IA-CEPA
A new chapter in Australian-Indonesian trade

By SHIPPING AUSTRALIA

Underweight, underperforming and due for an overhaul. That's one way to describe the Australia-Indonesia economic relationship.

At least, until now.

Entering into force on Sunday 5 July 2020 was the Indonesia Australia Comprehensive Partnership Agreement. Also known as IA-CEPA (typically pronounced 'Eye-Ay-Seppa'), it is hoped that the new free trade agreement will revolutionise the Indonesia-Australia partnership. Especially as Indonesia had (prior to COVID at least) one of the fastest-growing economies in the world.

Some two-way trade – but there could be so much more

A new economic chapter between Indonesia and Australia does need starting.

At the time of writing, Australia ranks a mere 13th on Indonesia's list of merchandise trade principal export destinations (1.6% of all exports) and 8th on its list of import sources (3.1% of all imports). On the other side of the ledger, Indonesia is 11th on the list of merchandise trade export destinations from Australia (2.0% of all exports) and 15th on the list of import sources (1.6% of all merchandise trade imports).

The total two-way trade is worth about A$11.81 billion a year (A$6.8 billion of exports to Indonesia and just under A$5.0 billion of imports from Indonesia).

So, while there is trade between the two nations, given the proximity, potential complementarity and vast economies of the two nations, it could be argued that there is potential for so much more.

Indonesia's economy

The potential freight opportunity presented by Indonesia's economy is vast. As explained by Dr Martin Stopford in his seminal work, "Maritime Economics", there is a simple and well-known relationship between the size of an economy and its seaborne trade. The bigger the economy, the greater the potential for seaborne trade.

The archipelagic nation's economy has a gross domestic product in excess of US$1.1 trillion (GDP (US$ bn) nominal prices), according to the Australian Department of Foreign Affairs and Trade. Unfortunately, the advent of COVID-19 has caused a slump in the Indonesian economy. In more normal times, the economy grew on average by about 4.6% over the last five years. That five-year average hides some quite phenomenal figures with 8.5% growth or more in the years of 2016, 2017 and 2019. The down, and the flat, years of 2015 and 2018 appear to have been caused by global macro-economic factors.

Indonesia's GDP per capita on a parity of purchasing power basis (GDP PPP per capita) is very compelling. For the last five years GDP PPP per capita has grown between 4.5% to 6.6% with an average growth of 5.8%. GDP PPP per capita stood at about US$10,700 in 2014 and by the end of 2019 it stood at just under US$14,000, according to DFAT data. By way of comparison, given that World Bank data puts Australian GDP PPP per capita at about US$53,000, it's clear that there is plenty of room for growth in Indonesia's economy.

Indonesia's population

While an increase in terms of a few thousand dollars per head may not sound much, the size and composition of the Indonesian population should be remembered. There are over 267 million Indonesians according to the World Bank. Poverty has been slashed by more than half between 1999 to 2019 to about 9.4% of the population. Over the same timeframe, Indonesia's middle class (defined by the World Bank as "economically secure") has grown from about 7% of the population to about 20% of the population. That's about 52 million Indonesians, which is more than twice the entire population of Australia. A further 45% of the Indonesian population – 115 million people – are free of poverty and are aspiring to achieve economic security.

"Demand from the middle class can drive growth. They are the source of almost half of the total household expenditure of Indonesia," said Rolande Pryce, acting World Bank Country Director for Indonesia.

About IA-CEPA

IA-CEPA covers both goods and services. In relation to goods, it covers tariffs and it also tackles such issues as rules of origin, customs procedures and trade facilitation, technical barriers to trade, sanitation and phytosanitary measures. In relation to trade in services it includes employment, finance, telecommunications, professional services, investment, electronic commerce, power policy, competitiveness, and economic cooperation, together with institutional arrangements and frameworks.

Benefits for Indonesia

For Indonesia, IA-CEPA will eliminate virtually all tariffs and Australian import duties so that nearly all Indonesian products will be tariff or duty free. Indonesia's Ministry of Trade hopes that a variety Indonesian exports will increase in volume. These include automotive, wood products and their derivatives (such as paper and cardboard), furniture, textiles and textile products, tools, communication and electronic equipment. Indonesia is also hoping for a boost in exports of aluminium, processed meat and fish, tobacco, cocoa, various manufactured goods, house lighting, plastics and plastic goods, fish and shrimp.

Benefits for Australian exporters

On the Australian side, nearly all Australian exports to Indonesia will similarly be tariff- and duty-free under IA-CEPA. Canberra is hoping for a boost for its farm exports such as an increase in volumes of grains. According to Senator Birmingham, Australian growers will be able to export 500,000 tonnes of feed grains, including wheat and barley tariff-free into Indonesia under IA-CEPA. Other Australian exports that may benefit include live cattle, meat, dairy products, horticultural products (as distinct from grain) such as potatoes and carrots. Australian manufacturers may also benefit as, according to the Australian Embassy in Indonesia, "the vast majority of Australian goods exports to Indonesia are used in Indonesia's manufacturing sector". Indonesia will also guarantee the automatic import of import permits for a variety of products.

Increased demand for imports and exports of these kinds of goods, along with a growing middle class, a rise in disposable income, and a mutually beneficial free trade agreement would tend to point towards long-term growth in the demand for the carriage of containerised freight to and from Australia and Indonesia.

As may be expected, a wide range of advocacy and trade groups have enthusiastically welcomed the entry into force of IA-CEPA. But there are signs that the hoped-for take off might not, well, take off.

A mutual lack of interest?

An increase in trade would presume a knowledge of, and interest in, the trading partner. There is apparently a low level of Australian interest in Indonesia and a low level of Indonesian interest in Australia.

The Australia-Indonesia Centre carried out an attitude study in 2016 and surveyed over 2,000 people. The Australia-Indonesia Perceptions report showed that 47% of Australians have little-to-no understanding of Indonesia in terms of its people and culture. A further 34% have a "moderate" understanding. About 26% of Indonesians had little-to-no understanding of Australia and 31% had a "moderate" understanding.

Kyle Springer of the think-tank, "Perth USAsia Centre", at University of Western Australia pointed out back in 2017 that the difficulties of doing business in Indonesia did not explain a lack of Australian interest in doing business in Indonesia. The difficulties and challenges of doing business in Indonesia were found to be about the same as doing business in China according to the World Bank's Ease of Doing Business Index (64.28 index points for China in 2017 and 61.52 for Indonesia). But the amount of Australian business being done in China far outweighed the business being done in Indonesia.

But why?

One word explains why. And that word is "narrative".

"What Australia does have is a narrative of China's economic rise and how it [Australia] has benefited directly from it… Rather than perception of risk and uncertainty, [a] working group explained that Australia simply has yet to see Indonesia as an opportunity. There is yet [to be] a narrative of Indonesia's rise and what it could mean for Australian businesses," Springer wrote.

Springer later argued that: "stronger ties between boardrooms are needed… exchanges of influential business people will pave the way to successful partnerships. In this context, it's hard to overstate the importance of IA-CEPA".

Hyping it up

Some commentators have argued that the IA-CEPA hype of a boost in trade is just that: hype.

Colin Brown, Adjunct Professor in the Griffith Asia Institute at Griffith University, noted a variety of problems in an article for the Australian Institute of International Affairs. He observed that Australian exporters will still have to deal with unreliable infrastructure, bureaucracy, and corruption. Furthermore, pre-existing trade deals before IA-CEPA mean that trade between Indonesia and Australia already enjoys low, or zero tariffs. He further argues that many Indonesian manufacturers do not want to export at all and, of those that do, Australia may simply be too small a market. They would likely be looking at China or the United States instead.

"We should not expect a major turn-around in the trade and investment relationship between Australia and Indonesia, at least not in the short or medium term," he wrote.

Indonesia: a growing economy

Year	GDP (US$b) (Current Prices)	% Change	Year	GDP per Capita PPP (Int'l $)	% Change
2014	891.1		**2014**	10,690	
2015	860.7	-3.4	**2015**	11,176	4.5
2016	932.1	8.3	**2016**	11,727	4.9
2017	1,015.30	8.9	**2017**	12,416	5.9
2018	1,022.50	0.7	**2018**	13,234	6.6
2019	1,111.70	8.7	**2019**	13,998	5.8
	Average	**4.6**		**Average**	**5.5**