-Indonesia helpdesk and standard information platform on each other's regulatory regimes.

Moreover, Indonesia would need to build up a strong certification and laboratory system to be able to fulfil technical regulations to enable its exporters to access EU markets. Several sectors could be targeted, notably: food and beverages, chemical products, agro-based industries, electrical and machinery components. **Similarly, EU products have difficulties accessing the Indonesian markets due to the prevalence of mandatory domestic technical requirements and that EU laboratories are not recognised to conduct testing to meet these standards.** As a first step, the cooperation programmes should aim at a better understanding of each other's regulatory frameworks and systems in order to facilitate market access. A strong emphasis should subsequently be put on building up the export quality infrastructure of Indonesia.

Cooperation should not only focus on market access but also through facilitation of direct investments, with a view to increasing the involvement EU firms in Indonesia to enhance access to higher technologies and export quality infrastructure. There is extensive scope for cooperation and technical exchanges in sectors where the EU possesses cutting edge technology and know-how. This would facilitate EU exports and investments while helping Indonesia to access advanced technologies and to upgrade associated human resources. For example the development priorities of the Indonesia National Industrial Strategy include electrification, food security and the restructuring of capital goods, identifying lead sectors such as:

- Development of green products and use of alternative energy (e.g. biomass and electrification)
- Automotives and aircraft industries
- Telecommunication/electronics products
- Pulp and paper
- Textiles and the apparel industry

9

Public Procurement, Infrastructure and Public Private Partnerships

Poor logistics and infrastructure discourage foreign direct investment and trade. The Vision Group strongly advocates that a CEPA will not realize anywhere near its full potential unless it goes hand in hand with comprehensive progress in infrastructure development. The direct link with a CEPA can be found in public procurement and local content requirements, both items which can hinder, slow down and diminish progress in large projects, either because local content is not available or because global companies have global product requirements. The Vision Group argues that European industrial companies and financial investors are currently hesitant to deploy their extensive resources pending fundamental progress on Public Private Partnerships. Below are some suggestions on how to do this.

First, a CEPA should discuss public procurement, notably in public infrastructure. The parties should agree on setting up transparency rules and negotiate additional levels of mutual access to the respective public markets.

Second, such a dialogue should cover the most important supply constraints in Indonesia, which lie in its logistics and infrastructure. This includes power, transportation, roads, and ports. For example, transportation costs are the highest in ASEAN. Indonesia does not take advantage of its unique archipelagic geography; it does not have a good international hub port. Domestic ports are also hindered by sub-optimal performance due to lack of capacity or poor management[5]. As a result there is a high degree of dis-connectivity[6]. External rating agencies have recently upgraded Indonesia's rating to BB+, one notch below investment grade.[7]All cite poor infrastructure as a downside risk to reach investment grade. **However, Indonesia is expected to reach investment grade in 2012, which could be a very good opportunity to attract more FDI, especially into infrastructure.**

Third, a fully functioning Public Private Partnership model (PPP) for infrastructure development including local companies and investors is critical to achieve progress. In December 2010 Indonesia put in place new PPP legislation and the first projects are under way. Commonly identified obstacles include poor planning, coordination and prioritization. Clarity on risk / return parameters need to be covered.

Fourth, Infrastructure projects will continue to require Government support in the form of guarantees for asset buy backs, to ensure and underpin minimum revenue and expected commercial returns. For this to work properly and to create incentives for investors, the exact type and level of support needs to be identifiable in clear cut frameworks. Indonesia cannot afford to default on any of its support obligations now that it is on the way to attain Investment Grade. To take on high numbers of full fledged payment guarantees puts that objective at risk. Indonesia therefore needs to be very selective on guarantee deployment.

The Vision Group therefore argues that FDI and local content restrictions (40% in procurement of goods, services, construction work, also for Public Private Partnerships) are hindering the progress of infrastructure development projects as they fail to create incentives and competitiveness for local and foreign companies. Local content is not necessarily available for certain projects so the requirement becomes impractical and a source of legal uncertainty. Such policies achieve the opposite of what is intended.

The Vision Group advocates a direct and substantial involvement of the **European Investment Bank (EIB)** in Indonesia's infrastructure development[8]. Another immediate opportunity consists in participation in and support for the **Indonesian Infrastructure Guarantee Fund (IIGF)** where additional capital and capacity building are both necessary[9].

The Vision Group recommends the Indonesian Government puts in place a single point of entry for firms and to reduce the complexity of the decision-making processes with regard to infrastructure projects, including dealing with certain aspects of regionalization.

The Vision Group also suggests a review of recently implemented legislation which has improved the legal framework for core infrastructure sectors, such as telecoms, electricity, oil and gas and water, but while also creating some additional barriers to infrastructure development. All European export credit agencies are open regarding Indonesia and there does not appear to be a competitive disadvantage for European companies in respect of export financing. It is not clear if Europe's export credit agencies collaborate sufficiently on bids involving multiple suppliers and there may be room for improvment on this. Meanwhile export credit agencies, especially from major industrial countries such as China, Japan and Korea, are fiercely competitive. The Vision Group argues that joint marketing efforts are necessary to create more proactive interest from European exporters and to attract European capital.

5 In a study on land transportation costs, LPEM-FEUI (2008) found that the trucking costs for a typical good using a typical truck in Indonesia (a number of provinces in Sulawesi, Java, and Sumatra were sampled) could reach as high as USD 0.34 per kilometre. This is higher than the average ASEAN, namely USD 0.22 per kilometre. A follow up study by LPEM-FEUI (2010) tried to measure the trucking cost in provinces that rely on water/sea transportation in addition to land mode. It was hypothesized that for archipelagic country, water and sea transportation should be an advantage. However, the study found that the cost could reach even higher at USD 0.50 per kilometre.

6 Domestic dis-connectivity implies sharp differences in prices even for basic commodities, where prices in remote areas can be double those of national averages. For example, the price of medium rice was around IDR 4,000 in Java, Kalimantan, Sulawesi, and Nusa Tenggara but IDR 10,000 in Paniai, Papua.

7 Standard & Poor's, 8th April 2011. FitchRatings, 6th April 2011

8 EIB supports viable public and private sector projects in infrastructure, industry, agro-industry, mining and services. Under the current mandate of EIB - covering the period the 2007-2013 - the EIB is authorised to lend up to € 1 billion into Asia for financing operations supporting EU cooperation strategies. There are currently no EIB projects in Indonesia.

9 IIGF was set up in 2010 as a 100% State Owned Enterprise and is designed to be a credible guarantee provider. It acts as insurance company and collects insurance premiums. Initial capital was Rp 1 trillion ($ 110 million); plus another Rp 1 trillion injected in 2010; hence total initial capitalization was $ 220 million. IIGF was developed with assistance from the World Bank which provided $ 500 million of guarantee support and from the Temasek Foundation which provided S$ 474,000

IPR: GIs and Enforcement

Strong Intellectual Property Rights (IPRs) protection is crucial to stimulating entrepreneurship and fostering a creative economy. Counterfeit products are a threat to public health and safety and a good protection of IPR is key to research and development. Furthermore, trade and direct investments are attracted by high standards of IPR protection. Improving the legal framework and strengthening enforcement (border measures and domestically) constitute principal incentives for investors as well as for new entrepreneurs.

It is also in the interest of investors and companies that both parties provide for a system of administrative protection of IPRs, avoiding costly and burdensome legal action before Courts. For these reasons, a CEPA should include a full and detailed chapter on IPR, the objectives of which should be to:

- Facilitate the production and commercialization of innovative and creative products, and the provision of services, between the Parties.

- Increase the benefits from trade and direct investment through the adequate and effective protection of intellectual property rights and the effective enforcement of such rights.

With both parties complying with the TRIPS agreement, the IPR chapter should cover all categories of intellectual property namely: copyright and related rights, patents, trademarks, designs; layout-designs, geographical indications, protection of undisclosed information and plant variety rights.

Not surprisingly, both parties expressed special interest as regards Geographical Indications (GIs) since they are both rich in traditional knowledge, agriculture and foodstuffs. Both Indonesia and the EU have already developed a system of protection for their GIs. Economically and culturally, GI protection is becoming an increasingly important issue for producers and an important part of development strategy. GIs are not only to be seen as a way to grant a fair financial return for high quality products but also as a way to keep farmers and communities in rural areas and to manage land properly. Protection of GIs is therefore also a way to develop parallel economic activities (such as processing industries and tourism) retaining value added in targeted areas thereby benefiting regional development.

The Vision group recommends that the level of ambition as regards GI protection should be high. Being part of a CEPA, GI/ protection should go beyond TRIPS obligations for foodstuffs and provide for extension of the protection at least to TRIPS article 23 level (referred to as TRIPS +).

To support Indonesia on these issues, the EU is already providing capacity building on IPR in the ASEAN region through various programmes (ECAP I through to ECAP III). However, further capacity building and facilitation may be needed for Indonesia in order to accomplish effective implementation of such IPR provisions. This cooperation may include exchange of information and experience on issues such as best practice, promotion dissemination, streamlining, management, protection and effective application of intellectual property rights, the prevention of abuses of such rights, and the fight against counterfeiting and piracy.

11

Competition Policy

Competition policy is a necessary means to create equal, non-discriminatory, and level playing fields in the two economies. Fairness in business activities without distorting competition is welfare enhancing to consumers in the economy. Fair competition will induce greater efficiency and productivity, in turn resulting in higher income levels and higher growth trends in the medium run. Competition policy should be effective in addressing unfair business practices that distort competition.

Many countries have established competition policy based on widely agreed principles whilst adjusting its aplication on to local conditions and to the business climate in their own economy. The trading partners will therefore have distinctive ideas and approaches towards competition policy

To ensure that companies effectively have equal access to each other markets, the Vision Group argues that the CEPA between Indonesia and the EU should include some disciplines that both parties would agree to implement through their respective competition laws. They might, for instance, agree to prohibit and sanction certain restrictive practices and transactions involving goods or services which distort competition, trade and investment, such as cartels or monopolistic abuses by companies and anti-competitive mergers and/or acquisitions. This would imply that anti-competitive practices will not be tolerated by the parties and would be subject to effective enforcement action, when they lead to harming consumers and higher prices. However in a longer term perspective, some sectoral exemptions from competition could be reconsidered. Competition law should also apply to state-controlled enterprises as this may help in fostering greater efficiency.

It would be important that the agreement would contain provisions that prohibit certain types of subsidies and state aids, which are considered to be particularly distorting thereby affecting trade and investment between the parties, in the letter and spirit of the WTO Agreement on Subsidies and Countervailing measures, and possibly go beyond it.

Recognizing that competition policy could contribute to creating a conducive, stable, and predictable development for trade, which is particularly important for small scale investors who decide on investing in Indonesia, it is important to establish closer cooperation in the field of competition policy, such as:

- Exchanging information concerning the relevant imposition of competition policy measures.
- Include provisions in the CEPA on consultations and dialogues on all matters relating to competition policy.
- Enhancing capacity building such as providing training, education, human resources development, and technical assistance, and possible exchange of staff or traineeships.
- Exploring the merits and scope of possible cooperation between the Competition Supervisory Commission of Indonesia and the European Commission.

12

Sustainability:
Environment as a Competitive advantage

Indonesia has long recognized the importance of improving the economic and social fabric of the Nation as a prerequisite for achieving environmental goals. It is best expressed by President Susilo Bambang Yudhoyono who has emphasized the importance of pro-poor, pro-job, pro-growth and pro-environment policiy. For the Indonesian government, the objective of "Sustainable Trade in Indonesia" is initially associated with trade that should not harm the environment (the first pillar) and this has been extended to embrace social concerns (the second pillar), and which finally includes the importance of economic growth (third pillar) as the basis to meet environmental and social goals.

The EU shares this same strategy of sustainable growth as embodied in the Treaty establishing the European Union as well as various policies and laws.

The Vision Group argues that sustainability is a political necessity but also an inevitability driven by consumer tastes increasingly demanding "environmental friendly products and services". It was identified that, if embraced and always put alongside growth objectives, this approach can also produce win-win solutions which combine sustainability and profitability. Namely, sustainability can be turned to profit and to advantage in our trade and investment relations.

The Vision Group identifies that a CEPA **should include concrete measures to promote the greening of EU-Indonesia trade and direct investment** while creating growth and jobs.

In the public sector, partners will be encouraged to work with the Government of Indonesia Ministry on Sustainable Trade by addressing the above three elements from the trade perspective.

A CEPA should, therefore, also include structures that ensure any sustainability policy neither accidentally impedes trade nor restricts growth or job creation. The recent example of laws against illegal logging is a good case in point where this environmental concern was jointly tackled by Indonesia and the EU but in a manner that actively increases and enhances Indonesia's competitiveness and access to the EU timber and timber product market.

Both Indonesia and the EU passed laws against illegal logging. This was not enough: legal timber might find problems entering the EU if buyers and authorities were unsure if it was legal or not – threatening jobs and growth. For this reason, the EU and Indonesia have agreed a **Voluntary Partnership Agreement**, effectively a form of mutual recognition, through which local SVLK legality origin certificates will be accepted by EU authorities as proof of legal origin and will be allowed into the EU. This assumes the Indonesian authorities implement the new SVLK effectively. This is the type of action the Vision Group argues should be incorporated in the CEPA – acceptance of an environmental policy (combating illegal felling of Indonesia's forests) but by designing actions that not only secure the €700 million of existing trade in wood products from Indonesia to EU but also gives Indonesia a chance to expand its market in the EU, taking market share from other countries who do not have a similar scheme and cannot offer the same level of "legality" assurance. Other sectors where such an innovative pro-environment, pro-growth, pro-jobs and pro-poor approach can be developed include palm oil and fisheries.

Consumers are increasingly demanding environmentally sustainable products and services across all areas. Industry is changing its operations to meet this market trend. European businesses already have high levels of compliance with the UN Corporate Social Responsibility definitions. A number of global leaders have integrated environmental concerns in corporate culture and responsibility. This has resulted in the use of cleaner production technologies, selected sourcing of raw materials with favourable carbon footprints and in general embracing a culture which is environmentally friendly by reducing energy consumption; and optimizing logistics etc. We recognize that the main driver behind this corporate change is market driven as consumers and corporate customers have increasingly shown a preference to source from environmentally friendly companies combined with growing awareness of shareholders to the global challenges faced.

Together Indonesia and the EU can drive this transformation enabling Indonesian manufacturing to move up the value chain in a sustainable manner, branding goods with higher value thanks to being sustainable and growing the business opportunities for both parties.

Capacity building and trade facilitation should be designed with these sustainability objectives in mind. Specifically there should be a framework of mutual understanding of the value of long-term sustainability overriding short-term economic gains; for example converting power plants to use more sustainable sources of fuel, transforming Crude Palm Oil production by reducing greenhouse gas emissions, implementing production methods and certification when relying on standards which enable goods to compete with quality and low carbon footprints.

In short, the Vision Group recommends that **CEPA should include concrete measures to promote green elements in EU-Indonesia trade and investment**, while creating growth, value and jobs. This must evolve to a competitive business model which benefits both parties. This can provide a platform for fighting climate change and protecting the environment.

13

Governance/Dialogue Structure

To secure the good functioning of a CEPA, effective institutions, institutionalised and continuous dialogues involving governments and business should be put in place. The strong dialogue that Indonesia and the EU currently have is proposed to be institutionalised under the Partnership and Cooperation Agreement. This would include annual ministerial meetings as well as a technical Working Group on Trade and Investment which would meet twice a year, fed by sectoral dialogues (currently investment, pharmaceuticals, food & beverages and industry & environment). These meetings should incorporate business and / or work with the recommendations of the institutionalised EU Indonesia Business Dialogue.

This combination of business and government dialogues, technical expert cooperation and financial cooperation **is a deliberate strategy to ensure Indonesia sees and obtains advantages from the EU-Indonesia commercial alliance.** This has been a feature of EU - Indonesia relations and will remain a cornerstone of future relations. Some examples in palm oil, timber and fisheries where this deliberate constructive strategy is being pursued today help to prove the point.

The Indonesian government has shown impressive commitments in each of the above areas and in promoting constructive dialogue with the EU. The successful EU Indonesia Business Dialogue in Jakarta in December 2010 has provided a good example. . Thanks to the joint work and leadership of Indonesia's Chamber of Commerce (KADIN) and the European chambers, supported by Ministers of Trade, Industry and Economic Cooperation, a concrete and workable set of recommendations on trade, investment and business were agreed and are currently being implemented and followed up.

The CEPA should have solid **'governance'** based on trust, friendship and rules. The specific follow-up of the CEPA treaty in its various areas of policy and capacity building requires permanent cooperation and consultation. Nevertheless, no matter how 'deep' economic relations are or will become, differences of opinion will emerge under any agreement anywhere in the world. The Indonesia-EU CEPA will be no different. Differences of opinion should not be allowed to simmer, let alone, to turn into trade conflicts. The recent experience in timber shows that dialogue and concrete willingness to address the issues, possibly with technical cooperation, can work. The CEPA should explicitly incorporate this idea. Firm dispute settlement, based on recognized international practice of today, should be included. Without that option the CEPA would loose credibility. However, given and backed by a credible dispute settlement procedure, partners should nevertheless employ other mechanisms, including intense dialogue and technical cooperation, before resorting to the use of dispute settlement arrangements.

14

Communication strategy

The commercial ties between the EU and Indonesia are strong and relations are positive and constructive. But perceptions lag behind current realities. So consultation on and socialisation of the CEPA in Indonesia and the EU will be crucial – explaining the existing scale and complementary nature of relations, how CEPA is different from other recent economic agreements and how it will bring rewards to both sides. Some key elements of the Communications Strategy are as follows:

- **Communicate Early and consistently for Positive responses.** The most important lesson from Indonesia's experiences is that meaningful and comprehensive communications and dialogue must begin at the earliest stages of building a new bilateral or regional relationship in order for all stakeholders to feel involved and make positive contributions. Governments risk negative reactions if there is little room for such contributions because decisions have effectively already been made.

- **Communicate the Innovations in CEPA:** The consultation must show the stakeholders the distinct and very largely positive features of CEPA. It should emphasize three fundamental positive outcomes:

  » **A Dynamic Approach to Growth, development and Jobs,** showing how CEPA creates growth, jobs, development and capacity building in non-technical terms so people can see the clear value added of the CEPA.

  » **Boosting competitiveness in the Wider Strategic Context of Integration,** showing how CEPA will strengthen Indonesia's competitiveness in ASEAN and East Asia and help to avoid that EU agreements with other ASEAN neighbours result in a declining share of European trade and investment for Indonesia.

  » **Turning Sustainability into a competitive advantage for Indonesia and EU.** Too often, sustainability is seen as a negative issue. Countries having embraced sustainability have found that it is becoming a source of growth and jobs. CEPA will help Indonesia and the EU to exploit sustainability as a source of growth and profit.

- **Communicate how capacity building under the CEPA will help ensure Indonesia obtains benefits:** CEPA's comprehensive and dynamic structure of dialogues, technical committees and financial cooperation (detailed elsewhere in our report as "capacity building") will help companies to deal with problems and realise opportunities.

- **Compensating for the costs of Adjustment:** the costs of adjustment for those companies which might have to restructure in the short run (somewhat negatively, named "losers") are probably rather limited given the complementary nature of this CEPA. Nevertheless, be open about this possibility and identify such subsectors or companies as early as possible so that the necessary adjustment policies and compensation packages can be communicated at the outset. Early identification will help develop a more balanced debate and assessment among all stakeholders. It is also likely to induce such companies to anticipate the effects of CEPA and adapt their business before such costs might fall upon them. Indeed, given complementarity, "losers" might in fact often only see their growth affected somewhat, without having to cut capacity or fire workers. Capacity building as well as phased implementation and exemptions will assure this aspect is addressed to maintain positive returns from CEPA for both parties.

- **Stakeholder Dialogue and Engagement.** The communication strategy will target all stakeholders in EU and Indonesia, paying special attention to Parliament (and the European Council in the EU), specific Ministers and Government Officials in Agencies affected by the CEPA, chambers of commerce and the Business Community, the Academic Community, the Media, civil society (including Consumers and union groups). Direct dialogue, classical media (newspapers, radio etc), internet and social media will be used to provide information and promote dialogue with these stakeholder groups.

PRODUCT SECTORS OF SPECIAL IMPORTANCE

ANNEX I

PRODUCT SECTORS OF SPECIAL IMPORTANCE

Reality of trade and investment policies differ between sectors for reasons related to the stage occupied by an industry its life cycle, the prominence of an industry in relation to the issues of sustainability, TBTs, SPSS, environment, illegal trade and some other issues. The Vision Group finds it appropriate to single out a few sectors of products in view of the prominence attached to them in the Indonesia-EU relations without intending to argue in favor of an active industrial policy.

Regarding market access (goods, services and investments) mentioned in the report, the Group proposes to consider a number of sectors of special importance. Some examples are provided below. Note that these are discussed also in chapter 9 on capacity building.

Palm oil employs workers from more than 3.5 million Indonesian households. Exports are surging. The EU is Indonesia's second largest palm oil market. However, there are concerns in Indonesia over possible consumer boycotts and on assuring fair access to the trade preferences under the EU's Renewable Energy Directive. The EU and Indonesia have a strong dialogue on the issue, involving both industry and civil society, to:

- Re-assure Indonesia that the EU market remains open. There is no restriction on Indonesia's exports of palm oil. Growth in EU market demand for CPO has been strong.

- Facilitate discussion between industry and civil society to promote better mutual understanding so civil society is aware of CPO industry concerns and industry can adapt to changing consumer tastes in the EU where sustainability issues are increasingly important to consumers.

- Technical dialogues to ensure technical thresholds for obtaining EU trade preferences for palm oil as a renewable energy source are set fairly. Scientific data, findings and dialogue will then feed into future revision of thresholds.

Wood and paper products are another key export area for Indonesia to the EU. Indonesia has long wanted the EU to strengthen its controls against the import of illegal timber products into the EU. Indonesia was of the view that, as long as such trade continued into the EU, it effectively promoted illegal timbering in Indonesia. However Indonesia does not want any EU action to reduce the EU market for Indonesian timber and paper products. In response:

- The EU first passed a law requiring importers in the EU to guarantee the legality of the source of their timber and paper imports.

- The EU and Indonesia have signed a Voluntary Partnership Agreement (VPA) that will assure access for legal Indonesian exports. If Indonesia is able to credibly implement its national legality system (SVLK), such SVLK certificates will be sufficient to guarantee access into the EU markets.

- The EU has provided €40 million in financial cooperation to support the timber sector in Indonesia and will provide a further €10 million to help industry and civil society to implement the SVLK law.

In the area of **fisheries**, Indonesian exporters to the EU found it hard to comply and prove compliance with the EU's tough food safety standards. A technical dialogue has been going on for the last three years to strengthen food safety testing and data collection in Indonesia so as to improve the safety of fishery exports. Financial support is being provided to help Indonesia strengthen its national system for testing. And the number of shipments that are rejected in the EU for food safety reasons has reduced as a result.

The pharmaceutical sector in Indonesia is particularly promising for EU business and the Vision Group would suggest removing the decree 1010 (obliging local manufacturing before selling products), increasing the FDI cap to 100% and ensuring better data exclusivity. These measures would greatly incentivize new EU direct investments coming to this sector in Indonesia, which have been stalled since the 75% cap was introduced in 2007.

In the Food & Beverages area, particularly beef, dairy and alcohol, EU business is experiencing a number of measures that restrict (potential) imports, such as pre-listing of establishments and recognition of EU food safety standards.

Moreover on **courier services and EDS, the Indonesian** Postal law is restricting door-to-door delivery and maintains restrictive treatment of foreign firms and investors; local content in **telecom**, (wireless broadband) also restricts EU business involvement in key sectors.

In general the Vision Group recommends linking Indonesian and EU business associations, to support business dialogues and to follow-up with financing to help materialise the potential.

ANNEX 2

POTENTIAL GAINS/ECONOMIC ANALYSIS

Estimating ex-ante the overall economic impact of a trade agreement is an important step in defining policy priorities. In this endeavour, computable general equilibrium (CGE) models are most suited in offering a sense of the likely economic results of an FTA. This section summarizes the main results of two separate simulations: (i) a short term, static assessment of a future EU-Indonesia trade agreement; (ii) a longer-term, dynamic analysis, taking into account the synergies that can be created between new trade and investment opportunities. While the static assessment yields the gains for Indonesia in the magnitude of 0.1% of its GDP, the dynamic analysis taking into account accumulation of international investment flows brings the gains to 1.3%.

I. Effects of the EU-Indonesia FTA: short-term assessment

One of the most widely used CGE models to estimate ex-ante the likely impact of a trade agreement is the standard static GTAP model. The underlying GTAP 7 database covers basically the entire world and contains detailed macroeconomic information for each country, thus allowing capturing inter-sectoral and inter-country effects a trade agreement is likely to induce. Before simulating the new trade agreement between Indonesia and the EU, a baseline against which results are benchmarked needs to be generated. The baseline takes into account Indonesian and the EU's bilateral FTAs with third countries that have been implemented since 2004. The policy scenario assumes tariff only full liberalization, i.e. the elimination of all tariffs in trade in goods.

One of the most important conclusions of this analysis is that although trade agreements need time to fully deliver their economic impact, even in the short run such a trade agreement would increase both Indonesian and the EU overall welfare. Given the tariff-only liberalization assumptions and the short-term time span, the additional effect on the Indonesian GDP is relatively modest. **Nevertheless, an additional 0.1% (524 million euro, based on the estimated 2010 GDP of Indonesia) could be generated annually.** Given the much larger size of the EU economy and its diversified economic and trade structure, the overall positive impact on EU GDP growth will also be relatively small in percentage terms. Overall, Indonesian gains will originate primarily in more favourable terms of trade following the FTA.

The detailed CGE disaggregation into economic sectors in Indonesia also allows a breakdown of economic effects by sector. While several sectors will clearly benefit as a result of the FTA, a limited number of economic sectors will be subject to adjustment pressure in the short run. While the nature of complex and fairly aggregate CGE models does not allow a more detailed sub-sectoral analysis, this suggests that possible short-term adverse impact on certain small and medium sized enterprises would require accompanying support measures. Among the likely source of this negative impact is the limited availability of technology, lack of capacity and inadequate infrastructure in Indonesia. Therefore, there is a case for supporting domestic policies in Indonesia and enhanced cooperation with the EU, including a reorientation of EU technical assistance in order to mitigate these adjustment costs. In the longer term, as the analysis described in the next section suggests, the new investment opportunities likely to be created by a comprehensive trade agreement, will also alleviate these costs and create new economic opportunities for most sectors.

The overall conclusion is that the FTA is expected to create better welfare and give an additional boost to economic growth in both partners. However, in the short-run, it is important to ensure that adjustment costs are adequately addressed by other domestic policies and through bilateral cooperation in key areas.

II. Longer-term, dynamic assessment of a bilateral trade agreement

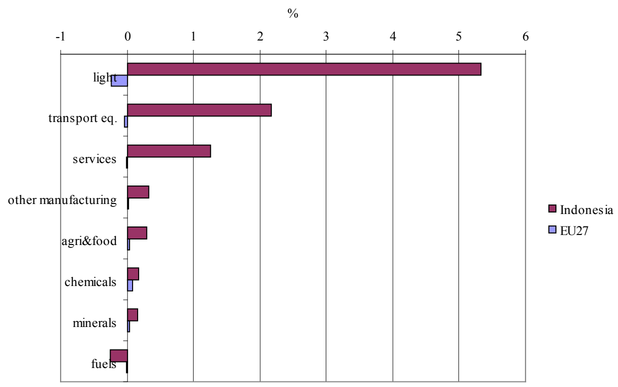
While some effects are clearly visible in the short-term, trade policy also leads to significant economic transformations in the longer-term. To complement this short-term, static analysis described above, CGE simulations were also performed using a dynamic GTAP model. The dynamic model gives the possibility of introducing international capital flows and the time dimension into the existing static framework. In other words, the distribution of the effects over time in this dynamic CGE model is obtained through the accumulation of capital and through capital flows among countries being influenced by changes in profitability rates.[10] This last feature seems to be particularly relevant for Indonesia, aiming at hosting more technologically-advanced foreign investment.

The underlying database on which the analysis is performed is, like in the static analysis, based on the same GTAP7 database, which is benchmarked to year 2004.[11] For the purpose of this exercise it was assumed that the future EU-Indonesia trade agreement enters into force in 2015. The time horizon of the simulations was set to 2030, after which all or the vast majority of the effects of an FTA implemented by 2015, should take place. Several results point out the importance of a longer-term assessment of the economic effects of a future EU-Indonesia trade agreement.

Instead of static 0.1% additional GDP growth for Indonesia, long-term dynamic gains are in the range of 1.3% of Indonesian GDP in the long run. **This translates roughly in the range of 6.8 billion of euro (based on estimated 2010 GDP of Indonesia estimate)**. Due to size and other economic asymmetries, the effect on the EU GDP remains in percentage terms much smaller.

In terms of sectoral effects, the output of Indonesian light industries is going to be 5% higher, than in a situation without the FTA (see figure 1). The production of transport equipment and parts as well as the provision of services are also going to increase by 2% and 1%, respectively. The only economic sector which shows a slight output decline of 0.3% is fuels. However, overall these sectoral effects suggest that the Indonesia economy ill become more diversified, relying more on manufactured rather than primary products and exports.

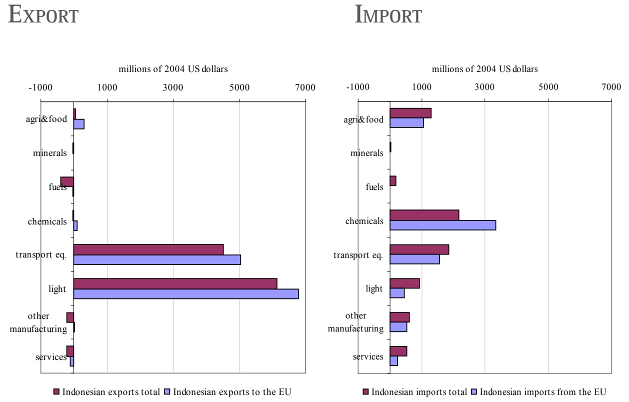
Figure 1: Effects on production in Indonesia and in the EU by sectors and countries, in %, cumulative changes in 2030 as compared to the baseline



10 The model gives a choice in terms of various policy parameters underlying the allocation of investment and savings. For the purpose of this analysis it was assumed that capital (both savings and equity) is relatively mobile among developed countries, while for the developing countries these are savings, which are relatively unrestricted, while the sources of founding for the local firms are more limited and skewed towards acquisition of capital domestically.

11 In order to bring the database closer to the current year, a number of adjustments had to be made on the original 2004 data. Thus, the baseline scenario includes a number of implemented EU's, Indonesian and ASEAN FTAs, phasing out the Multi-Fibre Agreement etc. The policy scenario is, for comparability purposes, the same as the one performed under the short-term analysis, i.e. tariff only EU-Indonesia FTA.

Figure 2: Effects on Indonesian trade values by sectors, in millions of 2004 US dollars, cumulative changes in 2030 as compared to the baselin



In terms of effects on trade volumes, Indonesian export of light industries and transport equipment is estimated to increase considerably. And as these sectors constitute together a large share of total Indonesian exports, when measured in constant prices, Indonesian exports of goods and services in 2030 is going to be higher by USD 9.8 billion (as compared to a situation without the FTA). Imports of (in particular) chemicals, transport equipment and agricultural products and processed food are also set to expand by around USD 7.7 billions. Therefore, the overall Indonesian trade balance in the long run will improve by around USD 2 billion.

III. Beyond a shallow FTA

Moreover, there are grounds to believe that if a deep and comprehensive trade agreement is going beyond simple tariff dismantling, is implemented, the economic gains are going to be even more substantial. A typical EU FTA contains many provisions going beyond tariff liberalization, such as approximation/mutual recognition of standards, enhancing competition, liberalisation of barriers to trade in services, opening up procurement markets etc. These provisions usually lower non-tariff barriers to trade and enhance trade creation leading to bigger overall welfare gains.

For instance, the dynamic results of the simulated FTA point out an increase by 2% in new FDI inflows into Indonesia in the short and medium-run (2016-2020) and by over 4% of new FDI inflows into Indonesia by 2030 (as compared to the situation in 2030 simulated without the FTA).

Possible additional effects, which can be brought about by the liberalisation of barriers to trade in services are perhaps the most interesting in this case. Recent study exploring consequences of the removal of restrictions on services by developing countries (CIE, 2010) pointed out that the effects of such an action on Indonesia would be in the range of 0.1% of its GDP. Most likely, such move will stimulate substantial additional FDI flows, in particular to the financial intermediation sector.

IV. Costs of doing nothing

One may think about other possible scenarios for the EU-Indonesia trade relations. In case no FTA is concluded while some bilateral agreements are taking place with other partners, trade diversion is most likely going to dominate any other effects with adverse consequences for Indonesia. On top of this, the GSP system undergoing changes is also going to impact upon existing trade flows. Stating how large welfare changes these might be is beyond the scope of this exercise. Nevertheless it is useful to remember that the changes simulated here show only one possible direction of events.

V. Trade and poverty reduction

Since the possible FTA raises concerns about its impact on poverty, we turn now to the topic of how trade influences poverty and what kind of effects can be expected in the case of the FTA between the EU and Indonesia. The dynamic GTAP simulations described above suggest an **overall rise in the Indonesian wages of 1.5% as a result of a trade agreement.** This is a strong indication that income levels in Indonesia, including for the poorer segments of the population will be positively affected. Returns to land (important for the rural population) will increase in the long run as well, but the change is going to be smaller. It is also important to emphasize that other supporting policies will certainly have a strong impact on poverty reduction, alongside the impact of trade policy.

Economic literature on the link of trade and poverty suggests that contrary to the general perception that trade may harm the poor, trade is in general poverty alleviating (see Winters et al. for a survey of applied studies). Whether trade liberalisation has a positive impact on poverty depends therefore on the development of markets for unskilled labour and often complementary domestic reforms are needed to enhance the ability of poorer households to exploit potentially beneficial changes (cf. Hertel and Reimer, 2005). Moreover, countries may need to strengthen social protection to mitigate adjustment effects of trade liberalisation (cf. Winters et al., 2004).

In the case of Indonesia ex-ante analysis has found trade liberalisation generally reduces poverty with more liberalisation entailing a stronger reduction in poverty. Robilliard and Robinson (2005), for example, find that full multilateral trade liberalisation would reduce the number of the poor by around 1.3 million people. Since the majority of the poor in Indonesia receive income from agriculture and transfers (Hertel et al., 2003), significant reductions in poverty will be driven by this strata. Henceforth for trade liberalisation to be poverty-reducing in Indonesia it should benefit these parts of society. Hartono et al. (2007) examines the poverty implications of the EU-Indonesia FTA as opposed to some other FTAs. They find that an Indonesia–EU FTA would benefit Indonesia relative to other FTAs (i.e. FTAs with India or Singapore) in terms of real GDP growth, increases in household income, and welfare. Moreover, an Indonesia – EU FTA is supposed to reduce poverty with increases in average household income disproportionately benefitting unskilled labour and rural areas.

Taking all the above into account, one should expect the full EU-Indonesia FTA, with all the tariffs eliminated across-the-board, to have the effect of alleviating poverty. Nevertheless, the inclusion of additional provisions reducing NTBs seems desirable as well as other effectively targeted support measures.

ANNEX 3

INDONESIA – EU DEEPENING FRIENDSHIP

EU and Indonesia: long history, strong present and great future...

Deep economic integration over a very wide spectrum of policies and legal obligations, and with the political acceptance of centralized common institutions, has been the foundation for European growth and stability for more than 50 years. Today, EU citizens from 27 Member States can travel, work and live without any constraints inside a market of 500 million people. Business enjoys genuine free movement of goods, services, capital; (to some degree) workers and codified technology and can establish itself anywhere in the Union. The world benefits from European integration. Indonesia's government has a single counterpart for trade, not 27 individual states. Indonesian exporters to Europe meet one EU standard, not 27 different standards. Indonesian visitors to Europe's "Schengen-area" need one visa and can travel throughout the "Euro-zone" using one currency.

Indonesia has developed rapidly into a strong, stable democracy as well as an emerging global economic power. It is a G20 member showing leadership on issues of global importance such as climate change, financial stability and peace. In Indonesia, the EU has found an important strategic partner that shares its values of development, diversity and democracy. Today it is a friendship that includes co-operation on education, climate change, emergency response, justice, trade and investment - all based on the core values EU and Indonesia share.

Bilateral EU and Indonesia Alliance – Equal Partners and Mutual Benefit

The existing EU and Indonesia alliance is extensive and important for both where a thriving economic partnership is paving the way for closer political relationship to the benefit of future generations of Europeans and Indonesians.

In the **political cooperation area**, cooperation has been expanding for two decades. This has ranged from from election observation during the late 1990's, through human rights and inter-faith dialogues and even to support on conflict resolution. The government of Indonesia requested support from the EU to assist in its conflict resolution strategy in Aceh. The EU provided the Aceh Monitoring Mission and facilitation of negotiations by President Ahtisaari.

In the area of **diversity**, people to people contact is growing every year. Students, businessmen and tourists are boosting these people to people flows towards the million per year level. In education, the EU provides about 1,000 grants to Indonesian students to study at European universities per year.

Thanks to the opportunities opened up by the **Partnership and Cooperation Agreement**, the EU and Indonesia have started cooperating in new areas such as on security issues like counter-terrorism, such as on research and technology, such as on human rights dialogue.

In the area of **development through trade and investment**, the EU and Indonesia mutually benefit from huge-scale commercial ties between the two economies:

1. The EU is Indonesia's second largest investor. Over 700 EU companies are operating in Indonesia, providing more than 500,000 jobs. This number will increase as Indonesia's economy continues on its path to rapid growth.

2. The EU is Indonesia's second largest export market. Indonesia's exports to EU currently stand at EUR 14 billion but are set to expand as Indonesian companies move up the value-chain.

In the **development through financial cooperation** area, the EU and its Member States provide over EUR 700 million annually to Indonesia across sectors vital for future prosperity such as education, health, trade and climate change:

1. The EU and its Member States are supporting Indonesia's climate change initiatives with US$1.5 billion, including projects encouraging forestry conservation and sustainable management. EU specifically supports Indonesia's REDD+ strategy, MRV system, and resilience to climate change impacts. The EU assists Indonesia's efforts to combat illegal logging and ensure credible legal verification through trade policies and co-operation with government agencies, the private sector and civil society and the EU promotes environment friendly consumption and production through projects in various economic sectors such as the batik industry

2. The EU and its member states have been leaders in supporting Indonesia after natural disasters. The EU was the largest donor to the Multi Donor Trust Fund for Aceh and Nias to support reconstruction efforts after the 2004 Indian Ocean tsunami. The EU has also provided significant financial support for humanitarian and long-term reconstruction assistance following the earthquake and tsunami in the Mentawai Islands, the Merapi volcanic eruption and in the aftermath of the Yogyakarta and Central Java earthquakes.

3. Since 2010, EU has provided funds directly to the Indonesian state budget to support Indonesia's own policies and priorities within education. EU co-funds with Australia a $1 billion programme to increase knowledge, competitiveness and towards equal opportunities in the education sector. The EU is supporting implementation of minimum standards to improve the quality of basic education in Indonesia.

An Emerging Global Alliance: Indonesia and EU together making a difference

Given that the EU and Indonesia share the same views and approaches to common global problems, EU and Indonesia are natural allies in the global domain and cooperation through bodies such as the UN or G20 is expanding rapidly.

1. In WTO, EU and Indonesia are working for fairer global trade and are engaged in negotiations to secure a fairer result in the WTO's Doha Development Round.

2. In the G20, EU and Indonesia worked to achieve a positive agreement on tackling the 2008 global financial crisis.

3. In climate change areas, EU and Indonesia have pledged to reduce greenhouse gas emissions: the EU by up to 30% by 2020 and Indonesia by 26% by 2020.

Major source for investments in Indonesia ... but so much more potential

The greatest strength of the commercial alliance between the EU and Indonesia lies in the greater tendency for EU **companies to invest in Indonesia**, rather than simply to trade with it. This assures Indonesia that its favourable trade balance with EU will continue (€7 billion in surplus in 2010) but also that the commercial alliance with the EU will produce far greater local value added for Indonesia:

1. Employment – existing EU investments generate over 500,000 jobs in Indonesia. However, the multiuplier rate is much larger: one EU investor recently commissioned an independent study to see the additional indirect employment benefits of its investment in the Indonesia economy – in addition to having some 10,000 direct employees, the study identified that 150,000 Indonesian were employed in wholesale and retail sectors associated with that company's products.

2. Technology transfer. By expanding investment, European companies bring the technologies to the Indonesian market – adding further intellectual and capacity value locally. For example, a company in Bandung formed a partnership with Airbus and now produces locally in Indonesia the struts that bind the wings of the Airbus A380 to the fuselage.

3. Mutual prosperity: European investors are the second largest in Indonesia encompassing oil and gas; mining; services; food products; metal and machinery; chemicals and manufacturing. EU Member States companies recognise the advantages of Indonesia for investment, which include: economic growth (soon predicted to reach 7%); a strong middle class; a stable political environment ; that Indonesia is the largest economy in a dynamic ASEAN and Asian region; its infrastructure opportunities; production networks and network of FTAs; also the availability of natural resources and its large labour force - and its increasingly competitive advantages that help position Indonesia positively in relation to China.

Conclusion – a Friendship that Could Grow Even Further

EU and Indonesia relations are already strong and growing healthily across the board. Trade and investment ties have always underpinned this alliance, thanks largely to the fact that there is great complementarity between the two economies. The EU and Indonesia do not make the same products and do not compete with each other. EU companies tend to invest in Indonesia rather than sell to Indonesia. These ties continue to bring massive advantage to Indonesia – a healthy trade surplus and investments by EU companies in Indonesia creating jobs and transferring technology. These ties also bring advantage to the EU – with great products coming to the EU, while EU investing companies continue to build their activities. Trade and investment will continue to underpin this alliance in the future.