

Competition

DISMANTLING BARRIERS TO COMPETITION AND INNOVATION

- ▶ Indonesia has made significant efforts in the last year to improve the business environment.
- ▶ But excessive and overlapping regulation, including across the different levels of government, still make establishing and conducting business difficult for both foreign and Indonesian businesses, holding back FDI and productivity in both services and goods industries.
- ▶ The performance of the Indonesian economy could be improved considerably by removing administrative and regulatory barriers to competition through a programme that reviews regulations.
- ▶ Whilst the Commission for the Supervision of Business Competition (KPPU) has developed its own toolkit (based on the OECD Competition Assessment Toolkit) to identify and lift barriers to entry that are inadvertently introduced by rules and regulations, a broader, systematic and uniform application of competition assessment would help.

What's the issue?

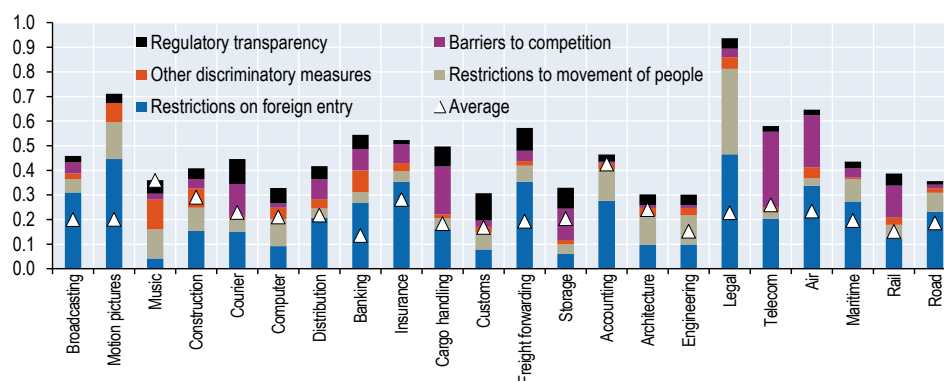
Indonesia has recently undertaken efforts to improve its business environment for both domestic and foreign firms with a series of reform packages released since September 2015, such as the revision to the Negative Investment List leading to thirty-five sectors being removed from the list and becoming fully open to foreign ownership. This improvement in the business environment is reflected in Indonesia's improved ranking in the World Bank's Doing Business report of 2016, where the country for example moved up 10 places between 2016 and 2015 on the ease of starting a business. But

while this has improved the situation, a poor business environment is still the key factor for holding back FDI, given the low starting point of the improvements. There is still excessive and overlapping regulation, including across the different levels of government, from national to sub-national government levels, which make establishing and conducting business difficult for both foreign and Indonesian businesses.

Regulatory restrictions on imports and exports of services are well above the cross-country average in

Indonesia restricts trade in services more than other countries

Services Trade Restrictiveness Index, from 0 (least restrictive) to 1 (most restrictive), 2015



Note: The Services Trade Restrictiveness Index database records measures on a most-favoured-nation basis; preferential trade agreements are not taken into account. The database has been verified and peer-reviewed by OECD members. The average is computed over all OECD and BRIICS countries.
 Source: OECD Services Trade Restrictiveness Index database.

all of the sectors covered by the OECD's Services Trade Restrictiveness Index (STRI; see Figure). This can be explained in large part by general regulations that apply to all sectors in the economy. Certain management positions in Indonesian corporations are reserved for nationals. Investments in all sectors are subject to screening, and price preferences are given to local providers in the context of public procurement. The acquisition of land and real estate by foreigners is restricted to right-to-use for only a limited period of years. The state has a prominent role in the economy. There is at least one major state-owned enterprise (SOE) in air transport, banking, broadcasting, construction, courier services, distribution, insurance, maritime, logistics and telecommunication services. A number of these SOEs are monopolies. At the same time, there are no discriminatory taxes or subsidies, and laws and regulations are transparent and grant due process to foreign providers (e.g. appeal procedures). Indonesia also applies restrictions to trade through the movement of natural persons. In particular, it maintains labour market tests on all categories of service providers covered in the STRI (i.e. intra-corporate transferees, contractual services suppliers and independent services providers). The duration of stay for all three categories is limited to 24 months on their first entry permit.

Why is this important for Indonesia?

Indonesia has a strong growth potential: it has abundant natural resources, a young population, a large domestic market and a broad-based and stable political system. Fully realising this potential will require Indonesia to improve the international competitiveness of its economy and better integrate into global value chains. A regulatory framework that is conducive to competition is also crucial in this regard, as recognised by the current government which has made improving the business climate a top policy priority. To this end, a systematic and harmonised evaluation of new and old regulations needs to be undertaken to identify and eliminate unnecessary barriers to competition. The Commission for the Supervision of Business Competition (KPPU) has developed its own competition assessment instrument that draws upon the OECD Competition Assessment Toolkit. However, implementation has so far been limited across Indonesia and there is no mechanism in place to ensure a systematic, coherent and harmonised approach is taken in the analysis of rules and regulations both horizontally across government as well as vertically at its various levels.

What should policy makers do?

- ▶ Work with the sub-national governments to move the regulation of business to best practice.
- ▶ Undertake competition assessment of the current regulatory framework in key industries to identify regulatory barriers to competition and potential alternatives.
- ▶ Implement competition assessment across ministries and on a more systematic basis to tackle significant restrictions to competition in both services and product markets.
- ▶ Integrate competition assessment as part of the regulatory process to ensure that new rules and regulations do not add new regulatory barriers to competition.
- ▶ Develop a mechanism to oversee the application of competition assessments to ensure coherent and uniform application across government and levels of government.



Further reading

OECD (2015), *OECD Competition Assessment Toolkit Vol. 1, 2, and 3*. OECD Publishing. <http://www.oecd.org/daf/competition/assessment-toolkit.htm>

OECD (2015), *The Future of Productivity*, OECD Publishing. http://www.oecd-ilibrary.org/economics/the-future-of-productivity_9789264248533-en