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Utilization of Free Trade Agreement in Indonesia: Firm-Level Data Analysis of the Yogyakarta Special Region

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Abstract

This study aims to observe the utilization of Free Trade Agreement (FTA) in the Special Region of Yogyakarta. The findings are obtained by processing primary data collected from in-depth interviews and a survey of firms by applying descriptive analysis. The findings show that FTA is utilized by merely 44% of the total population of 64 firms in Yogyakarta. The benefits of FTA obtained by firms include market access, ease of processing custom documents, and lower preferential tariffs. However, the disadvantages include onerous document requirements, limited information, and difficulties in understanding regulations. Another issue related to the utilization of FTA concerns the additional provisions, such as product certificates, timeliness in obtaining COO, guidelines on information access, and registration procedures. The policy implications of the findings are discussed in conclusion.

Keywords: Free Trade Agreement; utilization; business sector; firm-analysis

JEL classifications: F13; F14; F61; O24

1. Introduction

Free Trade Agreements (FTAs) are one of the most popular international trade liberalization instruments and have been implemented by many countries. The World Trade Organization (WTO) reports that the total number of identified FTAs in 2018 is 583, both at bilateral and regional levels¹. Particularly in Asia, the proliferation of FTAs has been mainly motivated by several events, including the economic integration between Europe and North America; the rise of the Asian economy as a global destination for production network following the 1997–1998 economic crisis; the establishment of the Association of Southeast Asian Nations (ASEAN); and as a response to the slow develop-

ment of the results of the 2011 DOHA round of WTO (Asian Development Bank [ADB] 2008).

In their development, FTAs have been widely debated among academics, policymakers and business actors. The debates have included their impact on economic and discriminations caused by the utilization of FTA schemes (WTO 2011). The rise of trade liberalization in Asia with the utilization of FTAs has occurred superficially and has failed to cover all trades in goods and services, causing an overlap in their employment (Das 2012).

Studies have been conducted to estimate the economic impact of FTAs using various approaches. The most common of these approaches are the gravity model and computable general equilibrium (CGE). Both have been widely used for in-depth observation of any improvements in welfare and income (Kawai & Wignaraja 2010b). The utilization of FTAs has been observed with regard to the volume of exports and imports at industry level, assuming that any firms utilizing FTA schemes and their facili-

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¹ *Regional Trade Agreements and Preferential Trade Arrangements*, https://www.wto.org/english/tratop_e/region_e/rta_pta_e.htm viewed on September 10, 2019.

ties can maximize their profits (Dean & Wignaraja 2007).

Despite their common use, the gravity model and CGE are unable to measure utilization. In order to observe the employment of FTAs, micro-level study is needed by conducting surveys at the firm level. However, many firms have failed to utilize FTA facilities optimally. Some are even unfamiliar with such agreements. This situation is in line with various research findings from Asia, showing that the employment of FTAs is non-optimal (ADB 2008; Baldwin 2007). The results of several studies conducted in Asia, such as those by Kohpaiboon & Jongwanich (2015), Takahashi & Urata (2010), Yunling (2010), Wignaraja (2014), and Hayakawa, Laksanapanyakul, & Shiino (2013), demonstrate that the utilization of FTAs by Asian firms is low. Such utilization in the business context encounters many impediments and problems, resulting in its less than optimal use.

Since Indonesia's involvement in AFTA in 1998, the government has been initiating trade agreements within an FTA framework with other countries every year. This is in line with the government's strategic plan to increase the volume of Indonesian trade and widen access to international markets².

However, the Indonesian economy has not seen a significant impact, as shown by the volume of national trade (Effendi, 2014). Sitepu & Nurhidayat (2015) find that five Indonesian FTAs are underutilized, as measured by FTA preferential indicators. Hayakawa (2015) uses Japanese-affiliated firms in ASEAN as a research sample and finds that the firms operating in Indonesia encounter several impediments that cause less than optimal utilization of FTAs, especially in the AFTA framework.

Therefore, this study on the utilization of FTAs using a survey of firms is important. It aims to stimulate the employment of FTAs by considering their ben-

efits to economic development, particularly to the performance of international trade. With regards to its objective, the study attempts to examine the utilization of FTAs at the firm level by conducting a survey in the Special Region of Yogyakarta. Based on a report on import-export performance in the Special Region of Yogyakarta, there is an increase in the numbers of Certificates of Origin (COO) by 17.5% from 2016 to 2018 and the number of the exporters each year³. This indicates an improvement in export performance in the province during this three year period.

In the same period, the value of non-oil and gas exports increases by 19.35%, a greater percentage compared to the average export value in other provinces such as Java and Bali⁴. The availability of an international airport and customs offices for type-B customs and excise has supported the export-import activities. In addition, Yogyakarta, as one of main tourist destinations, has needed less time to internationalize from the outset due to its high exposure to foreigners (Revindo 2017a).

Similar regional studies have been conducted in Japan and China. In Japan, Takahashi & Urata (2008) conduct surveys on Japanese firms in Osaka, Kobe and Kyoto to examine the utilization of Japanese FTAs. In addition, Yunling (2010) conducts a study on various provinces and big cities in China. These studies aim to establish the use of FTA schemes in the business sector, particularly at the regional level.

This study aims to observe the utilization of FTA schemes by firms and to identify the benefits and impediments encountered by them in the process. In addition, the study is expected to provide an academic contribution to the empirical studies regarding the utilization of FTA due to the limited studies at the micro-level.

²Strategic Plan of the Indonesian Ministry of Trade 2015–2019, <https://www.kemendag.go.id/files/pdf/2016/08/31/rencana-strategis-2015-2019-id0-1472633241.pdf> viewed on September 10, 2019.

³Realization of Export Import Performance Report, December 2018, The Daerah Istimewa Yogyakarta Industry and Trade Office

⁴Provincial Non-Oil and Gas Export Development, 2018, Ministry of Trade.

2. Literature Review

Economic integration through trade agreements is one option for removing trade barriers (WTO 2011). Bhagwati, Greenway & Panagariya (1998) explain the relationship between discriminative trade policies—Custom Unions (CU) or PTAs (Preferential Trade Agreements, including Regional Trade Agreement and Bilateral Free Trade Agreement)—and non-discriminative trade policies of the WTO. The CU concept, adopted from Viner (1950), is regarded as the first phase of regionalism, followed by FTA (Bhagwati 1991). These are basically discriminative trade policies, as opposed to the GATT with MFN tariffs.

A free trade agreement basically aims to eliminate trade barriers, both tariff barriers and non-tariff barriers, to member countries, in order to increase the prosperity of the member countries (Baldwin & Kawai 2013). For this basic purpose, many countries around the world have initiated agreements at the bilateral, regional and multilateral levels. Maggi & Rodriguez-Clare (1998) identify two main reasons for a country to commit to FTA. First, the state attempts to minimize losses due to distortions caused by politically-protected industries by other countries, in which the countries do not have a comparative advantage over organized industries or products. Second, an attempt is made to prevent delayed losses from the process of impairment or productivity in any business sectors depending on governmental protection.

The formation and initiation of FTAs is developing extensively, marked by the increasing number that have been notified and submitted to the WTO. This has led to a debate regarding their positive and negative impacts, especially their effects on the business world. Kawai & Wignaraja (2010a) discuss two contradictory views of FTAs, namely their benefits to the business world and the negative impacts of their utilization. Bhagwati (2008) remarks that the utilization of FTAs in developing countries remains discriminatory and results from comprehensive negotiations. Another cost of FTAs is the

trade creation effect on local firms in less competitive member countries, in which they lose in the competition with more competitive member states. This means less competitive countries experience decreasing welfare (Bhagwati & Panagariya 1996).

Trade between FTA members is growing, as the number of agreements increases. Nevertheless, it remains unknown how intensively Asian FTAs are actually used (Hiratsuka et al. 2009). About one half of world trade is now taking place among FTA members (WTO 2007). However, examining total trade flows between FTA partners overstates the amount of trade that takes place on a preferential basis. This is partly because the tariff schedules of many FTA members increasingly contain duty-free MFN rates without further tariff reductions.

Actual utilization of preferential rates depends on a range of factors (WTO 2007). It is related both to the benefits of using preferences (notably the size of the preference margin) and the costs (e.g. the rules of origin and other administrative requirements to be fulfilled). This implies that firm-specific characteristics, such as size, experience, ownership and access to information, are the determining factors in the utilization of FTAs.

The recent development of FTA studies has sparked two strands of academic focus in Southeast Asian economics. Model-based studies attempt to analyze the economic effects of FTAs. Two movements have developed within this type of study. The first uses the partial equilibrium gravity model of bilateral trade to evaluate the trade creation and trade diversion effects of FTAs (Yang & Martinez-Zarzoso 2014), while the second uses the sophisticated computable general equilibrium (CGE) model to simulate the welfare effects of FTAs. By assuming that any firms can maximize their profits and completely utilize FTAs with sufficient information and knowledge, the study predicts that FTAs substantially increase welfare and income (Dean & Wignaraja 2007).

Research on the employment of FTAs using a firm-level survey was conducted by the Asian Develop-

ment Bank in 2007–2008 on export-oriented manufacturing firms and various types of industries in six countries in East Asia. At the same time, the Inter-American Development Bank (IADB) also conducted the same survey in four countries in Latin America (Estevadeordal, Harris & Suominen 2009). These two regions represent the vast areas for the formation of FTAs. By comparing data on customs related to commodity or product utilization preferences, the two studies concluded that many firms did not gain benefit from utilizing FTAs and some even did not use them at all.

Several factors cause the low rate of utilization of FTA by firms. The first of these is the insignificant margin of preference tariffs caused by the low MFN rates of the products or industries, meaning no profit margin is achieved (Kawai & Wignaraja 2010a). Second, the complex and restrictive ROO application process requires firms to pay transaction costs. Supposing a firm has more than one market destination country, it is required to use different FTAs and ROOs, clearly resulting in additional costs (Manchin & Pelkmans-Balaoing 2007; Tumbarello 2007).

Several studies on the utilization of FTAs in Indonesia have been conducted. In general, the results show that they remain underutilized. Wigjoseptina, Yunita & Sofiyandi (2015), in their survey on manufacturing and service firms in Jakarta and Surabaya towards ASEAN FTAs, find that low use by firms is mostly caused by limited knowledge about FTAs, and that medium and small-scale firms face more difficulties in their employment. Moreover, only a small percentage of the survey sample considered FTAs in their business planning. Sitepu & Nurhidayat (2015), from the fiscal policy office, find that five Indonesian FTAs are underutilized, as measured by FTA preferential indicators. Insignificant margin preferences and difficulties in following procedures are the factors causing this underutilization.

In addition, Tambunan & Chandra (2014) reveal that medium, small and micro firms have the least trade activity in relation to the facilitation of FTA in

ASEAN countries. This low activity is influenced by limitations of knowledge and information, financial access, and also complicated COO/ROO requirements. It is mainly only large and multinational firms that actively utilize FTAs as they are capable to do so. In spite of the escalating number of Indonesia's FTA, Revindo (2017b) found that Indonesian small medium enterprises inability to seize trade opportunity. Furthermore, Indonesian SMEs encounter varied and complicated export barriers, it might be as general export barriers, specific export barriers such as region and export stage barriers.

Indonesia began its trade liberalization within the FTA framework in 1992, marked by the country's participation and involvement in the formation of the ASEAN Free Trade Agreement (AFTA). Based on the Asian Regional Database Center database, nine FTA schemes in Indonesia are categorized as effective. These schemes have already been notified to the WTO, out of a total of 38 agreements proposed by the Indonesian government⁵.

The Free Trade Agreements that have been effectively implemented and notified to the WTO include the ASEAN FTA, ASEAN China FTA, ASEAN Korea FTA, ASEAN Japan FTA, ASEAN India FTA, ASEAN Hongkong-China FTA, ASEAN Australia-New Zealand FTA, Indonesia-Japan EPA, as well as the Indonesia-Pakistan FTA. Meanwhile, 28 agreements are still in the process of consultation, negotiation and finalization of the draft agreement letter.

The utilization of FTAs is closely related to the main users of the facility, namely firms. Use of the FTA facility in the form of Certificates of Origin (COOs) by exporters and importers can now be viewed through Indonesian electronic certificates of origin. COOs are used to certify the origin of products or commodities. They are issued by the Certificate of Origin Issuing Agency, and currently 94 agencies are spread throughout Indonesia.

Any parties holding trade agreements with countries

⁵ Lists the 48 ADB-member countries/economies in Asia and the Pacific, <https://aric.adb.org/fta-country> viewed on September 10, 2019.

that have an FTA with Indonesia can take advantage of preferential tariffs. COOs are not only used as a preference for reducing or imposing import duties with other countries, but are also useful as a main document for exporting products or commodities to other countries, as evidence for submitting letters of credit, for export financing, as a tool for checking allegations of dumping, and for determining the origin of goods⁶. Table 2.1 shows the names of the COO form codes in each FTA in which Indonesia takes part.

Table 2.1: Certificate of Origin Forms

FTA Name	COO Form Code
ASEAN Trade in Goods Agreement	D
ASEAN-China FTA	E
ASEAN-Korea FTA	AK
Indonesia-Japan EPA	IJEP/JIEPA
ASEAN-Australia-New Zealand FTA	AANZ
ASEAN-India FTA	AI
Indonesia-Pakistan PTA	IP
ASEAN-Japan CEPA	AJ

Source: Directorate General of Customs and Excise, Ministry of Finance (Processed for this study)

To support the utilization of FTAs, the government also provides an integrated online portal facility to access business license registration with customs access for exporters and importers through a single online submission⁷. In addition, Official Website Indonesia National Single Window is available to check HS codes, export duties, import duties, VAT, income tax, sales tax on luxury goods, and product restrictions.

The employment of FTAs does not only require COOs, but also an additional document, namely the certificate of ROOs (Rules of Origin) for the exporting firm. ROOs do not apply universally, thus they need to be adjusted to the destination countries in accordance with the commodity code. ROOs contain information about the authenticity of the original

⁶Regulation of the Minister of Trade of the Republic of Indonesia No 24 of 2018 on the provisions and procedures for issuing Certificates of Origin for goods originating from Indonesia

⁷Government Regulation No 24 of 2018 on electronic business licensing services and the Regulation of the Minister of Finance 71/PMK.04/2018 on permit services of electronic business attempting to integrate with customs, excise and taxation fields.

goods from Indonesia, with several predetermined criteria in each agreement⁸.

In the Special Region of Yogyakarta, the licensing and management of COOs is issued by the Certificate of Origin Issuing Agency under the Office of Trade and Industry of the Special Region of Yogyakarta. Type-B customs offices also support international trade activities related to customs administration.

Firms need to follow two processes to obtain a COO, namely registration and filing the application. Several documents need to be prepared by the exporter, including the Taxpayer Registration Number, Trade Business License, and Firm Registration Certificate. The registration process can be made by accessing the e-COO website, then visiting the Certificate of Origin Issuing Agency office and bringing the required documents for verification. Once verification has been made, the firm can use of the e-COO.

3. Method

This study used cross-sectional data sourced from the results of the survey on firms in the Special Region of Yogyakarta. The sample includes all firms that had conducted international trade activities, such as export or import, within the last 3 years (2016–2019) with countries with FTAs with Indonesia (ASEAN countries, China, Japan, South Korea, Australia, New Zealand, India, and Pakistan).

3.1. Survey

Using purposive sampling, 64 firms comprised the population sample, registered by the Department

⁸Regulation of the Minister of Trade of the Republic of Indonesia No 59 of 2019 on the second amendment to the Regulation of the Minister of Trade No 24 of 2018 on the procedures for issuing Certificates of Origin for goods originating from Indonesia.

of Industry and Trade of the Special Region of Yogyakarta. The survey was conducted from March to May 2019.

The questionnaire consisted of several sections. The first covered the identity of the firms, consisting of location, industry, product or commodity, trading activities (export or import), investment value, trading partner countries, volume and value per year. The second section included knowledge and utilization of FTA, the option of COO form, the support of relevant institutions, and sources of information in implementing FTA. Meanwhile, the third section dealt with the perceived benefits of and impediments to utilizing FTAs (including tariffs, access, ROO, non-tariff barriers, and the role of institutions).

The questionnaire also included several open-ended questions to clarify answers in the previous ones. In addition, interviews were conducted with several sample of firms to validate the responses in the questionnaire.

3.2. In-Depth Interviews

In order to support and strengthen the study analysis, open question sections were provided in the questionnaire. In addition, if the questionnaire was completed to the researcher directly, an interview was conducted to clarify the answers and to obtain comprehensive information regarding the utilization of FTA by the respondents. Interviews were held with several informants, namely firm owners, directors and import and export office staff.

The open questions included the benefits of the utilization of FTA; the reasons why firms did not obtain benefit from the use of FTA COO; and suggestions and criticisms based on experiences with the COO administrative process and ROO management, and suggestions for the future utilization of FTA schemes. The interviews allowed the researcher to obtain relevant information and descriptions related to the use of FTA schemes.

4. Results

4.1. Respondent Profile

The study included 64 firms, with the highest distribution in Bantul Regency, followed by Sleman Regency and Yogyakarta Municipality.

In addition, to broaden the information regarding the spread of the firms, the locations were divided based on the categories of special industry zone and special district zone. The enactment of special zones was based on a local government decree issued to encourage firm productivity. The map in Figure 4.2 shows the distribution of the sample respondents in the special zone.

4.2. Descriptive Findings

The results of the survey show that 44% of the firms utilize FTAs. They are quite varied in terms of scale and type of product or commodity.

Based on firm size, half of the total sample has utilized FTAs. The proportion of utilization is also influenced by the number of samples obtained, in which the proportion of large-size firms is lower than small and medium-sized ones. Figure 4.3 shows that firms in each scale have utilized FTAs. Aside from firm size, the study also consider the use of FTA schemes based on industry type.

FTA is most utilized by furniture and handicraft firms. Based on the export data obtained from the Department of Trade and Industry of the Special Region of Yogyakarta, this industry represents the highest volume and value in the region and shows the highest awareness of implementing COOs to facilitate market access⁹. The leather, leather goods and sports industry ranks second, with the main export-oriented products include sports gloves, tanning leather, and raw leather materials. In addition, other

⁹Export Import Performance Realization Report, December 2018, Industry and Trade Office of the Special Region of Yogyakarta.

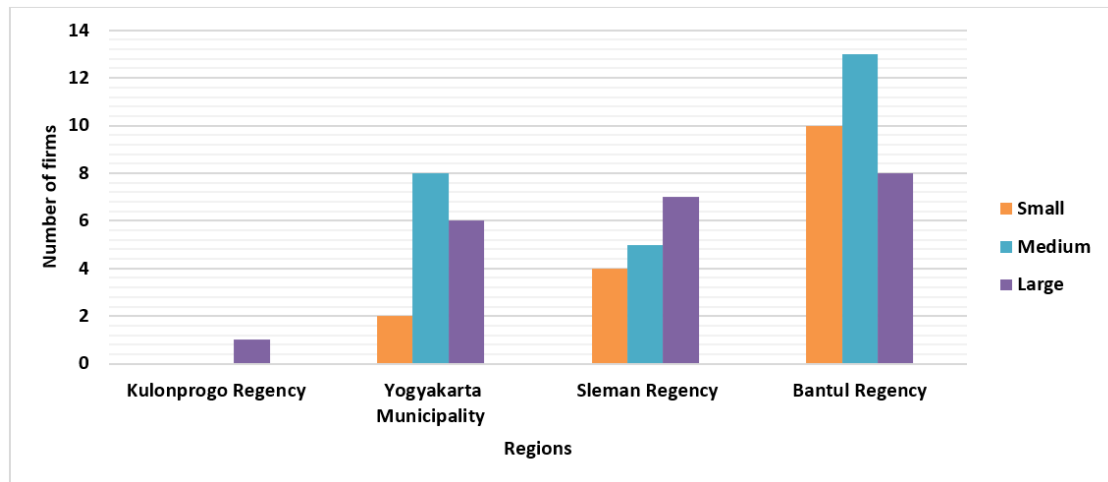


Figure 4.1: Sample Size Based on Region and Scale

Source: Author (2019)

firms include the producers of charcoal products (briquettes), wigs and sports equipment.

Considering the small size of the research sample, there are more firms that do not utilize FTA schemes. For example, charcoal products (briquettes) experience growth with the emergence of some new producers, with the majority of these products is exported to the Middle East and Europe.

The number of samples for wig firms is limited because some firms refuse to participate. Two primary industries in this study are agricultural firms producing food commodities such as fruit and the metal industry. Wood and wood products industry shows a low rate of utilization of FTA due to the complex regulations on legality and forest products. The basic metal, metal, electronics and food industry also has a low rate of use of FTA as these producers often utilize the services of third parties.

The firms already utilizing FTAs gain benefits but also encounter some obstacles. Figure 4.6 summarizes the respondents' statements regarding the benefits of and impediments to utilizing FTA schemes.

The utilization of FTA can provide benefits for firms. However, not all firms (14%) gain such benefits. Market access is the most common benefit, be-

cause the FTA members will enjoy easier access to the destination countries.

The employment of FTA schemes also affects the ease of custom administration, with a percentage of 22%. Firms that have implemented a scheme find it easier to apply for the related documents on notification of the export of goods. In addition, lower preference rates also provide benefits to the firms as they increase profit. One interesting fact uncovered by the survey is that 12.5% of firms states that the use of rules of origin in COOs provides benefits. This is contrary to previous studies mentioning that ROO is an impediment to the utilization of FTAs. Furthermore, in the use of FTAs, firms do not only gain benefits, but also encounter several obstacles, as shown in Figure 4.7.

The main impediment to the employment of FTAs is the requirements of customs regulations. Registered firms able to access the conditions on e-COOs should pay attention to PEB documents and the various processes at the customs and excise agency to obtain an export service memorandum for COO management and a COO form suitable for the destination country. Limited information and the difficulty in understanding the provisions are another impediment to using FTA. Despite the availability of an online-based service, this does not nec-

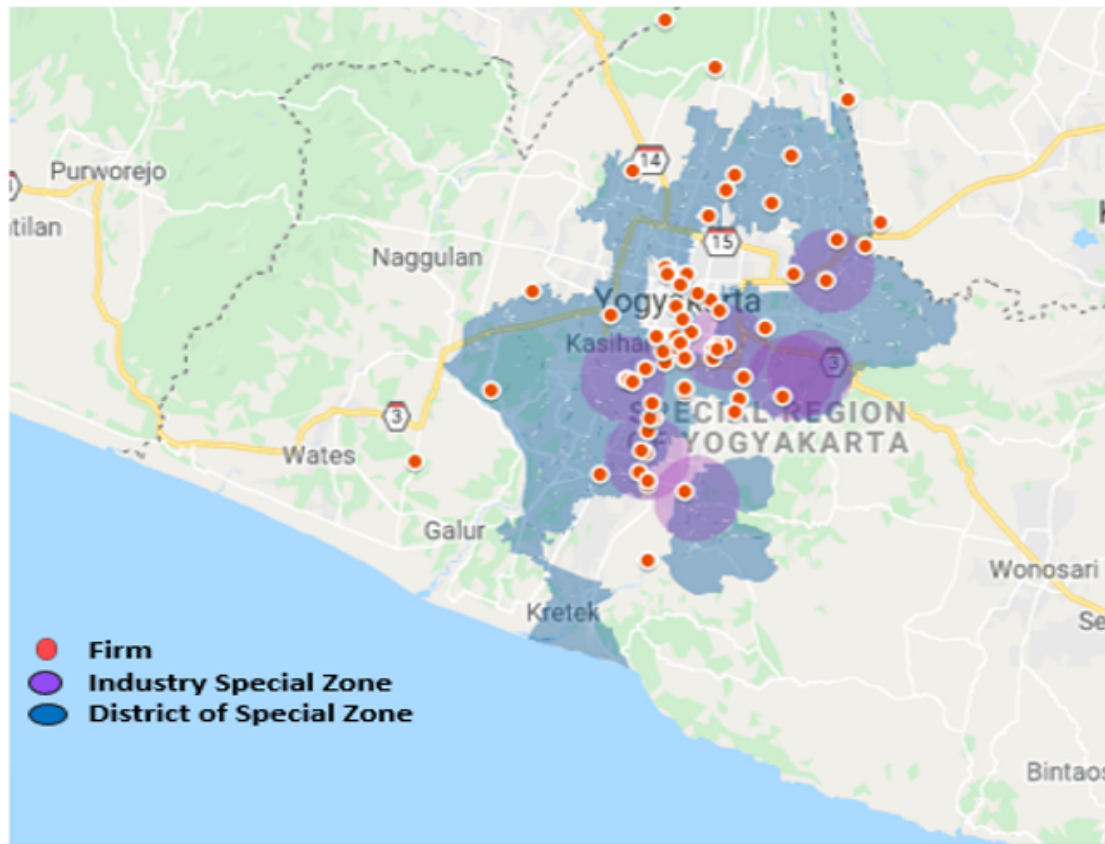


Figure 4.2: The Distribution of Sample
Source: Author (2019)

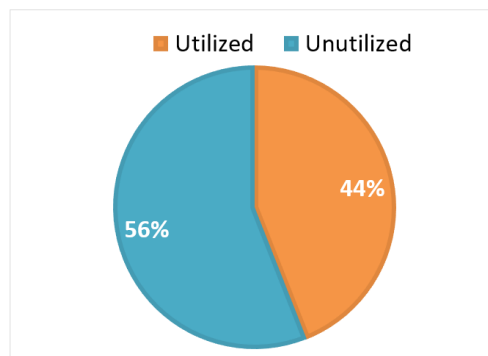


Figure 4.3: Utilization of FTAs by Firms
Source: Author (2019)

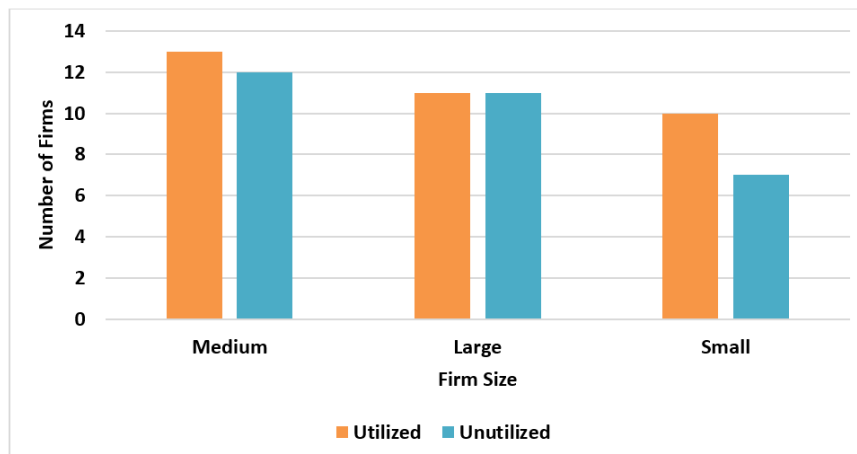


Figure 4.4: Utilization of FTA Based on Firm Size

Source: Author (2019)

essarily provide easy access to information. In addition, due to several technical regulations related to products, firms find it difficult to adjust the provisions to their products. This adjustment also adds additional costs for firms. However, some firms (17.24%) find no impediments to utilizing FTA schemes.

Based on the results of the survey, 56% of the sample firms does not utilize FTA schemes. Several main reasons for this are revealed by the firms, as presented in Figure 4.8.

The most common reason why firms do not implement FTAs is cooperation with third-party services in the management of documents and the delivery of goods. These third-party services usually provide forwarding services or sea cargo expeditions. Difficulties in obtaining information is the second biggest reason for firms not using FTA schemes. There are two issues related to the delivery of information: first, the information provided by the government is not delivered appropriately; and second, problems in the firm such as a lack of resources disrupt the delivery of information regarding the utilization and provisions of FTA schemes. In addition to issues regarding information, complex regulations also affect firms' decisions not to employ FTA schemes, related to the complicated process of obtaining COO forms. Observed from the business perspective, speed and accuracy are required in

delivering goods to consumers.

Also related to firm conditions, small trading volume also encourages firms to use third-party services, related to the requirements and provisions for exporting goods. Even though ROO provides benefits to firms, it also raises problems due to the difficulty in meeting ROO requirements in order to obtain a COO. This issue affects firms whose production involves imported products.

4.3. In-Depth Interview Findings

Interviews were conducted to strengthen the findings of the study by participating with firm representatives, including owners, general managers, and export and import staff representatives. Interviews were held following the respondents' participation in completing the research questionnaire.

As explained in the literature review, online systems is applied to access information, register, and obtain COO forms from the Certificate of Origin Issuing Agency. However, observed from the perspective of the Department of Industry and Trade and Customs, some firms complain about the system. Basically, the system is intended to simplify and accelerate service access. However, many obstacles are still faced by firms, including unstable

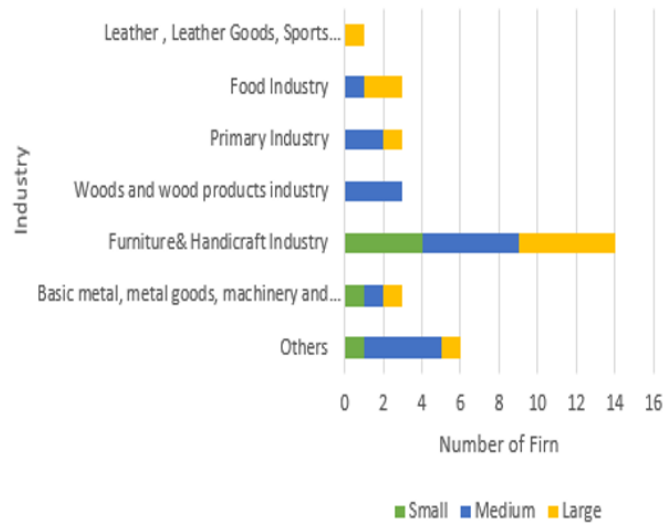


Figure 4.5: Utilization of FTA Based on Industry Type
Source: Author (2019)

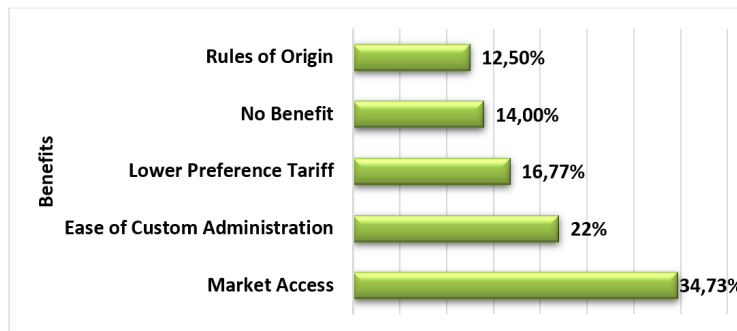


Figure 4.6: Benefits of Utilizing FTA Schemes
Source: Author (2019)

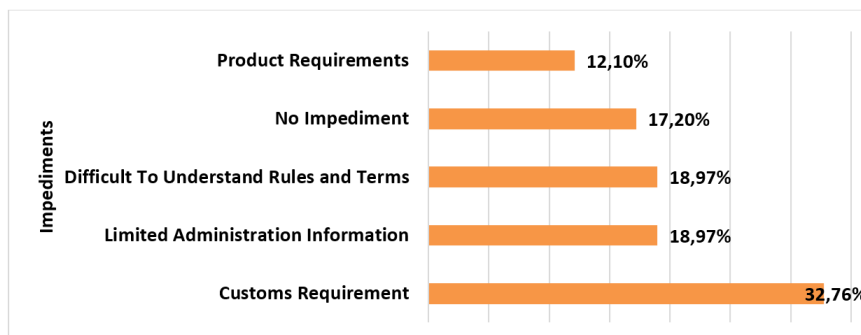


Figure 4.7: Impediments to Utilizing FTA Schemes
Source: Author (2019)

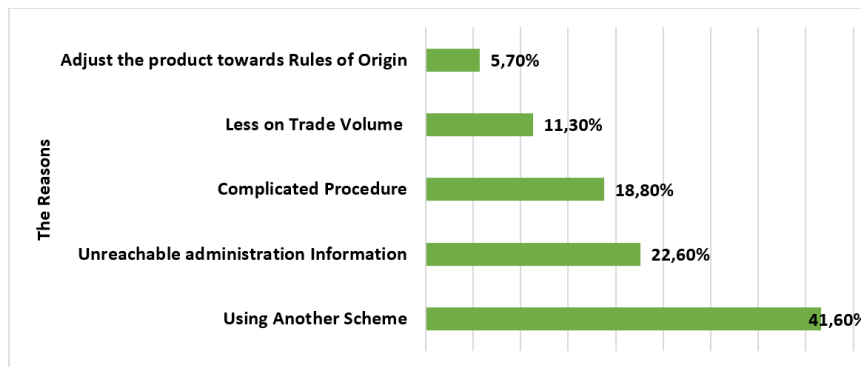


Figure 4.8: Reasons for Not Utilizing FTA Schemes

Source: Author (2019)

online systems, unavailability of forms, and a lack of guidance on using the system. As a consequence, some firms experience difficulties in completing the requirements. A lack of details and information regarding Harmonized Standard (HS) code alignment is another issue encountered.

Other issues related to the application of FTAs are late notifications and unavailability of the required forms. Profit-oriented firms and manufacturers providing services to consumers require a fast service, but they are often faced with technical problems related to the required documents. Timeliness is also necessary in the management and issuance of the required documents, considering the fact that in international trade, punctuality and consumer confidence are among the main priorities, especially for international consumers. Some firms complain about the insufficient service, complicated bureaucracy, the requirement of officials' signatures, and lateness of the service.

The involvement of two authority offices in the management also causes inefficiency and overlapping in the fulfillment of requirements. In addition, socialization and direction have to date has not been provided optimally. Along with the growth of new exporters and importers, some firms recommend that technical assistance should be provided by the government.

Not only in relation to administration and documents, the problems faced by firms are also related

to the certification of goods for certain products, such as in the wood and furniture industry. Prior to obtaining the COO document, this industry is required to hold timber legality certification, in the form of a timber legality certificate, commonly called an SLVK (*Surat Legalitas Verifikasi Kayu*), that must be updated every year. In order to obtain this certificate, an audit process must be conducted by a private party. Any firms that do not have this certificate cannot conduct export activity. The timber legality verification system charges a high fee and must be obtained every year. Firms engage in furniture and wood business recommend the establishment of a governmental certification body to reduce firm costs.

Firms engage in primary-need industries, for instance fruit, also experience problems in quarantine management. Even if the firm is in accordance with the standards, its application is rejected without clear explanation. As a consequence, it suffers losses. Apart from the impediments, some firms express their appreciation of the online-based COO system, allowing them to track and validate data. The respondents recommend specific guidance on accessing e-COO.

The firms that do not utilize the FTA scheme prefer to use third-party services. This is based on the consideration that third-party firms provide services in shipping, transportation and document assessment. Even though firms have to pay higher prices

for two services at the same time, they are willing considering their timeliness and practicality.

4.4. Discussion

As observed in the descriptive findings, the utilization of FTAs by firms in the Special Region of Yogyakarta is low, as indicated by the analysis results, showing that only 44% of firms uses the scheme.

Based on the descriptive findings, lower than optimal employment of FTAs is demonstrated by several firms of varying sizes and product types. To utilize the FTA scheme, firms have to adapt and adjust their products to meet the provisions, design a business plan, and hire more skillful workers to obtain and understand the related information on the FTA scheme. In addition, a lack of information and knowledge remain as impediments for firms to using FTAs, even though the government already provides assistance such as the FTA Centre and Official Website Indonesia National Single Window.

Moreover, to meet the provisions and regulations, firms are required to allocate more budget for production process. However, in reality, not many firms have sufficient budgets and are willing to adapt and adjust their business processes. In addition, as mentioned in the descriptive analysis, firms with a low volume of production mostly decide not to utilize the FTA scheme and chose other schemes instead, such as freight forwarding services and selling their products to third parties.

The rate of utilization also varies based on the type of commodity or product. This is in line with the different requirements and provisions for each product and commodity. Some firms decide not to use FTAs as they would have to adjust their products to meet the rules of origin (an additional mechanism to determine the origin of products in the employment of the FTA scheme). This finding is confirmed by the results from the interviews, showing that certain products have specific terms in order to utilize the FTA scheme, such as wood and wood products.

It is important to highlight that to utilize FTAs, firms need to comply with several steps and procedures prior to taking advantage of the facilities. Prolonged steps and procedure result in a low rate of utilization, as shown in Figure 4.6. The procedure includes administrative requirements that involve industry and trade provincial offices (Ministry of Trade) and customs offices (Ministry of Finance), the institutions that procure COOs and facilitate the FTA scheme. Firms are required to obtain the related information and follow the terms and rules to partake in FTAs. In fact, the technical procedure, including administrative requirements, rules and terms regarding the use of FTAs, has become one of the biggest impediments faced by firms (Figure 4.5). Moreover, the involvement of two government institutions is considered inefficient.

It takes a great deal of effort and cost for firms to utilize the FTA scheme, as shown in Figure 4.6. Customs are also an impediment, especially regarding the Export Permit Letter (*Pemberitahuan Ekspor Barang*), even though some respondents report that they enjoy the ease of customs administration (see Figure 4.5). At the same time, the information regarding the acquisition of COOs from the trade office is complicated and unattainable. Figure 4.10 explains the steps and procedures that firms need to comply with in the utilization of FTAs.

Accuracy and efficiency are essential in the business sector, but this is not supported by the prolonged and complicated procedures shown in Figure 4.7 and the previous explanation. Firms have to deal with these issues when utilizing FTAs. Based on the interviews, many firms complained about the system and the service provided by the authorities.

The respondents reveal that simple and clear provision is needed in business matters, in particular regarding the cost of production and the buyer. In relation to this issue, the government has attempted to simplify the procedure and improve the quality of the service by introducing an electronic registration system, as shown in Figure 4.9, as well as online single submission, known as the Indonesia National Single Window. However, the respondents find that

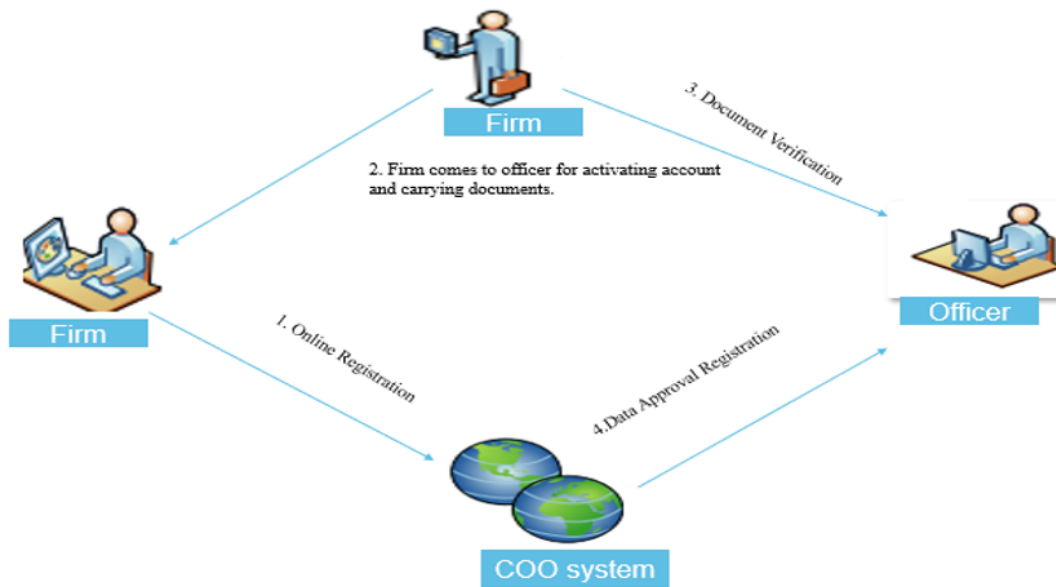


Figure 4.9: Registration Procedure to Activate Account with the Necessary Documents

Source: Ministry of Trade, Republic of Indonesia (Processed for this study)

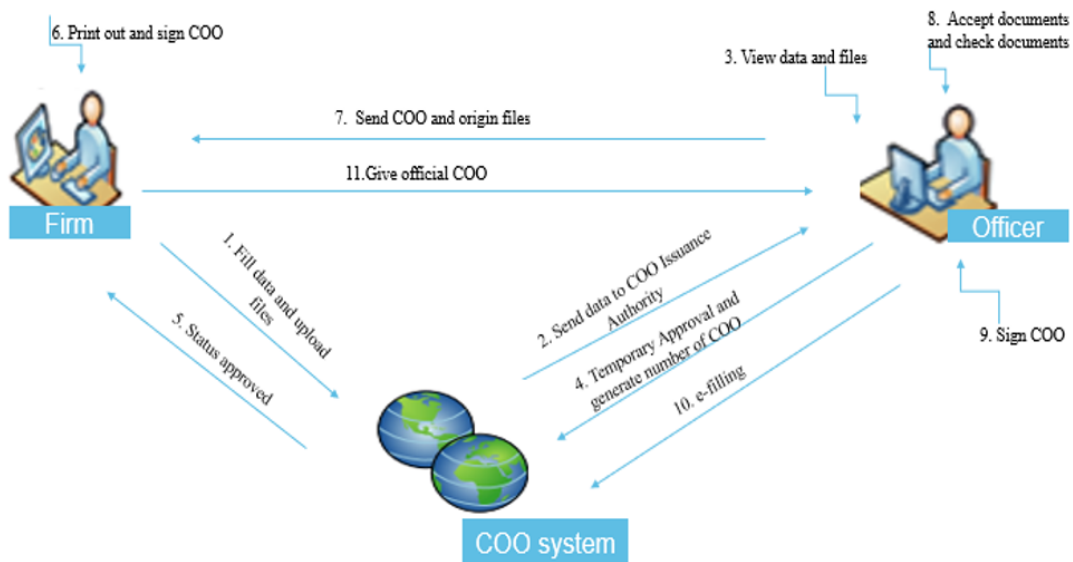


Figure 4.10: Procedures to Obtain a COO

Source: Ministry of Trade, Republic of Indonesia (Processed for this study)

the online system is frequently down. In addition, new or small-scale firms expected assistance from the government to help them enter the international market with the use of FTAs.

The respondents do not only complain about the limited information, but also the overlapping provision. Further assistance in utilizing the FTA scheme is also needed due to the double provision from different authorities. The lack of government support leads to lower employment of FTAs, meaning that more than half of the total research sample prefers to use another scheme. This is reasonable, as firms strive to reduce production costs and increase the efficiency of their business processes. Obviously, this finding is in contrast with the aim of FTAs, designed to encourage the international trade process.

On the other hand, even though the rate of the utilization of FTA remains relatively low, it does not mean that FTAs are not beneficial. Market access, ease of custom administration, and lower tariffs are the top three benefits experienced by firms using the scheme. Market access represents the possibility for the firms to sell their goods in foreign markets. Each FTA scheme consists of two or more countries, thus the possibility of entering the international market will be higher due to this privilege.

Another benefit is related to the preference tariffs. The firms are subject to lower tariffs, as mentioned by the respondents, stating that they have had higher margin benefits. Regarding the requirements of customs administration, even though it is previously mentioned that the firms face impediments in terms of goods adjustment to meet customs rules, some respondents also report the ease of the customs administration service and the availability of information.

5. Conclusion

This study has two objectives; (1) to observe the utilization of FTA schemes by firms, (2) to identify the

benefits and impediments encountered by firms in utilizing FTA schemes and to investigate the related issues on the utilization of FTA.

Novelty of this study is providing academic contribution to empirical studies regarding the utilization of FTA as studies of the utilization of FTA at micro level is limited and this study examines all of firms conducting international trading with all Indonesia's FTAs.

This study find that the utilization of FTA scheme at firm level in the Special Region of Yogyakarta is only 44% of the total 64 firms. The firms utilizing FTA scheme are reported to obtain several benefits, including the increase in market access (34.73%), ease of customs administration requirement (22%), lower tariff (16.7%), unbeneficial (14%), and rules of origin (12.50%).

On the other hand, the impediments encountered by firms in the utilization of FTA include customs requirement (32.76%), limited information (18.97%), difficulties in understanding the rules and terms (18.97%), no impediment experienced (17.20%), and the requirements for goods to meet the rules (12.1%). Additionally, 41.06% of respondents is using another scheme. These percentages are based on the respondents' responses.

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