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FOCUSING ON LOGISTICS: AN ENABLING APPROACH TO TRADE?

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OUTLINE

- “Enabling Trade: Valuing Growth Opportunities” – WEF-WB Report 2013
- Barriers to Trade: Case Studies of Logistics Costs
- An Enabling Trade Approach for Indonesia?



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WEF-WB Report 2013 “ENABLING TRADE: VALUING GROWTH OPPORTUNITIES”



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New context for Trade: Intermediate Goods and GVCs lead International Trade Flows

- **“Made in the World”** (WTO): Not one country but many countries involved in producing a single good
- New pattern of Trade → Global Value Chain (GVC)
- As a consequence, transport services have increased...
- So...

Logistics Costs (including transport) are more and more important and constitute a key factor in competitiveness



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Exports (of domestic value-added and gross) between major regions, 1995

Figure 1: Exports (of domestic value-added and gross) between major regions, 1995



Source: www.oecd.org/trade/valueadded

- Domestic value added shares 90% or more
- Domestic value added shares between 80-90%
- Domestic value added shares 80% or less



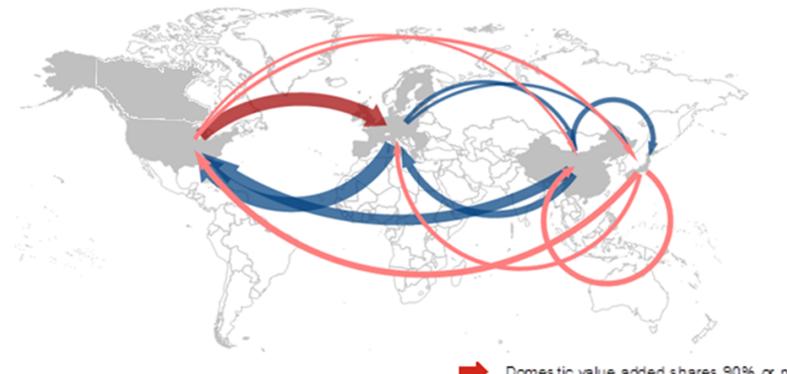
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Exports (of domestic value-added and gross) between major regions, 2005

Figure 2: Exports (of domestic value-added and gross) between major regions, 2005



Source: www.oecd.org/trade/valueadded

- Domestic value added shares 90% or more
- Domestic value added shares between 80-90%
- Domestic value added shares 80% or less



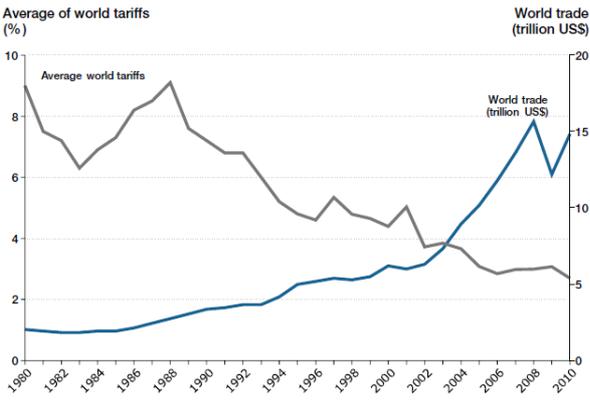

Logistics Barriers are far more significant impediments to Trade than are Tariffs today!

↓

FOCUS SHOULD BE CHANGED FROM TARIFF REDUCTION TO “ENABLING TRADE” APPROACH




Figure 1: Tariff removal has been successful in increasing trade



Source: Tariffs adapted from Coatsworth and Williamson, 2002 and Mitchel, 1992; referenced in Nenci, 2009; World Bank, World Trade from World Trade Organization report, 2012.

The last 30 years have seen a Large Reduction in Tariffs



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**What are the main impediments to Trade today?
Policy makers focus : SUPPLY CHAIN BARRIERS**

- Today, the biggest deterrents to trade are the lack of infrastructure, border policies, efficient services and institutions that create obstacles to the movement of goods: **SERVICES KEY AMONG THESE.**
- 4 main issue areas affecting supply chains **before and after the border** :
 - **Market Access**
 - **Border Administration**
 - **Telecommunications and Transportation Infrastructure (SERVICES)**
 - **Business Environment**



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Supply Chain Barriers to Trade

Figure 2: Supply chain barriers to trade

Definition: The lack of infrastructure, institutions, policies and services facilitating the free flow of goods over borders

Market access	Border administration	Telecom and transport infrastructure	Business environment
1. Domestic and foreign market access - Quotas - Import fees – not tariffs (e.g. tax schemes) - Local content requirements - Rules of origin - Technical, sanitary and phytosanitary measures or other requirements - Import/export licenses	2. Efficiency of customs administration 3. Efficiency of import-export procedures (e.g. coordination between border agencies; administration burden of complying with standards)	5. Availability and quality of transport infrastructure 6. Availability and quality of transport services 7. Availability and use of information and communication technologies (e.g. tracking, electronic-tolls, communication)	8. Regulatory environment - Investment policy - Hiring foreign workers - Other regulatory environment issues (including trade finance) 9. Physical security

Note: The Global Enabling Trade Report identifies 9 pillars, this is an extended list including several sub-pillars as tested in a separate survey for this study.



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Consequences of Supply Chain Barriers

Supply chain barriers weigh on a business engaging in trade in 4 direct ways:

- Adds to costs - in terms of higher operating costs and increased capital expenditures
- Worsens the delays faced by business in making shipments less predictable or longer
- Reduces volume of trade activity
- Increases risk

» From World Economic Forum, Global Enabling Trade Report, 2012



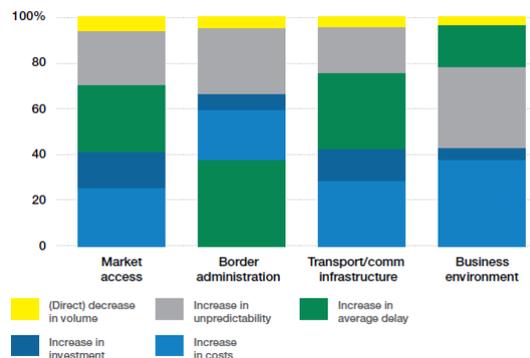
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Consequences of each kind of Barrier to Trade

Figure 4: Each trade barrier can disrupt a company's supply chain and lead to higher costs

% of consequences for each issue area



Note: Includes manufacturing, retail and logistics, N=108
Source: World Economic Forum survey.



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How do firms deal with Barriers to Trade?

- A company's experience will vary by the specific barrier it encounters and the actions, if any, it takes in response
 - Example: A company that must contend with frequent truck breakdowns resulting from badly maintained roads (poor transportation infrastructure) might:
 - accept a higher average delay in shipments; or
 - purchase additional trucks, thereby increasing capital expenditures
- **BOTH RESPONSES INCREASE COSTS**



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How do firms deal with Barriers to Trade?



- For instance, transportation delays will be more harmful to a company that sells fresh fish than to one that sells canned tuna.
- A company's response will necessarily increase costs and be **reflected in input higher prices** to other producers using the product and passed on to consumers, or **directly in higher final prices**.



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NEW WORLD BANK- WORLD ECONOMIC FORUM JOINT STUDY on “ENABLING TRADE” 2013

- **Focuses on Logistics and Calculates Costs of Supply Chain Barriers to operations of actual firms based on 18 Case Studies**
 - Two key components of supply chain barriers considered:
 - **1. BORDER ADMINISTRATION**
 - **2. TRANSPORT AND COMMUNICATIONS INFRASTRUCTURE (SERVICES)**
- WEF-WB Report “Enabling Trade: Valuing Growth Opportunities” 2013
http://www3.weforum.org/docs/WEF_SCT_EnablingTrade_Report_2013.pdf



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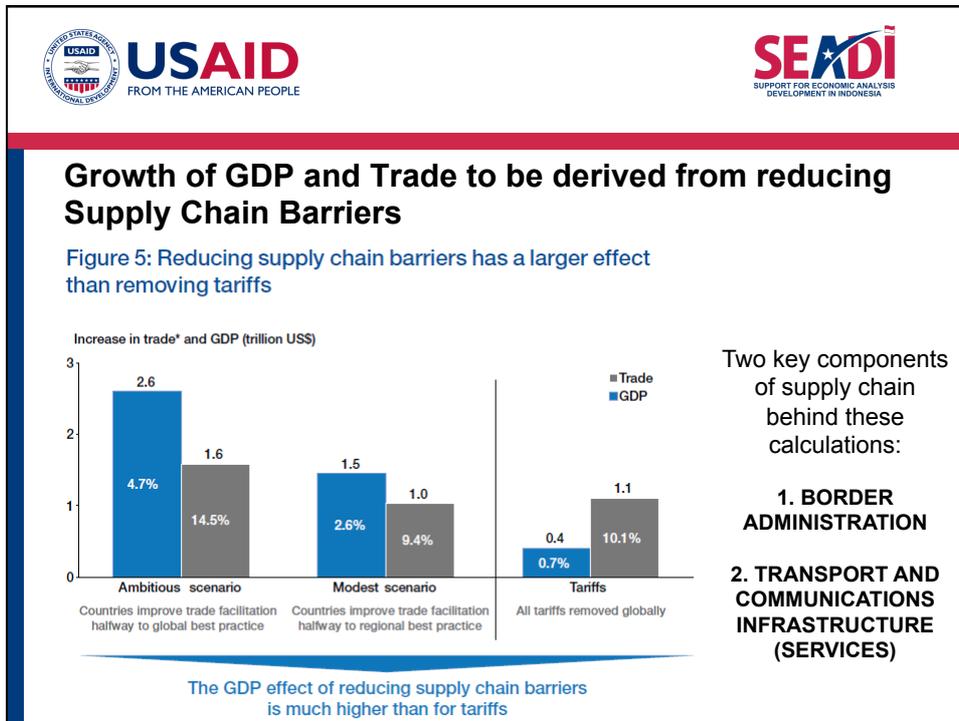
Report shows that gains from reducing Logistics Barriers to Trade would be HUGE

Reducing supply chain barriers could increase world GDP five times more than removing all tariffs.

- Reducing supply chain barriers to trade halfway to global best practice could potentially increase world GDP by nearly 5% and trade by 15%.

» WEF-WB Enabling Trade Report 2013

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WHY IS LOWERING SUPPLY CHAIN BARRIERS SO EFFECTIVE?

- Because it eliminates resource waste, whereas abolishing tariffs mainly reallocates resources.
- Moreover, the gains from reducing barriers are more evenly distributed among nations than the gains from eliminating tariffs, reducing inequality worldwide.

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Source: "Enabling Trade: Valuing Growth Opportunities". WEF Report, 2013



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Distribution of the Gains to Trade and GDP from REDUCTION OF LOGISTICS BARRIERS

- Gains in GDP associated with trade facilitation would take place in **all regions**, though they would be **concentrated in those with the greatest improvements**.
- These regions would include sub-Saharan Africa, South Asia, parts of Central and West Asia, as well as other developing regions.

Economic gains from barrier reductions are more evenly distributed across countries than the gains associated with tariff elimination



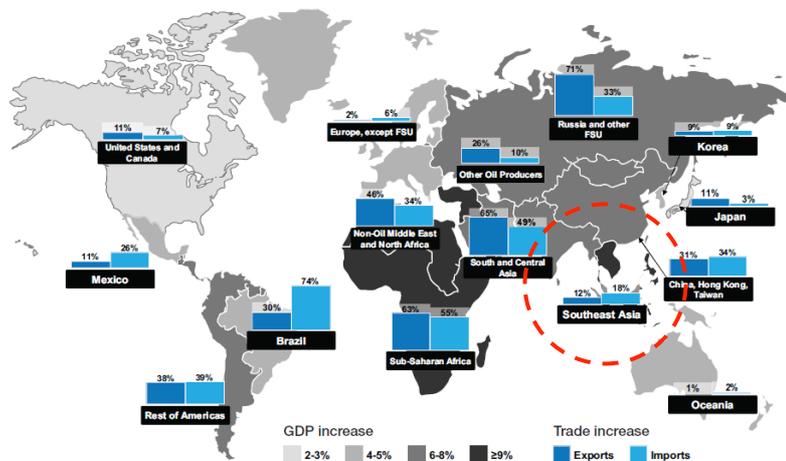
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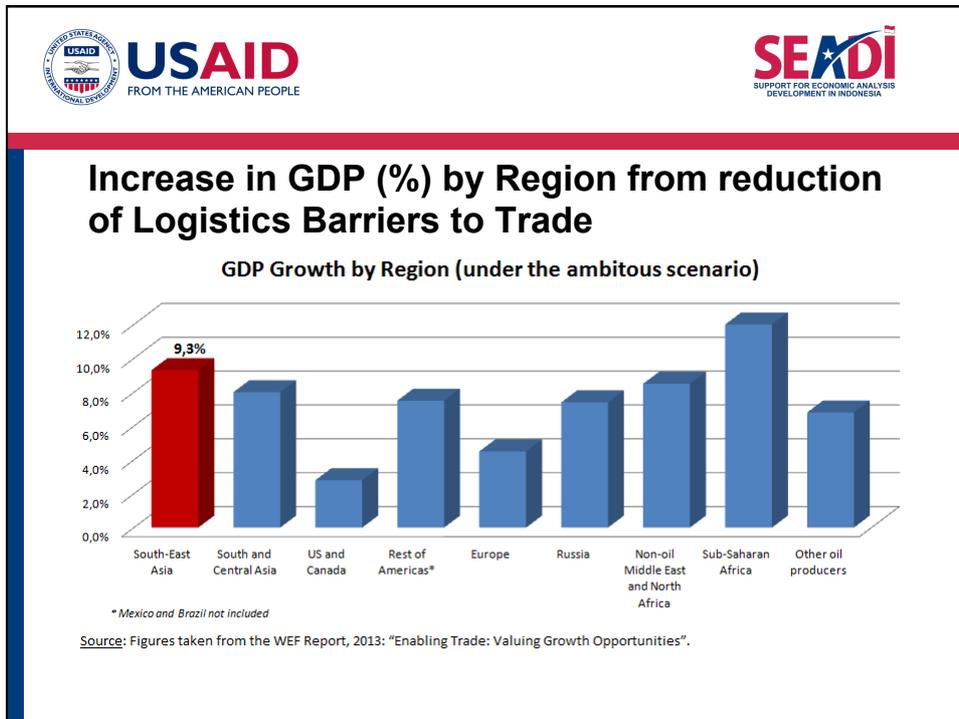


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Implications by Region (under the ambitious scenario)

Figure 6: Impact per region varies under the ambitious scenario





Who are the main beneficiaries from reduction in LOGISTICS COSTS TO TRADE?

- Reducing supply chain barriers lowers costs and hence lowers prices, both **for consumers and for firms that use these inputs.**
 - Consumers gain access to a wider variety of goods.
 - Workers benefit also – should stimulate employment growth.
- In the long run, this promotes a **shift in resources to more productive industries and firms, thereby increasing productivity and wages.**

Reducing supply chain barriers also makes locations more attractive for off-shoring investment.

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Source: "Enabling Trade: Valuing Growth Opportunities". WEF Report, 2013



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Logistics Barriers to Trade

CASE STUDIES



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1. Rubber Products from South-East Asia

- South-East Asia accounts for 70% of the world's production of rubber, which is the raw material used in countless final products, including surgical gloves and many other healthcare applications
- Monopoly position → producers in the region have power to impose high prices that squeeze distributors' margins
- Suppliers of medical disposables and devices have little room to bargain and are forced to endure supply chain bottlenecks that result in high **inventory costs and tie up capital**



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1. Rubber Products from South-East Asia

Why is are supply chains disrupted?

- Substandard infrastructure (services)
- Poor quality control
- Long lead times make the supply chain unreliable
- Corruption
 - A certain European-based distribution company hardly ever sources from some countries in SE Asia, due to the corruption it has encountered. It believes these business environment factors have prohibited the development of strong infrastructure and technological capabilities.



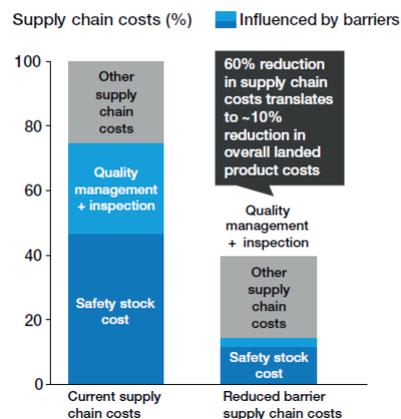
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1. Rubber Products from South-East Asia

Figure 16: Lowering supply chain barriers would reduce supply chain costs by some 60%



Eliminating supply chain barriers could:

- **reduce inventory lead times by as much as 90 days**
- **lower supply chain costs by some 60%**
 - **Note:** Gray box shows infrastructure/transport costs




2. EBay and the importance of SMEs in services

SMEs → Important in domestic economies as a source of jobs and growth BUT do little exporting

Why?

- SMEs cannot afford the fixed costs associated with global distribution networks (along with many other factors)

However...

- Internet helps SMEs participate in global business
- Internet-based SMEs are able to serve niche markets independent of their location




2. EBay and the importance of SMEs in services

- Of the firms doing business on eBay – many with fewer than five employees – 97% of those with more than US \$ 10,000 in annual sales sell their goods internationally.
- Although the Internet facilitates cross-border trade, supply chain barriers still interfere:
 - **Logistics costs**
 - **Express delivery costs**

If merchants decide to sell internationally, they will typically limit their sales to the countries whose regulations are easiest to navigate and whose shipping services are most reliable. Or they may transfer the risk and complexity to the buyer.



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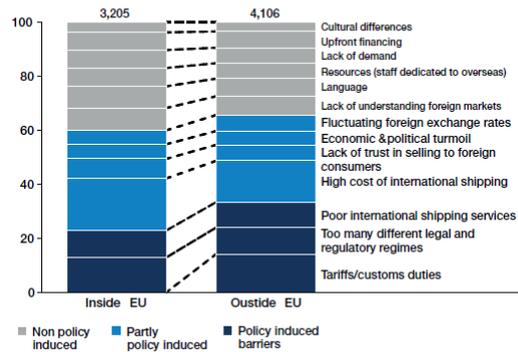


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Two-thirds of the Supply Chain Barriers are the result of Policies (20% of these in Services area)

Figure 20: A significant part of factors limiting trade mentioned by merchants are policy induced

Barriers acknowledged by German sellers
Responses indicating that the barrier is significant (%)



Source: eBay, Bain analysis.



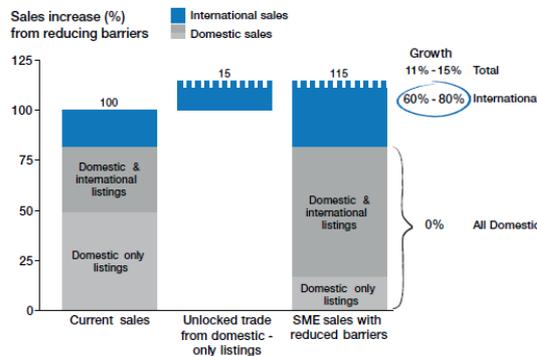
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2. eBay : lowering logistics barriers could increase international sales by 60% to 80% !

Figure 21: Based on pilots, there is an estimated 60% to 80% increase in cross-border sales by reducing barriers



SMEs could increase e-commerce cross-border trade by **60%-80%**, which is equivalent to a **US\$ 4.8 to US\$ 6.4 billion gain in trade**

If this behavior held for the entire global e-commerce market, international trade from the Internet might unlock **~US\$ 95 billion**



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3. IATA - Air Transport Services

Air Cargo Transport

- Less than 2% of total commercial transport by volume; but
- Accounts for approximately 35% of total value

The air cargo industry still relies heavily **on slow and inefficient paper-based shipping processes.**

2005 →

IATA in partnership with other major associations launched an industry-wide project to adopt lower-cost, more reliable electronic documentation



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3. IATA - Air Transport Services

Paperwork

- Average shipment typically needs **more than 30 documents**
 - customs forms; transportation docs, like airway bills and flight manifests, and commercial documents such as invoices, packing lists and certificates of origin
- These forms pass through the hands of up to **seven parties**
 - shippers, freight forwarders, ground-handling agents, airlines, customs brokers, customs agents and other government authorities
- Physical Documents **must be stored**
 - Retrieving an archived invoice or air waybill in a storage facility can take as long as **40 minutes**.



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3. IATA - Air Transport Services

Potential Gains from the Streamlining Program

- Using digital technology to pre-clear shipments before they arrive at the airport, for example, could prevent between 70% and 80% of paperwork-related delivery delays at destination.
- E-freight could yield annual savings for shippers and the air transport industry a total of nearly US \$ 12 billion.



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3. IATA - Air Transport Services

Is the Electronic Documentation Program working?

- To date, the e-freight initiative has been prevented from being universally adopted by:
 - Government regulations
 - Barriers in information and communications technology
 - Failure to achieve a critical mass of users to achieve network-effect benefits



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4. Express Delivery Services

Why do Express Delivery Services often struggle to operate in some markets?

- Customs clearance delays
- Lack of standardized procedures
- Poor infrastructure in less-developed regions

Implications for Consumers and Producers?

- Raises costs
- Lowers standards of service
- Frustrates efforts to improve supply chain efficiency and reliability

How countries choose to address these factors will ultimately influence their competitiveness & ability to participate in supply chains



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5. Express Delivery Services

Some delays can be easily addressed by Policies

- **Use of risk-analysis tools to guide which shipments are subject to border inspection could significantly speed up clearances.**
- **US:** officials target only potentially high-risk parcels for inspection, 92% of Express Delivery Services Co. shipments are cleared prior to shipment arrival at the border, and not all of the remaining 8% of shipments are physically inspected.
- **Netherlands:** officials rely on an analysis of electronic information to determine which shipments will be subjected to physical inspection, reducing the need for examination to just 2% to 3% of parcels.
- **Mexico:** authorities physically inspect 10% of all shipments and sometimes carry out a secondary inspection by independent contractors to guard against customs errors or wrongdoing. (Previously inspection carried out for 100% of shipments)



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5. Express Delivery Services

Some delays can be easily addressed by Policies

- **Limited number of hours that various countries' customs offices are open**
 - At major hubs in advanced markets like the US and Europe, customs is open round the clock, enabling express services companies to count on minimal downtime.
 - This is not the case in China, India and across much of Latin America, where Express Delivery Services Co. must sequence arrival of packages to coincide with customs opening hours.



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5. Express Delivery Services Co.

Some delays can be easily addressed by Policies

- **Lack of standardization and coordination in clearance process across countries and blocs**
- Adopt WCO's Kyoto Convention guidelines:**
- To create simplified custom procedures that can be carried out in a predictable, consistent and transparent environment.
 - Use of information technology and risk
 - "Single Window" electronic procedures, whereby documents are submitted once and are easily transferred across agencies and borders.

Just 81 of WCO's 178 member states have signed on to these common procedures!



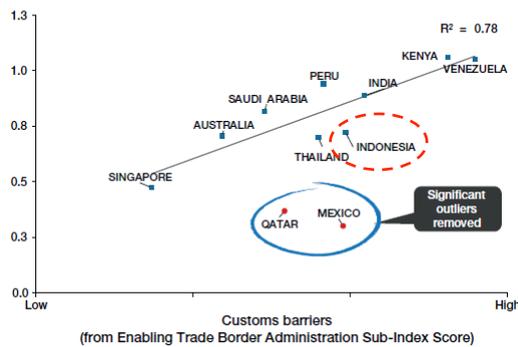
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5. Express Delivery Services Co.

Figure 35: Handling costs for express services are highly correlated with customs barriers

Unit handling cost in different destination countries (US\$/pound)



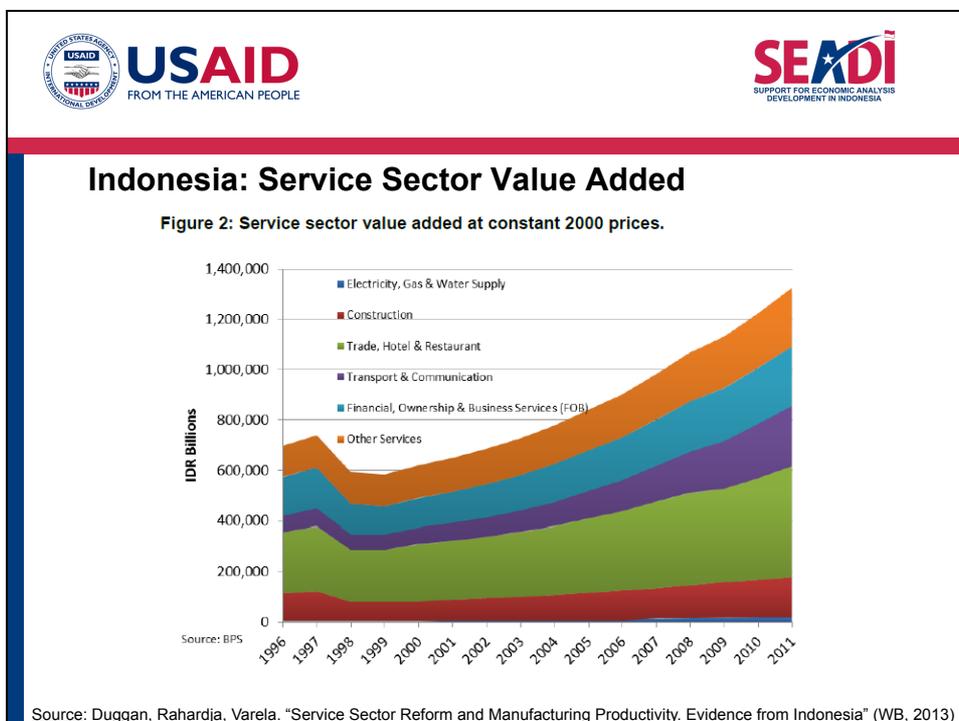
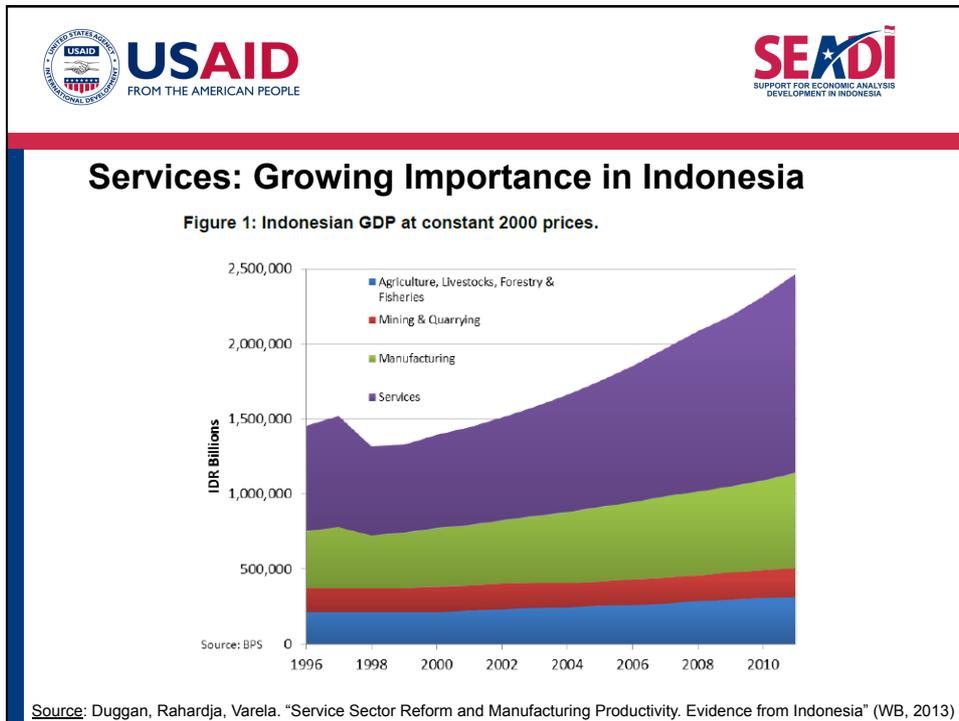
- Waiting time effects represent nearly 25% of the shipping costs companies pay per package.
- Among markets evaluated, Singapore is the top performer



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Enabling Trade Approach **INDONESIA & LOGISTICS**





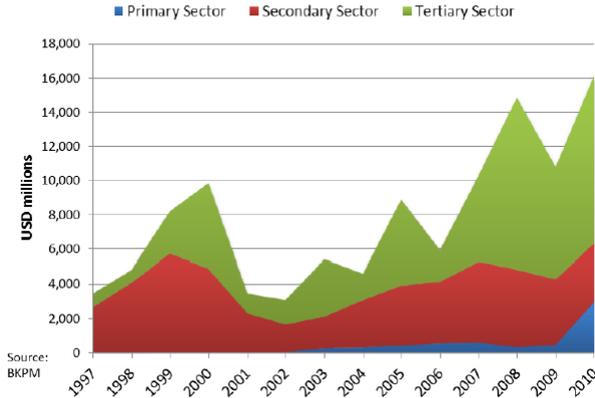
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FDI in Indonesia: Service Sector growing fastest

Figure 6: Inward FDI by sector.



Source: Duggan, Rahardja, Varela. "Service Sector Reform and Manufacturing Productivity. Evidence from Indonesia" (WB, 2013)



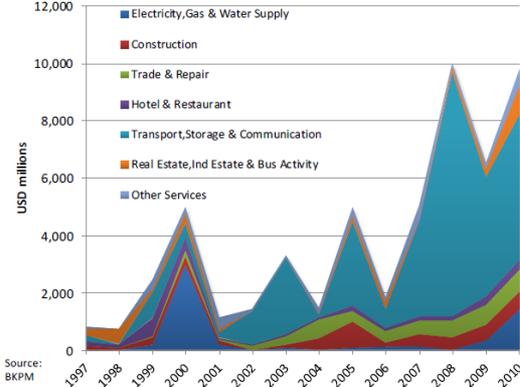
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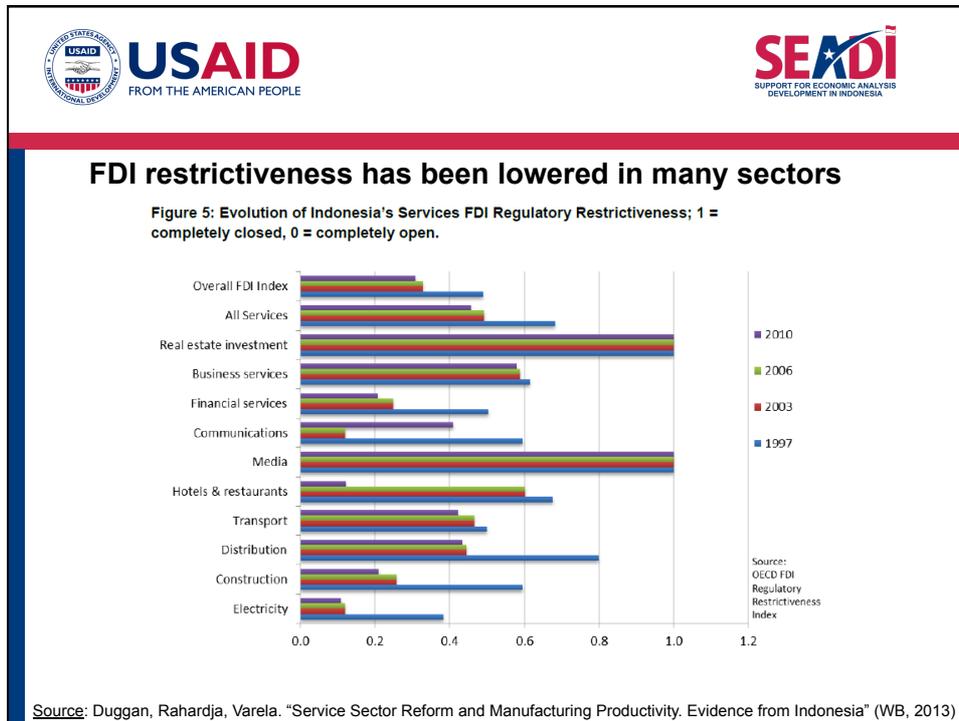
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FDI received by Service Sector Breakdown- Indonesia

Figure 7: Inward FDI by service sub-sector.



Source: Duggan, Rahardja, Varela. "Service Sector Reform and Manufacturing Productivity. Evidence from Indonesia" (WB, 2013)



Link between FDI policy restrictiveness and economic performance

- Relaxation in service sector FDI policies accounted for 8% of the observed increase in manufacturers' total factor productivity in Indonesia over 1997-2009!
- If services related to freight and logistics services remain sheltered from foreign investment and competition in Indonesia, costs will remain high and service quality poor (transport and distribution – still high FDI restrictiveness)



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BUT – THERE IS MUCH MORE TO BE DONE TO IMPROVE PRODUCTIVITY AND LOGISTICS

- **Logistics costs in Indonesia are estimated to be nearly double those in South Korea, and nearly three times those in Japan**
- Total factor productivity gains accrue disproportionately to those firms that are relatively more productive; those gains are directly linked to the relaxation of restrictions in the transport and electricity, gas, and water sectors.
 - (WB Study for Indonesia, 2013)

Source: Duggan, Rahardja, Varela. "Service Sector Reform and Manufacturing Productivity. Evidence from Indonesia" (WB, 2013)



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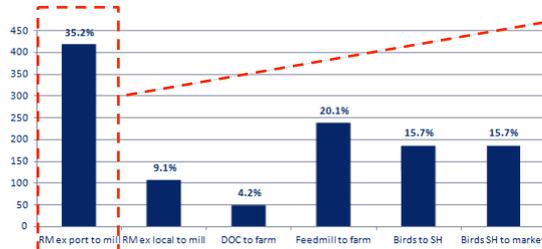


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Exp: Transport Costs –Chickens Indonesia

Transport Costs → 4.7% of the retail price for broilers

Figure 3-10
All Indonesia Transport Costs for Broilers to Consumer (Rp/kg chicken) and Percentage Breakdown of Transport Costs by Activity



The highest cost is for imported raw materials from port to mill

Source: "Indonesia's Poultry Value Chain. Costs, Margins, Prices, and Other Issues". Nathan Associates Inc and USAID. (2013)



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Why is this transport cost elevated?

- The high import component of Indonesian poultry feed
- **Inefficient port handling facilities (insufficient berths in Jakarta)**
- **Excess demurrage due to slow turnaround of vessels**
- **Slow time for transport from port to mill requiring 2-4 times as many trucks to execute the process (with associated over capitalization of the trucking sector)**

High costs reflect inefficiencies in port and road infrastructure

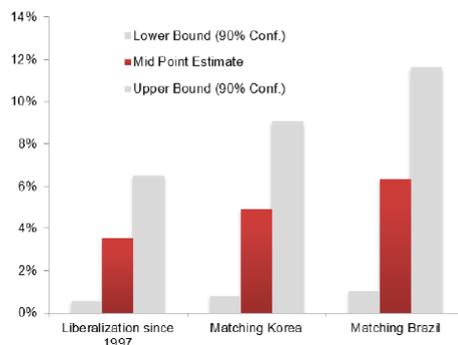


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Increased Total Factor Productivity derived from liberalization in Services in Indonesia: Comparison with Korea and Brazil

Figure 13: Estimated effects of service sector liberalization on Total Factor Productivity, and some simulations. The red bars indicate the point estimates of the induced effects; the grey bars show the lower and upper bounds of 90% confidence intervals.



If Indonesia were to match policies of these service sector reform champions, the productivity gains for Indonesian manufacturing firms would be over 5%, instead of the 3.5% realized as results of current reforms

Source: Duggan, Rahardja, Varela. "Service Sector Reform and Manufacturing Productivity. Evidence from Indonesia" (WB, 2013)



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Where does Indonesia stand in the world with regards to...?

- ICT Development
- Environment for Doing Business
- Logistics Performance
- Trading Across Borders



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ICT Development Index (2011)



Source: ITU (2011)



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Doing Business Index (2012) in Indonesia and RCEP Countries

Economy	Ease of Doing Business Rank	Starting a Business	Dealing with Construction Permits	Getting Electricity	Registering Property	Getting Credit	Protecting Investors	Paying Taxes	Trading Across Borders	Enforcing Contracts	Resolving Insolvency
New Zealand	3	1	6	32	2	4	1	21	25	17	13
Korea, Rep.	8	24	26	3	75	12	49	30	3	2	14
Australia	10	2	11	36	37	4	70	48	44	15	18
Japan	24	114	72	27	64	23	19	127	19	35	1
China	91	151	181	114	44	70	100	122	68	19	82
Indonesia	128	166	75	147	98	129	49	131	37	144	148
India	132	173	182	105	94	23	49	152	127	184	116

Total 185 Economies

Source: Doing Business Index 2012 (WB)



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Logistics Performance Index Ranking (2012) in Indonesia and RCEP Countries

Country	Ranking
Japan	8
Australia	18
Korea, Rep.	21
China	26
New Zealand	31
India	46
Indonesia	59

Total 155 Economies

Source: LPI ranking and scores, 2012. (WB)



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Trading Across Borders Index (WB - 2012) in Indonesia and RCEP Countries

Country	Rank	Documents to export (number)	Time to export (days)	Cost to export (US\$ per container)	Documents to import (number)	Time to import (days)	Cost to import (US\$ per container)
Korea, Rep.	3	3	7	665	3	7	695
Japan	19	3	10	880	5	11	970
New Zealand	25	5	10	870	6	9	825
Indonesia	37	4	17	644	7	23	660
Australia	44	6	9	1100	7	8	1120
China	68	8	21	580	5	24	615
India	127	9	16	1120	11	20	1200

Total: 185 Economies

Source: Table made using the Tradin Across Borders, Doing Business Index 2012 (WB)



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Indonesia: where is space to improve in trade?

Nature of Export Procedures	Duration (days)	US\$ Cost
Documents preparation	11	150
Customs clearance and technical control	1	169
Ports and terminal handling	2	165
Inland transportation and handling	3	160
Totals	17	644

E.g. Days for document preparation take more than 55% of the process for both imports and exports

Nature of Import Procedures	Duration (days)	US\$ Cost
Documents preparation	13	210
Customs clearance and technical control	4	125
Ports and terminal handling	4	165
Inland transportation and handling	2	160
Totals	23	660

Source: Trading Across Borders, Doing Business Index 2012 (WB)



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Recommendations for Policy Makers - Government

- Create an agency or an inter-ministerial committee that focuses on logistics performance
- Establish a working group that incorporates the private sector into these discussions
- **Design a program to reduce logistics barriers to trade, especially those that can be addressed by policy making (clearance processes at customs, transport, infrastructure): (New 5-Year Plan?)**
- Take special account of SMEs needs, which still have a huge potential for the international market



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Recommendations for Policy Makers - Negotiators

- Focus on services that impact on logistics and liberalize them
- Launch a global effort to pursue conversion of manual and paper-based documentation to electronic systems, using globally agreed data formats
- **Take into account that policy restrictiveness toward foreign firms in the service sector seems to be a clearer determinant of manufacturing performance than actual FDI flows in services : OPEN UP FURTHER KEY SERVICE SECTORS TO FDI, i.e. TRANSPORT, DISTRIBUTION, TELECOM**
- In negotiating trade agreements, pursue a “whole of the supply chain” or “holistic” approach to negotiating removal of barriers



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Expanded AFAS / RCEP Trade Agreement

Liberalizing Commitments
in Logistics Services

Border Administration –
more Efficient

These two topics could go together as the heart of a new focus in order to position the entire ASEAN region as a center of integrated production, consumption and trade.

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Thank You

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