



CENTRE FOR
STRATEGIC AND
INTERNATIONAL
STUDIES

Economics Working Paper 03 – 2016

Services Sector Development in Indonesia and the Implementation of AEC Measures in Services

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November 2016

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Abstract

The ASEAN Member States (AMS) agreed that freer flow of services would become an integral part of the ASEAN Economic Community in order to support economic development in the region. However, while the initiative has set an ambitious target, its implementation has been less convincing. This article looks at the implementation of several ASEAN initiatives on trade in services in Indonesia. The country seems to be lagging behind in implementing its commitments to provide greater market access for services providers. Therefore, Indonesia might lose opportunity in economic development from not being able to acquire benefits from the availability of high quality services.

Keywords: Service sector, trade in services, Indonesia in AEC context

1. Introduction

The service sector is becoming more important in the current global economic environment. The sector is not only important in its own right – that is, by creating economic value and providing employment opportunities – but also crucial to improving the productivity, efficiency and competitiveness of other sectors. As an input to other economic activities, outputs of the service sector such as telecommunications and logistics can determine the overall efficiency of the production process, while business services, e.g. accounting and marketing, ensure that business can be managed in a proper and efficient manner. The provision of high quality services is therefore a prerequisite for sustainable economic growth.

Just as countries can increase economic welfare by trading without the need to produce everything by themselves, necessary services can also be supplied from abroad. In fact, trade in services has been growing at a faster pace than trade in goods since the 1980s¹ and trade in transportation services alone has increased by more than 7% over the past 15 years.

The growing importance of trade in services has attracted a lot of attention from policy makers. While trade in services allows countries to have access to the quality services they need, those countries also tend to have less favourable perspectives on giving greater market access to service suppliers from overseas. This often leads to reluctance in implementing service sector reform, as it may trigger opposition from vested interests that enjoy excess profits or rents from existing protections.

Commitments under international agreements can thus help countries gain stronger support for services sector reform. Furthermore, these agreements provide credibility in international markets, which in turn attracts investments and internationally recognized service providers. In recognition both of their rising role in international trade and of the need for further liberalization, services were included in the multilateral trade architecture of the World Trade Organization (WTO) in the form of the General Agreement on Trade in Services (GATS).

Similarly, services have featured prominently in a growing number of bilateral and regional agreements, including ASEAN and ASEAN trade agreements. The ASEAN Member States (AMS) agreed that freer flow of services would become an integral part

¹ WTO, 2012, World Trade Report 2012. Trade and Public Policies: A Closer Look at Non-Tariff Measures in the 21st Century.

of the ASEAN Economic Community in order to support economic development in the region. However, while the initiative has set an ambitious target, its implementation has been less convincing.

This article looks at the implementation of several ASEAN initiatives on trade in services in Indonesia. The first part of the article reviews several efforts that AMS have been conducting on services agreements, preceded by brief discussion on service sector development in the region. The second part examines service sector policy in Indonesia and how initiatives at the regional level have influenced the policy. Finally, the article closes by proposing several possible recommendations for policy development, both in Indonesia and for greater ASEAN integration.

2. Services Development in AMS

Table 1 presents some key characteristics of the service sector in ASEAN countries. One thing that we can see from these figures is that the service sector in ASEAN countries has a smaller role than it does in developed countries. With the exception of Singapore, services in these countries account for less than 50% of total GDP value, compared to the 70% of total GDP or more that appears in many developed economies. These figures have not changed much over the last 20 years and in countries such as Indonesia and Thailand, services contribution seems to be declining. These trends are somewhat in line with the notion of two waves of service sector development described by Eichengreen and Gupta (2009)².

Nevertheless, services in more developed countries such as Malaysia are starting to improve. This is likely the product of shifts away from traditional services, such as trade, hospitality and dining, to more modern and knowledge-intensive sectors such as finance and business, whose contributions to these economies is increasing.

While these figures represent the direct contribution of services to economies, the contribution of services as inputs to other economic activities, especially exports, is even more staggering. Figure 11 shows the contribution of services to exports from ASEAN countries, taking into account the importance of value chains in the economy³.

² Eichengreen, B. and Poonam Gupta, 2013. "The two waves of service-sector growth," Oxford Economic Papers, Oxford University Press, vol. 65(1).

³ Services contribution in an industry can come directly as services inputs in production process, e.g. transportation or business services used in the industry, or indirectly from services inputs of intermediate goods, e.g. transportation used in the upstream industry. The data from OECD Trade in Value Added (2013) take account both direct and indirect contribution of services in exports

On average, ASEAN members, with the exception of Singapore, do not include many service components in their exports when compared to more developed countries.

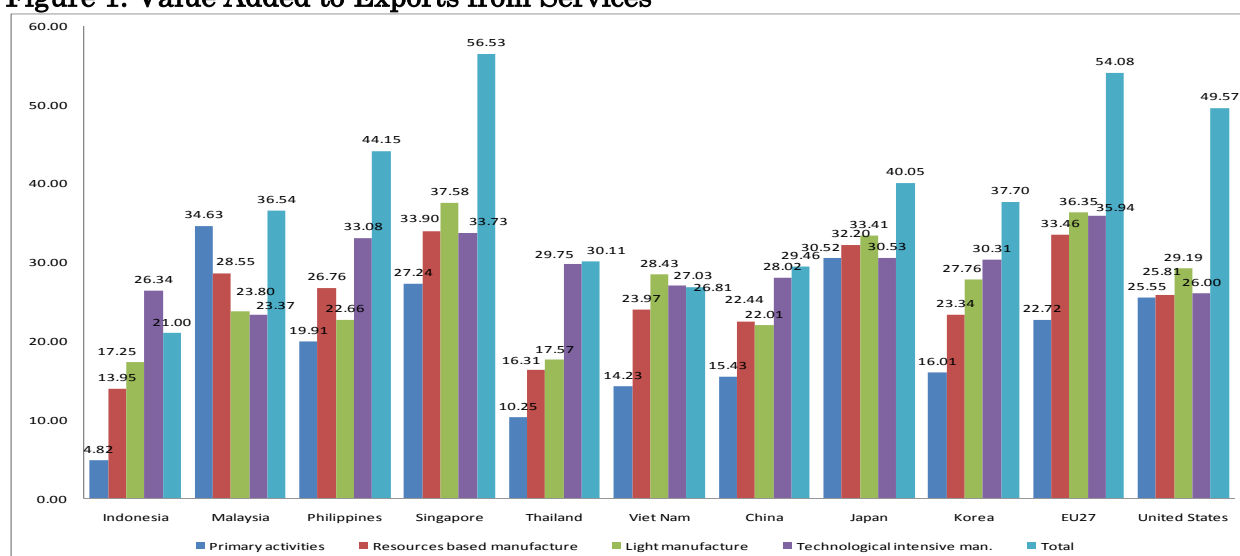
Table 1. Services in the Economy (% of GDP)

	Total Services		Trade		Hotels and Restaurants		Transport and Storage		Real Estate and Dwellings		Public Administration, Community, Personal, and Other Services		Communication, Finance, and Business Services	
	1990	2013	1990	2013	1990	2013	1990	2013	1990	2013	1990	2013	1990	2013
Indonesia	42.4	42.6	13.5	10.8	3.2	3.3	6.1	4.6	2.9	2.9	10.1	13.4	6.5	8.9
Malaysia	44.9	52.6	10.9	17.2	2.2	2.8	3.8	3.4	5.4	3.1	8.3	13.2	14.4	13.0
Phillipines	50.8	57.6	14.7	17.9	N.A.	N.A.	3.2	6.3	5.8	11.9	15.7	13.8	11.5	7.7
Singapore	67.8	66.4	13.1	17.5	3.5	2.1	11.4	6.4	3.6	4.3	9.6	10.7	26.6	29.7
Thailand	50.9	47.8	17.8	16.8	5.4	5.7	4.5	7.0	2.2	2.6	9.7	13.4	11.3	4.3
Vietnam		34.3		13.4		3.9		3.0		2.0		9.6		2.4
China	31.5	46.9	6.8	9.6	1.6	N.A.	3.8	4.4	2.1	N.A.	7.9	N.A.	9.4	N.A.
India	46.1	68.9	11.8	14.1	1.0	1.4	6.4	6.5	5.0	11.4	13.3	28.6	8.8	6.9
Korea	51.5	54.0	11.8	8.1	2.4	2.4	4.7	3.3	6.5	7.2	14.8	17.8	11.2	15.2
United States	73.4	77.6	12.9	11.7	3.4	2.7	3.0	2.9	12.1	13.0	23.0	23.7	18.9	23.6
Japan	59.8	73.6	12.8	14.4	N.A.	N.A.	4.9	4.8	9.4	11.7	19.1	24.0	13.6	18.7
France	69.2	74.1	11.8	10.6	2.3	2.8	4.6	4.7	9.8	12.0	21.7	23.8	18.9	20.3

Source: CEIC Database

In Indonesia, services only significantly contribute to the export of technology-intensive manufacturing, although that figure still remains lower than values in other countries. Elsewhere, services contribute significantly to the value of goods produced in the manufacturing sectors, making up 25-35% of the value of exported products. Again, technology-intensive manufacturing, such as that of electronics and machinery, uses more services in the production process, and is more dependent on GVCs than are other sectors of the economy.

Figure 1. Value Added to Exports from Services



Source: OECD Trade in Value Added Database (2013)

Most of the contribution from services originates in domestic economies. In Indonesia, less than a quarter of the value added to exports from services comes from abroad. In contrast, the value added from foreign services makes up almost half of the value of exports from Thailand and Malaysia. This indicates that services play an important role in international value chains occurring in ASEAN countries. Clearly, services from one country in the region not only contribute to the production of exported goods in that country, but also to the production of exported goods in other ASEAN countries. From the OECD TIVA database we can calculate that around a third of ASEAN countries' export value comes from other ASEAN countries, indicating a certain level of services integration.

However, this integration is mostly done indirectly through the services “embedded” in intermediate goods used in ASEAN production networks. Direct contribution of foreign services through export and import remains relatively low, in large part because of a strict regulatory framework governing services.

3. ASEAN's Initiatives on Services: A Brief Assessment

Recognizing the importance of services trade, ASEAN members have initiated negotiations concerning the services sector since 1995, when the countries first decided to negotiate an ASEAN Framework Agreement on Services (AFAS). Three main areas of commitments commonly appear in an agreement on trade in services. The first one is related to market access for services from abroad or from foreign services providers. The second form of commitment involves concerns about trade in services and national treatment, and regulates what foreign providers of services need in order to obtain the same treatment as domestic providers. The third area involves commitments that require domestic regulations to follow reasonable, objective and impartial rules, often achieved by providing greater regulatory harmonization.

The AFAS aims to provide greater market access and to promote national treatment, as well as to ensure other commitments concerning services from ASEAN members. Member countries have already completed nine rounds of negotiations and are currently in the midst of negotiating the tenth, with each round producing a schedule of new commitments.

These services trade commitments among ASEAN members are notable for several reasons. First, the process of integration is gradual, both in terms of the breadth of sectors being included and the level of integration and commitments. Table 3 provides a summary of the liberalization targets for services under AFAS. By 2015, there will be 128 sub-sectors committed by ASEAN members, in contrast to 2009 when there were only 65 sectors committed. Among those subsectors, 48 are highlighted as priorities and will be liberalized more progressively.⁴ In committing sectors to AFAS, countries agreed to lift restrictive measures, unless otherwise specified.

Table 2. Summary of AFAS Target

	8 th Package	9 th Package	10 th Package
Target	2012	2013	2015
No. of	80	104	128
Mode 1	All 80: None	All 104: None	All 128: None
Mode 2	All 80: None	All 104: None	All 128: None

⁴ Those 29 priority sub-sectors come under e-ASEAN, healthcare, air travel, and tourism. Nine sub-sector of logistic are later added into priority list but with later liberalization scheduling.

Mode 3MA FE	29 PIS: 70%	29 PIS: 70%	29 PIS: 70%
	51 Non PIS & LOG : 51%	9 LOG: 70%	9 LOG: 70%
		66 OTHER: 51%	90 OTHER: 70%
Mode 3 MA Limitations	29 PIS: No limitation	29 PIS: No limitation	29 PIS: No limitation
		9 LOG: No limitation	9 LOG: No limitation
	51 Non PIS & LOG: max 2 lim	26 OTHER: max 2	90 OTHER: No limitation
		26 OTHER: max 1	
Mode 3NT	Max 4 lim/subsektor (including	Max 3 lim /subsektor (including	Max 1 lim /subsektor (including horizontal)
Mode 4	To be agreed	To be agreed	To be agreed

Source: AFAS Scheduling

The level of commitment from countries has also increased steadily. AFAS clearly targets Mode 1 and Mode 2, wherein there are no limitations or restrictions for the two modes of supply for committed sectors, while restrictions are gradually lifted for Mode 3⁵. Given this, permissible foreign equity participation in ASEAN countries is expected to reach 70% by 2015, with priority sectors expected to reach that level even earlier. Limitations for national treatment as well as other limitations on market access are also expected to diminish or be eliminated by 2015.

Just like in the WTO/GATS, ASEAN countries are making commitments that are more restrictive than many domestic policies that are currently in place. Adopting a paradigm in which regulators use “policy space” to manage the services sector, commitments for liberalization, especially for Mode 3’s foreign equity participation, have been lower than what the actual policy allows, although still higher than what member countries committed in GATS. Indonesia, for example, did not schedule retail sub-sectors in the AFAS 8th commitment, although that sub-sector is allowed almost 100% foreign equity participation. In maritime services, Brunei, Cambodia and Singapore allow 100% foreign investment in some sub-sectors that they have not committed to the

⁵ AFAS follows WTO/GATS description on modes of delivery of services trade. There are four modes of supply: Mode 1 cross border supply, Mode 2 consumption abroad, Mode 3 commercial presence and Mode 4 movement of natural person

AFAS, while Malaysia and Vietnam appear to have no regulatory restrictions on entering the sectors they have not committed⁶.

Countries sometimes utilize this “policy space” by increasing restrictions in certain sectors. In 2007, foreign ownership limitations in Indonesia’s telecommunications were reduced to 49% for fixed line services and 65% for mobiles (from 95%). This can be done since AFAS and GATS commitments for foreign ownership were just below 49%.

However, some commitments appear to give preferential concessions by setting lower restrictions than actual domestic policies, especially in more recent rounds of negotiations. In short, while liberalization is still limited, the targets for services integration in the AFAS under the ASEAN Economic Community seem to have offered some concrete results.

Although the ASEAN services agreements work on a preferential basis, they also seem to moderately discriminate against non-members. This is important for two reasons: first, one of the benefits from liberalization is an increase in competition between service providers that leads to better quality services. Limiting market access to only a handful of trading partners by having restrictive “rules of origin” thus reduces the potential benefits of competition. Second, this discrimination also limits the incentives of foreign providers to invest in ASEAN countries.

This “trade diversion” effect of services agreements is reflected in the article “Denial of Benefits,” which describes the extent of benefits offered to providers from outside the region. In AFAS, in order to be eligible to receive the benefits from preferential liberalization, the requirement is simply to have substantial business operations in one of the ASEAN countries; a term which is itself up for interpretation, but which is less restrictive than requirements such as ownership⁷.

Another feature of ASEAN’s efforts towards integration is the current lack of commitment to addressing domestic regulations at the regional level. The AFAS does not specify how members deal with diversity and differences in the regulatory framework of services. Line ministries and government agencies have separate venues

⁶ Dee, P., 2013, “Does AFAS have Bite? Comparing Commitments with Actual Practice”, available at https://crawford.anu.edu.au/pdf/staff/phillippa_dee/2013/does-afas-have-bite.pdf. Last retrieved at 15 September 2015

⁷ Beviglia-Zampetti, A. and P. Sauvé, 2006, “Rules of Origin for Services: A Review of Current Practice,” In Estevadeordal, Antoni et al., (eds), *The Origin of Goods*, Oxford University Press and CEPR, London.

to discuss their specific services development, such as ASEAN ministerial meeting for telecommunications or for transportation.

These sector-specific regional forums are intended to be a medium of greater cooperation. However, the programs of these ministerial meetings are aimed at inducing technical cooperation, as opposed to cooperation over regulation and policies. The sectoral approach of this cooperation framework also increases the possibility of preserving old paradigm of services development that tend to miss cross-sectoral linkages and the importance of the services sector.

The only efforts toward regulatory cooperation are those conducted through mutual recognition agreements that focus on eight professional fields: medicine, nursing, dentistry, architecture, engineering, land surveying, accounting, and tourism. The MRAs are intended to facilitate the movement of skilled labor by allowing for the mutual recognition of qualifications of professional services suppliers from other ASEAN countries. While this facilitates the exchange of skilled labor, more time is needed for these countries to design more coherent regulations.

In summary, AMS's commitments on the services sector is limited only to its liberalization aspects, by agreeing to have greater market access among ASEAN members, particularly on foreign equity limitations and national treatments. However, such liberalization may not have significant effect on the actual policies in each country, since many of the commitments are still below the actual current regime of allowable foreign participation. In addition, facilitation in the services sector is limited to the MRAs for eight professional sectors, with no plan to discuss future regulatory harmonization.

4. Indonesia and ASEAN Services Initiatives

4.1 Policy in Indonesia's Service Sector

Indonesia's service sector has emerged as a new source of growth. While the sector has always been the largest in the Indonesian economy, several changes have taken place during the last three decades of economic development. Along with the economy's structural transformation from agricultural-based economy to manufacturing and later to a services-based economy, the service sector's contribution to Indonesia's GDP has increased from 38% in 1970 to 51% in 2014. In accordance to its greater contribution to GDP, the services sector has become the biggest source of job creation as

well, constituting 43% of total employment. Indonesia's services trade has also grown steadily due to increasing export and import activities.

Indonesia does not have a single comprehensive development policy on services; instead services policy is split across several different sets of policies according to each service sub-sector. The development of the services sector, however, is discussed in the Medium Term National Planning (*Rencana Pembangunan Jangka Menengah Nasional*, RPJMN) 2015-2019, with a focus on increasing service sector competitiveness to reduce trade balance deficits⁸. The policy is also related to the introduction of some restrictive measures to limit services imports. However, there is not much discussion in the RPJMN on a strategy for services development in order to support general economic performance and competitiveness.

The introduction of restrictive measures in RPJMN comes from the concern that one of the important sources of Indonesia's current account deficits is the import of services. This includes the use of transportation from foreign providers as well as the import of financial services. In fact, almost half of Indonesia's services imports are in transportation and financial services; thus, the government is willing to reduce the deficit by increasing the competitiveness of domestic providers.

While this is a reasonable concern, it is also worth mentioning that the reason behind this increase is related to ever growing international trade activities. As trade has been growing rapidly during the last three decades, the need for logistic services has become more prominent and cannot be satisfied by domestic transportation providers. A similar situation has also happened for trade financing and insurance that has caused an increase in Indonesia's import of financial services. So while the import of services may put services balance in deficit, it is necessary to support exports and to improve competitiveness in general. Putting more restrictive measures on the import of services might harm the competitiveness of the Indonesian economy even further, especially if domestic providers are not able to meet that demand or to provide quality services.

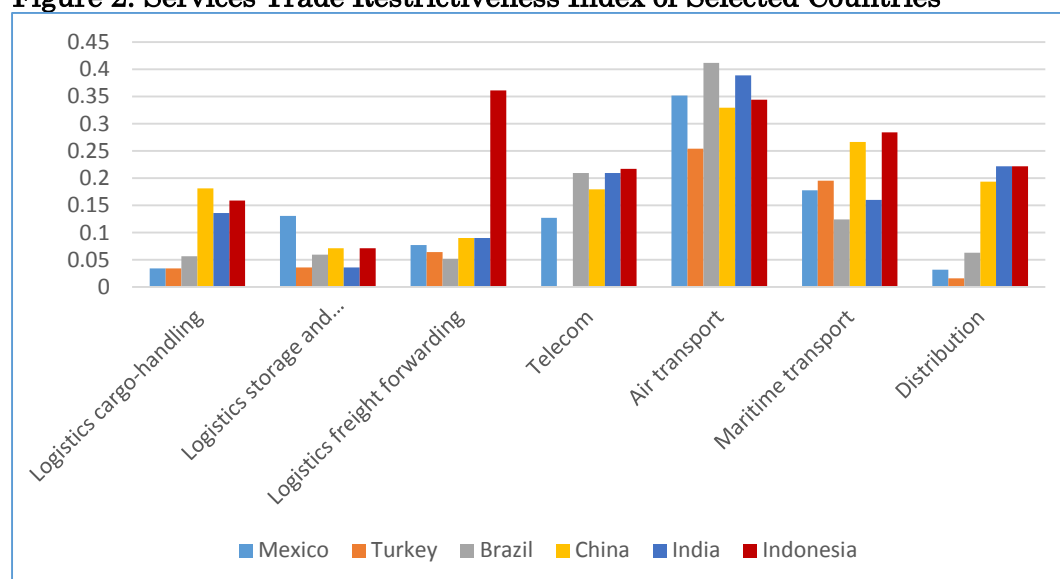
The Services Trade Restrictions Index (STRI) compiled by the World Bank shows that Indonesia's overall STRI is relatively high among East Asian countries. Indonesia's relatively high STRI is related to the high restriction in road freight transportation, rail freight transportation and professional services in legal professions. While Indonesia's restriction is comparable to other countries in the region under Mode 1 (cross border

⁸ Republik Indonesia, Rencana Pembangunan Jangka Menengah Nasional 2015 -2019 Buku 2 (RPJMN, National Medium-Term Development Plan 2015-2019, Book 2)

supply) and Mode 4 (movement of natural persons), Indonesia is more restrictive in Mode 3 (commercial presence) than many other countries⁹. Since a bigger portion of services trade is conducted through commercial presence and investment, these policies create significant restrictions to trade.

Another STRI indicator from OECD provides a detailed description of restriction policy. Figure 2 provides a glimpse of the level of restriction for several sectors, especially those important for productivity improvement and competitiveness. Indonesia's policy is relatively more restrictive than other emerging countries, particularly in logistics and maritime transport. Higher STRI is due to restrictive policy on foreign investment to those sectors. Indonesia's new 2014 negative list of investment, for example, allows lower foreign participation in logistic sector than the 2010 negative list. Given that improvement of the logistics sector depends upon the development of port services and multimodal services, limiting foreign ownership might hold back the development of services sector in Indonesia.

Figure 2. Services Trade Restrictiveness Index of Selected Countries



Source: OECD STRI

4.2 Implementation of AEC Services Measures

As mentioned above, services agreement among ASEAN countries focus on liberalization efforts, in particular in Mode 1 and Mode 3. Of all the targeted 128 subsectors being liberalized with a foreign equity limitation of more than 70% by the

⁹Services Trade Restrictions Index, the World Bank, available at <http://iresearch.worldbank.org/servicetrade/default.htm#>, accessed at 15 August 2015

end of 2015, there are 104 subsectors have been committed in the latest AFAS Package 9. The commitment in the Package 9 allows foreign equity participation (FEP) to be greater than 70% for 29 priority integration sectors (PIS) and 9 logistic sectors, and to be greater than 51% for all other 66 services sectors¹⁰. Indonesia has managed to follow commitments in the Package 9 for 81 subsectors of 104 subsectors being committed. The biggest number of services subsectors with FEP greater than 51% fall under business services.

Despite being one of the priority sectors, Indonesia seems to be lagging behind in following commitments in health related services, although some progress has been made. In the new Negative Investment List (*Daftar Negatif Investasi*, DNI) issued in 2014 new exceptions were made for ASEAN investors, which seems to be a step forward in ASEAN integration. This Negative Investment List allows 70% foreign ownership in hospitals held by ASEAN investors in all provincial capitals in East Indonesia except Makassar and Manado. However, there is presently no visible progress toward implementing commitments on other health services.

The country also has difficulties implementing the commitments in communication services. Only around a third of fifteen communications subsectors being committed as PIS have reached the target of having foreign equity limitation greater than 70%. On the 2014 DNI, there has been both progress and regression in terms of the telecommunication sector's openness to foreign investment. Fixed telephone lines are now open to being financed by a maximum of 65% foreign investment, which constitutes a rise from the previous 49% limit. However, a serious regression has occurred in the data communications and internet access sector, where the maximum amount of foreign ownership allowed for both services is now 49%, as opposed to the previous 95% maximum for data communications services and 65% for internet access services.

Indonesia will face even greater difficulties implementing the target for services liberalization currently being discussed under AFAS package 10. Under the current regulatory environment, many subsectors still limit FEP to less than 70%. Many of the limitations are described in the 2014 DNI. Indonesia might revise the DNI to allow exceptions for foreign equity from other ASEAN countries, which would be quite straightforward since the DNI is normally dictated by a Presidential Regulation that requires no parliamentary intervention.

¹⁰ The 29 PIS include subsectors in four services sectors of business services, communication, health related and social services and tourism and travel services.

Problem can arise in other subsectors in which the FEP limitation is regulated by laws, which are determined by legislative process. This is the case for many subsectors, including logistics, which is part of PIS. Since revision of these laws will take time and a lot of effort, Indonesia might require transition time to implement the services liberalization target.

Indonesia might also face issues related to national treatment principles of the services agreement in AFAS, especially with regard to taxation policy, land use and professional qualification requirements. Indonesia's tax laws dictate that foreign and joint venture companies are subject to different treatment than domestic firms. Indonesia also prohibits foreign companies from owning land, although joint ventures are exempted from this prohibition and allowed to have land use rights as well as building rights. However, these regulations might not be in line with the target of having an equal national treatment principle under AFAS.

4.3 Implementation of MRA in services

There are several approaches to how MRAs for services are to be implemented among ASEAN countries. MRAs for architectural and engineering services have a clearly laid out course of action; the agreements are equipped with guidelines on criteria and procedures to obtain the status of an ASEAN Chartered Engineer/Architect. The agreements also specify the establishment of committees at regional level to coordinate and monitor implementation. MRAs on nursing services and tourism professionals also describe actions needed to develop the core competencies needed in the regional committees. Finally, there are MRAs for dental and medical professionals that both describe guidelines for the recognition of foreign professionals and also state that they need to be in compliance with the host country's requirements and necessary assessments. MRAs in other professional services require ASEAN countries to conduct bilateral or multilateral agreements to enhance the mobility of professionals.

Indonesia has implemented MRAs in engineering services and architecture by establishing the Indonesia Monitoring Committees; an agency responsible for developing, processing and maintaining registrations for ASEAN chartered engineers and architects. Despite reasonable implementation of the MRAs for these two services, the agreements seem to have been unsuccessful in attracting professionals to apply for regionally recognized certifications. In architecture, there are only 129 domestic applicants who have undergone the screening process, and only 51 that have been

selected and registered as the ASEAN Architects (AA) by the ASEAN Architect Council. In engineering services the situation is also the same: only 211 domestic applicants have undergone the screening process, while 154 domestic applicants have been selected and registered¹¹.

Being registered as an ASEAN Professional, however, does not mean that foreign workers can automatically work in Indonesia. Foreign architects, for example, must also be registered with the Ministry of Manpower as foreign workers, as described in Decree of the Minister of Manpower and Immigration No. 12/2013 concerning Guidelines for Recruiting Foreign Workers, and Law No. 6/2011 concerning Immigration. However, foreign architects face little urgency to get registered since the regulations do not appear to be sufficiently binding and they can still practice as consultants or corporate employees without obtaining foreign architect status.

Indonesia has also been quite successful in aligning its regulations to support the implementation of MRA in nursing services, especially in creating an official framework within which foreign nurses can come to work as registered nurses in Indonesia. The registration process for foreign nurses working in Indonesia is very similar to that of native nurses, although the permits for foreign nurses expire much sooner. However, despite all the facilitation there are officially no foreign nurses currently working in Indonesia, although it has been recognized that many have entered the country as consultants and are therefore not registered through the ASEAN MRA.

Since the other MRAs for medical and dental professionals do not specifically provide details on how movement of these professionals should be facilitated, the implementation at national level remains improper. There are some efforts toward harmonization of regulations to ensure that they support and do not contradict MRA implementation, though the scale is very limited. There are also attempts at dissemination of MRA-related information through a website, but language barriers remain an issue that has prevented sufficient access to this information.

¹¹ Damuri, Y.R., I. Setiati, D. Christian, E. Sasmito, 2014. *ASEAN Economic Scorecard (AEC) Phase Four: Furthering the Implementation of AEC Blueprint Measures*. Unpublished Report of CSIS for ERIA.

5. Policy Recommendations for Indonesia: Why Should the Country Pursue More Progressive Attitude?

The main bottleneck in service sector development in Indonesia, including in implementation of AEC commitments, is institutional reluctance. The regulatory authorities seem to lack political incentive to liberalize the sector further to meet AFAS commitments. The government of Indonesia is still reluctant to commit to further liberalization, even for the sectors and subsectors that have little or no foreign investment restrictions. This lack of political incentive seems to stem from the view that regional commitments do not align with the national interest or the specific interests of the regulatory authorities. Also, there still may be a widespread belief amongst various authorities that integration brings more harm than good to the country.

Despite being framed as protecting the national interest, protectionist policy has cost Indonesian society very dearly. For example, the lack of political incentive to liberalize the healthcare sector has led to deficient healthcare facilities in several regions in Indonesia and also in the quality of service delivery. In another instance, the protectionist regulatory regime in the maritime sector has imposed high transportation and logistics costs on the users of these services, as supporting infrastructures and efficient cargo handling processes remain highly insufficient. Internet fixed broadband penetration rate in Indonesia is among the lowest of ASEAN member countries; only 1.19 persons in 100 inhabitants are connected to broadband internet, which is much lower than Malaysia (10.14) or Thailand (8.21)¹².

The government of Indonesia should realize that further liberalization of services would help building the country's competitiveness and is necessary to support economic development. Greater market access to the services sector would enable the economy to take advantage of higher quality services available in the region. In addition, while in the short term intense competition may hurt domestic producers of services, in the longer term deeper liberalization increases incentives for domestic providers to innovate and improve their performance. Positive impacts can be found in several cases of services liberalization in Indonesia, e.g. the airline industry and mobile telecommunication.

¹² ITU Key ICT Indicators, available for download at <http://www.itu.int/en/ITU-D/Statistics/Pages/stat/default.aspx> Last retrieved on 30 August 2015.

While a deficit in services balance might be an obvious and reasonable concern, it should be noted that the solution to this issue may not necessarily come from reducing services imports or erecting more restrictive regulations. The availability of high quality services, even if they come from abroad, would improve Indonesia's competitiveness and eventually increase exports. Deficits in services trade is not a problem if the trade balance can record a substantial surplus as a result of an improvement in competitiveness, while at the same time it reduces the pressure of current account deficits.

Since most industrial benefits of liberalization come from competition, creating pro-competitive regime can be an alternative to liberalization. With a stronger competition policy regime existing providers would need to rearrange their business strategy and work in more efficient manner, which would be beneficial not only for the competitiveness of services, but also for the economy as a whole. Indonesia adopted formal competition policy regime in 1999 by enacting a law on competition and founding a committee to oversee its implementation. However, these institutions still need to be strengthened in order to create pro-competitive regime. In order to increase the competition, it is necessary for the country to facilitate business creation so that it will be easier for potential service providers to set up new businesses and bring competition to the industry.

It is also important for Indonesia to specify a roadmap for regulatory reform in the services sector. This would serve as reference for businesses to prepare for the future actions, and contribution from business will be crucial to implementing this kind of roadmap. A forum for dialogue between stakeholders in services may contribute substantially to the creation of the roadmap as well, especially with regard to service sector development. It is also important for this roadmap to be in line with Indonesia's commitments in AEC measures and to take advantage of regional initiatives.

6. Policy Recommendations at Regional Level: Where Should ASEAN be Heading?

ASEAN has gone a long way towards integrating its services sectors with all the commitments under AFAS and the promotion of mutual recognition agreements (MRAs). However, there remain areas where ASEAN can enhance integration in the region.

Services development in the region needs to be based in the new perspective of GVC development, in which services are considered important both in their own right,

as well as functioning as “enablers and inputs” to other economic activities and sectors (including other services sectors, manufacturing, or agriculture). While this might appear to be common sense, the complete adoption of this philosophy would bring about a substantial change to service development strategies. The objective of services development should no longer be about how to create competitive sectors, but rather about how to provide high-quality, efficient and cheaper services. Countries can build strong domestic services to support both value chain development and upgrading, but should not do so through regulations that favour inefficient providers who could jeopardize the whole supply chain.

AFAS should aim to promote a greater amount of liberalization in the context of regional integration, using the development of a regional value chain. Member countries should thus use existing negotiation frameworks to commit to greater regulation beyond that which already exists in their regimes. It may be a good time for ASEAN members to consider new approaches towards liberalization, including the use of a negative list approach or hybrid approach.

The current AFAS uses a GATS-like approach, wherein members agree to open up their services market by deciding which service sectors they need to liberalize and what commitments would work best to achieve these ends. In contrast, negative list agreements start with the assumption that an economy should be principally free from restrictive measures unless an exception is specified. This principle encompasses various agreements concerning investment, cross border services, and the movement of natural people.

While the integration of services among ASEAN countries would bring a lot of benefits to economies across the region, non-discriminatory liberalization initiatives offer the potential to benefit them even more. ASEAN countries should also participate more in multilateral schemes. Since all members with the exception of Lao are members of the WTO, ASEAN should make more harmonious decisions in other multilateral trading forums. For example, ASEAN members should work together while negotiating the Trade in Services Agreement (TISA), which is an attempt to extend GATS commitments, frameworks, and scheduling modalities. If accepted by WTO Members, this agreement will complement and strengthen the GATS, in the same way that GATT 1994 complemented & strengthened GATT 1948.

Lastly, in addition to liberalization, cooperation over domestic regulations regarding services needs to be taken more seriously. A certain degree of regulatory coherence should be achieved to ensure better services development and to support the regional value chain. Regulatory coherence can be achieved through the formation of guidelines that lay down guiding principles for the regulation of specific sectors (as was done in the Telecommunication Services Reference Paper from the WTO). However, these guidelines must be subject to review after certain periods of time in order to keep them up-to-date with new developments.